GMS Flash Alert

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Czech Republic – Brexit: What's Happening from Personal Tax, Social Security Perspectives?

The end of 2020 will also bring the end of the transition period under the Agreement on the Withdrawal of the U.K. from the European Union (EU).[1] Thus, from 1 January 2021, U.K. nationals working in the Czech Republic may be affected by changes in the areas of personal income tax, as well as social security and health insurance.

WHY THIS MATTERS

During the transition period, between 1 February 2020 and 31 December 2020, the United Kingdom is being treated as if it were still part of the EU for the purposes of the Czech Income Tax Act (ITA) and for social security and health insurance purposes. Therefore, U.K. tax residents working in the Czech Republic have still been entitled to enjoy the same favourable tax treatment provided by the Czech Income Tax Act to EU tax residents; and for social security purposes, they were fully covered by the EU regulations on social security coordination.

However, from 1 January 2021, U.K. tax residents will no longer be considered as EU tax residents. For that reason, their Czech tax position will be slightly different; for instance, their right to reduce their tax base by claiming certain tax deductible items will be restricted.

From a social security perspective, if no agreement on the future relationship between the U.K. and the EU is entered into by the end of this year, then from 1 January 2021, the EU coordination regulations will **only apply** to those EU and U.K. citizens who were part of a certain cross-border relationship between the U.K. and the EU before 1 January 2021, and will only apply during the period of this relationship without any interruption or change. Employers that post their workers to the Czech Republic after 1 January 2021, should be aware that there is no bilateral social security agreement with the United Kingdom.

Details

Social Security

In the transition period after the U.K.'s withdrawal from the EU, the EU coordination regulations continue to apply when determining the social security and health insurance schemes the posted worker is subject to and the benefits distributed from such schemes.

If, as noted earlier, an agreement on the structure of future U.K.-EU relations is not achieved by the end of this year, the second part of the Withdrawal Agreement will be activated from 1 January 2021, stipulating, among other things, that the EU coordination regulations will **only apply** to those EU and U.K. citizens who were part of a certain cross-border relationship between the U.K. and the EU before 1 January 2021, and will apply during the period of this relationship so long as there is no interruption or change to the working arrangement.

The wording and scope of an agreement are currently being discussed. If the agreement is concluded before the year-end and enters into effect on 1 January 2021, the second part of the Withdrawal Agreement will not be activated and cross-border relations between the EU and the U.K. relating to social insurance are expected to be governed by the new agreement.

KPMG NOTE

It is anticipated that the European Commission will provide more detailed information on how individual member states and relevant social security institutions should interpret "without any interruption" and "without any change." The European Commission has recently declared how to proceed after the end of the transition period between the EU and U.K. as regards posted workers.[2] These statements may significantly restrict social security and health insurance premiums of posted workers after 1 January 2021.

However, Czech social security and health insurance institutions have indicated[3] that they are currently not planning to proceed in accordance with this statement; a similar approach is expected to be applied by other EU member states as well.

If in the Country before 1 January 2021, What Won't Change

For workers posted from the Czech Republic to the U.K. and vice versa before 1 January 2021, no changes to social security and health insurance shall occur in the new year. Over the posting period, all forms issued before the end of 2020 should remain valid, including A1 forms confirming the worker's participation in an insurance scheme of a particular state and all other relevant forms (e.g., S1 Forms confirming a worker's entitlement to full medical care at the state of residence).

KPMG NOTE

The situation of those to whom the above rules will no longer apply from 1 January 2021 must be assessed on an individual basis, taking into account both Czech and U.K. social insurance legislation. Since the Czech Republic does not currently have a bilateral social security agreement with the U.K., it may happen (similarly as before the accession of the Czech Republic to the EU) that employers will have to pay social security and health insurance for the posted workers in both states or that the posted workers will not be insured in either state. (However, the U.K. and the EU currently are making every effort to enter into a bilateral agreement at the EU level, which should be legally binding for all member states.)

Personal Income Tax

From the Czech personal income tax perspective, it is necessary to consider that from 1 January 2021, U.K. tax residents working in the Czech Republic will not be entitled to certain deductible items and tax credits, because the Czech Income Tax Act[4] grants these benefits only to EU or EEA residents.

U.K. tax residents with more than 90 percent of their worldwide income from sources in the Czech Republic will be able to claim in their Czech tax returns for 2021 only a basic tax credit for the taxpayer, or possibly a tax credit for students, similar to other tax residents outside the EU or EEA. Thus, they will no longer be able to reduce their tax base, for example, by donations for charitable purposes or to apply a tax credit for a dependent child or spouse.

The fact that the U.K. will no longer be an EU or EEA member state could also affect the calculation of the super-gross salary as currently valid under the Czech Income Tax Act. The super-gross salary represents the tax base – it is generally a sum of gross salary plus the employer's portion of social security contributions. The salary of the employees who are subject to compulsory British National Insurance contributions and are subject to taxation in the Czech Republic would no longer be increased by compulsory British National Insurance contributions. However, from 1 January 2021, it will be increased by so-called Czech hypothetical social security insurance as in the case of employees with employers outside the EU or EEA. However, as the abolition of the super-gross salary taxation is expected as of 1 January 2021,[5] employers may be able to avoid this issue (for prior coverage, see GMS *Flash Alert* 2020-408, 24 September 2020).

KPMG NOTE

Organisations with U.K. national employees who are working or will be assigned to work in the Czech Republic after 1 January 2021, should consult with their qualified global mobility advisers and/or tax service providers about potential changes in the organisation's Czech tax and social security exposure as a result of the end of the transition period.

FOOTNOTES:

1 Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, 2019/C 384 I/01, *OJ C* 384I, 12 November 2019, pp. 1-177. For related coverage of Brexit and the Withdrawal Agreement and immigration matters for U.K. nationals, see our other Brexit reports in GMS *Flash Alert*, at: https://home.kpmg/xx/en/home/insights/2015/09/flash-alert-brexit.html.

For more on the EU-U.K. Withdrawal Agreement, see: https://ec.europa.eu/info/european-union-and-united-kingdom-forging-new-partnership/eu-uk-withdrawal-agreement_en.

2 See point 2.3. of the provision-services-posting-workers_en.pdf (europa.eu).

3 Based on informal discussions between officials with the Health Insurance Bureau (*Kancelář zdravotního pojištění*) and Ministry of Labour and Social Affairs (*Ministerstvo práce a sociálních věcí*) and representatives of the KPMG International member firm in the Czech Republic.

4 Income Tax Act No. 586/1992 Coll.

5 See proposed amendment to the Income Tax Act approved by the Czech Parliament https://www.psp.cz/sqw/text/tiskt.sqw?o=8&ct=910&ct1=0&v=PZ&pn=2&pt=1 (in Czech).

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