New developments in tax legislation

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Content:

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The following newsletter provides a summary of the most important changes in tax and accounting practice which will take place as of 1 January 2012.

1. Remuneration to employees and company management

1.1. Remuneration to statutory bodies members

As there were certain interpretation ambiguities at the beginning of this year, there will be a change in the taxation of remuneration to executive directors and collective bodies members (boards of directors and supervisory boards). These changes will concern taxation and insurance and will result in the same treatment as in the case of remuneration to employees, i.e. the remuneration will be subject to the relevant social and health insurance and the costs of remuneration to collective bodies members will be a tax deductible cost of a company.

These changes are illustrated in the following table:

<table>
<tr><th></th><th></th><th>Health insurance</th><th>Social insurance: sickness insurance</th><th>Social insurance: pension insurance</th><th>Tax deductible cost of the company</th></tr>
<tr><td rowspan="3">2011</td><td>Executive director (“jednatel”)</td><td>Yes</td><td>No</td><td>Yes</td><td>Yes</td></tr>
<tr><td>Collective body member</td><td>Yes</td><td colspan="2">No</td><td>No</td></tr>
<tr><td>Employee</td><td>Yes</td><td colspan="2">Yes</td><td>Yes</td></tr>
<tr><td>2012</td><td>Executive director, collective body members as well as employees</td><td>Yes</td><td colspan="2">Yes</td><td>Yes</td></tr>
</table>

1.2. Further changes

For 2011 the threshold for the social and health insurance deductions amounts to CZK 1,781,280 (the insurance is not deducted from the annual income exceeding this threshold). In 2012 there will be a significant reduction in the social insurance threshold to CZK 1,206,576; the health insurance threshold will automatically increase to CZK 1,809,864.

Agreements for the performance of work (“dohoda o provedení práce”) may newly be entered into for 300 hours per year (until now the maximum amount of hours has been 150). In months in which the remuneration exceeds CZK 10,000 it will be necessary to pay the social and health insurance.

The annual discount for a cared for child will increase by CZK 1,800 to CZK 13,404; the main discount of the payer will again be CZK 24,840 which is the same amount like in 2010 (in 2011 it was lower by CZK 1,200 – the so-called “flood related one hundred crown bill“).

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2. Value added tax

2.1. Change in the reduced tax rate
From 1 January 2012 the reduced tax rate will change from 10 to 14%. The rate applies among others to construction and repairs to constructions of smaller housings. The rate valid until the end of 2011 will continue to apply to the accounting for deposits paid in 2011; for customers that are not entitled to a tax deduction it will be beneficial to pay most of this amount until the end of the year.

2.2. A regime of transferred tax duties in relation to construction works
A regime of the so-called transferred tax duty will apply to the provision of construction and assembly works where the customer is a tax payer. The duty to file and pay the taxes will not apply to the service provider but to the recipient of such service (this procedure is commonly known as a “reverse charge” and currently applies to services received from abroad).

The payer will pay to the supplier only the price of the service as such. If there is no entitlement to the deduction from the received service, the tax will be paid directly to the relevant financial office. If the payer is entitled to a deduction, the payer will state this in the same tax return and these two items will be set off. This will improve the cash-flow for the recipients of construction and assembly works with the entitlement to a deduction as it will no longer be necessary to wait for the return of the VAT from the relevant financial office.

2.3. Further changes in the VAT
Situations where the recipient of a performance becomes the guarantor for any unpaid tax from this performance, will also include cases where the recipient (VAT payer) send the whole or a part of the payment to an account held with a foreign bank. Therefore we recommend paying special attention to payments for received performances with the Czech

VAT that are to be sent to foreign entities or Czech entities with accounts abroad.
A missing tax identification number in a received document is today an obstacle in applying the right to the deduction – as of January it will also be possible to demonstrate this identificator in a different manner.

3. Creation of a specialised financial office

As part of the organisational changes in the Financial Administration of the Czech Republic, a Specialised Financial Office will come into existence as of 1 January 2012 which regardless of the territorial competency will administer the relevant tax agenda of selected entities. In addition to banks and insurance houses the Specialised Office will also administer entities with annual revenues over CZK 2 billion and entities that belong to their VAT group.

The Specialised Office should employ specialists trained with a focus on large businesses that regional financial offices could not administer properly.

4. Real estate tax for solidified surfaces

As we informed you earlier, 2012 will bring changes in the real estate tax rates for solidified surfaces (until now regarded as other area with a tax rate of CZK 0.20 per square metre). Areas solidified through construction will, depending on the purpose, be taxed with the rate of CZK 1 per square metre (in the case of the primary agricultural production, forest and water management), or with the rate of CZK 5 per square metre (in the case of industry, construction, transportation, energy and other entrepreneurial activities).

This change will need to be reflected in the real estate tax return which is usually filed by 31 January each year.

According to a statement of the Minister of Finance solidified surfaces should not include public communications (for example public car parks adjacent to shopping centres), landscaped land or solidified surfaces without a construction work being created (for example using gravel or laid panels).

5. Further tax developments

The Parliament approved a tax reform draft amendment which will bring significant changes in future in the administration of taxes and insurance and will introduce a single collection point for taxes, social and health insurance, changes in the super-gross salary concept, changes in the exemption of share sales by individuals, a different taxation of dividends for individuals and so on.

These new changes will certainlynot apply before 2013. It is also expected that the Senate will also have a say in the tax reform or that the parameters of the tax reform will change during the next year. We will keep you informed about any further changes.

We trust that you will find the legislative and interpretation changes favourable to a larger degree. We will be pleased to discuss any impacts of the above changes on to your company or how they may work in practice..

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