



Investment in the Czech Republic

KPMG IN THE CZECH REPUBLIC



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Contact us

KPMG Česká republika, s.r.o.

Pobřežní 1a

186 00 Praha 8

Czech Republic

Tel.: +420 222 123 111

Fax: +420 222 123 100

E-mail: kpmg@kpmg.cz

www.kpmg.cz

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Preface



Dear Reader,

Investment in the Czech Republic is one of a series of booklets published by KPMG in the Czech Republic to provide information to those interested in investing or doing business here.

This publication has been prepared to assist those considering investment or starting business in the Czech Republic. Its purpose is to provide some general guidelines on investment and business. The information contained in this booklet is of a general nature and should be used only as a guide for preliminary planning purposes. As the tax and legal systems in the Czech Republic are still comparatively new, certainty about the legal effects of transactions is sometimes therefore less easy to obtain than in more developed economies. In addition, Czech and EU legislation is frequently amended. Accordingly, the information should be viewed only as a general guide. Please consult KPMG in the Czech Republic for specific advice concerning your situation.

KPMG in the Czech Republic employs several hundred professionals who can offer you such assistance. They would be pleased to provide you with more detailed information on the matters discussed in this publication.

Every care has been taken to ensure that the information presented is correct and reflects the situation as of April 2010.

More detailed information can be obtained from KPMG in the Czech Republic (www.kpmg.cz) which provides audit, tax and advisory services for Czech and multinational companies, government entities and inward investors.

Thank you for taking the time to read this guide. All of us here at KPMG in the Czech Republic hope that you will find it helpful and informative.

František Dostál

Managing Partner of KPMG in the Czech Republic and Regional Chairman and Chief Executive Officer of KPMG in Central and Eastern Europe (CEE)

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Chapter 1

General information about the Czech Republic

Overall characteristics

The Czech Republic is a fully democratic country with a market economy. It enjoys political and economic stability.

The Czech Republic has been a member of the European Union since May 2004 and NATO since 1999. It is also a member of a number of other major international organisations, including the Organisation for Economic Co-operation and Development (OECD), the United Nations, International Monetary Fund, International Labour Organisation, the World Trade Organisation and the Council of Europe. It is believed that the Czech Republic will secure its long-term economic development by meeting all the duties and obligations arising from membership of these organisations.

The Czech Republic has a highly developed industrial base. Its main industries include manufacturing and engineering, automotive, electronics, construction, machinery, metallurgy, glass manufacture and beer production. However, the service sector has also become much more developed over the past 20 years, particularly in the country's main urban centres and their surrounding areas. Record inward investment flows, European dominance in television and computer production, a complete automotive supply chain, and a proven track record in supporting global ICT operations (Information and Communication Technologies) have helped sustain the Czech Republic's growth and underpinned its international competitiveness. In addition, the rapid growth in the number of Czech suppliers, a shift away from labour-cost-sensitive investments to high value-added activities and extensive R&D as integral parts of global networks have boosted growth. The Czech Republic ranked as the most successful transforming country among 125 surveyed countries around the world, according to the renowned Bertelsmann Transformation Index 2008.¹

¹ Bertelsmann Transformation Index 2008; at: http://www.bertelsmann-transformation-index.de/fileadmin/pdf/Anlagen_BTI_2008/BTI_2008_Brochure_EN.pdf

Economy and fiscal policy

Currently, the main principle of government economic policy is to find ways of minimising the impact of the global economic crisis on the Czech economy. A strong and detailed strategy can be put forward only after a parliamentary election to be held in May 2010.

In recent years, the Czech Republic has had one of the lowest levels of inflation in Central and Eastern Europe: the average rate was 1.9 percent in 2005, 2.5 percent in 2006 and 2.8 percent in 2007. In 2008, inflation rose sharply to 6.3 percent, but dropped to 1.0 percent in 2009.² Unemployment had been steadily declining, from 7.9 percent in 2005 to 7.1 percent in 2006, 5.3 percent in 2007 and 4.4 percent in 2008. However, since then the unemployment rate has risen again, to 6.7 percent in 2009, and reaching 9.8 percent at the end of January 2010.³

Table 1: Czech Republic: Key Macroeconomic Indicators – Real Economy Indicators⁴

Indicator		2005	2006	2007	2008	2009
GDP	CZK bn, current p.	2,983.9	3,222.4	3,535.5	3,689.0	3,627.2
GDP per capita	CZK/cap, curr. p.	291,561	313,868	342,494	353,701	345,727
GDP per capita in PPS⁵	PPS/capita, curr.p.	17,058	18,213	19,949	20,150	.
GDP	%, y/y, real terms	6.3	6.8	6.1	2.5	-4.2
Final consumption expenditure	%, y/y, real terms	2.6	3.9	3.7	2.8	1.2
Household consumption	%, y/y, real terms	2.5	5.0	4.8	3.6	-0.3
Gross capital formation expenditure	%, y/y, real terms	-0.8	9.6	9.4	-2.7	-18.1
Gross fixed capital formation expenditure	%, y/y, real terms	1.8	6.0	10.8	-1.5	-8.3
Exports of goods and services	%, y/y, real terms	11.6	15.8	15.0	6.0	-10.2

² Czech Statistical Office; at: http://www.czso.cz/csu/redakce.nsf/i/mira_inflace

³ Czech Statistical Office; at: <http://www.czso.cz/csu/csu.nsf/aktualniinformace>

⁴ Czech Republic: Key Macroeconomic Indicators. Sources: CZSO, Ministry of Labour and Social Affairs of the CR, CNB, Ministry of Finance of the CR and Czech Hydrometeorological Institute, April 2010; at: http://www.czso.cz/eng/redakce.nsf/i/macroeconomic_indicators

⁵ Purchasing Power Standards

Indicator		2005	2006	2007	2008	2009
Imports of goods and services	%, y/y, real terms	5.0	14.3	14.3	4.7	-10.2
Domestic effective demand	%, y/y, real terms	2.4	4.5	5.5	1.7	-1.3
GDP deflator	%, y/y	-0.3	1.1	3.4	1.8	2.7
Gross disposable income	CZK bn, current p.	2,837.1	3,044.2	3,268.1	3,394.2	3,382.1
Gross national saving	CZK bn, current p.	714.2	795.4	863.1	807.0	743.4
Gross national saving rate	%	25.2	26.1	26.4	23.8	22.0
Gross household saving rate	%	8.2	9.6	10.9	10.4	9.5
Aggregate labour productivity	%, y/y	5.2	4.9	3.3	0.8	-2.5
Unit labour costs	%, y/y	-1.2	0.7	2.8	5.3	1.3
Energy specific consumption	%, y/y	-5.6	-5.2	-5.9	-5.7	.
CO₂ emissions	%, y/y	-1.0	4.6	3.2	.	.
Industry – sales	%, y/y, real terms	8.1	11.6	10.8	0.5	-15.1
Construction – sales	%, y/y, real terms	3.7	13.9	7.4	-1.1	-1.0
Services – sales	%, y/y, real terms	3.0	4.6	8.8	0.3	-9.3
Agriculture – sales	%, y/y, real terms	8.0	-3.7	-6.6	-3.8	13.1
All first job holders	%, y/y	1.2	1.3	1.9	1.6	-1.4
ILO⁶ general unemployment rate	%, avg.	7.9	7.1	5.3	4.4	6.7
Long-term unemployment rate	%, avg.	4.2	3.9	2.8	2.1	2.0
Registered unemployment rate	%, avg.
Registered unemployment rate (new meth.)	%, avg.	8.97	8.13	6.62	5.45	7.98
Average gross nominal wages 1)		5.0	6.6	7.2	8.3	4.0

⁶ International Labour Organisation

Indicator		2005	2006	2007	2008	2009
Average real wages 1)		3.0	4.0	4.3	1.9	3.0
Average gross nominal wages 2)	%, y/y	5.1	6.4	7.3	8.4	3.5
Average real wages 2)	%, y/y	3.1	3.8	4.4	2.0	2.5
Avg. old-age pension/avg. wage	%	41.1	40.8	40.6	40.0	41.6
CPI⁷	%, y/y, avg.	1.9	2.5	2.8	6.3	1.0
CPI	%, y/y, Dec	2.2	1.7	5.4	3.6	1.0
PPI⁸ – industry	%, y/y, avg.	3.1	1.5	4.1	4.5	-3.1
PPI – construction work	%, y/y, avg.	3.0	2.9	4.1	4.5	1.2
PPI – market services	%, y/y, avg.	-0.4	3.4	1.6	3.8	1.5
PPI – agricultural producers	%, y/y, avg.	-9.4	1.1	16.5	8.8	-24.8
Prices of exports of goods	%, y/y, avg.	-1.5	-1.2	1.3	-4.6	0.2
Prices of imports of goods	%, y/y, avg.	-0.5	0.3	-1.0	-3.3	-3.5
Exchange rates	%, y/y, avg.	-1.0	-1.5	2.3	-1.3	3.8

Notes: y/y = year-on-year change; . = not available; * = end of period

The global financial market crisis and subsequent recession were reflected in the Czech economy by a marked slowdown in economic growth in 2008 and a drop in GDP in 2009. GDP was predicted to decrease by 4.0 percent in real terms in 2009 and slightly increase, by 1.3 percent, in 2010. In line with the expected easing of the global crisis, economic growth should speed up, reaching 3.8 percent in 2012. The general state of government finances during 2008 turned out to be slightly worse than expected, and the deterioration in public finances continued to accelerate significantly due to the strong impact of automatic stabilisers and the government stimulus package to support the economy. On the other hand, the Czech Republic has so far avoided the banking sector crisis.

⁷ Consumer Price Index

⁸ Producer Price Index

Table 2: Czech Republic: Key Macroeconomic Indicators – Monetary Indicators

Indicator		2005	2006	2007	2008	2009
CZK/EUR	avrg.	29.784	28.343	27.762	24.942	26.445
CZK/USD	avrg.	23.947	22.609	20.308	17.035	19.057
Nominal effective exchange rate	%, y/y	6.4	5.2	2.6	11.6	-4.2
Real effective exchange rate	%, y/y	5.0	2.5	2.8	9.6	-5.3
M2	%, y/y	8.0	9.9	13.2	6.6	4.0
Current account (CA) of balance of payments	CZK bn	-39.8	-77.2	-113.1	-22.9	-37.0
Financial account (FA) of balance of payments	CZK bn	154.8	92.4	125.8	59.0	95.1
Change in foreign exchange reserves	CZK bn	-92.9	-2.1	-15.7	-40.1	-60.6
CA/GDP	%	-1.3	-2.4	-3.2	-0.6	-1.0
FA/GDP	%	5.2	2.9	3.6	1.6	2.6
CNB international reserves (CNB IR)	CZK bn	726.7	656.6	631.0	716.0	764.3
CNB IR/GDP	%	24.4	20.4	17.8	19.4	21.1
Coverage of goods & services imports by CNB IR	month	4.2	3.4	2.9	3.2	4.0

Reducing general government deficits and improving the structural parameters of public finances will be the fiscal policy priorities for the coming period. Formulating and enforcing a medium-term fiscal strategy, however, is currently complicated by the forthcoming election. The main objectives of fiscal policy are therefore to ensure that the government deficit in 2010 is kept at 5.3 percent of GDP and gradual consolidation in subsequent years, so that the Czech Republic eliminates the excessive deficit by 2013.

Other government fiscal objectives are:

- limiting the negative impacts of economic development in 2009 on general government finances, through the adoption of measures to reduce the deficit;
- reducing the administrative burden and tax distortion by simplifying the tax system;
- increasing the effectiveness of government expenditure.

Table 3: Czech Republic: Key Macroeconomic Indicators – Fiscal Indicators

Indicator		2005	2006	2007	2008	2009
General government deficit (surplus)	CZK bn	-106.7	-84.9	-23.9	-100.3	-215.0
General government deficit (surplus)/GDP	%	-3.6	-2.6	-0.7	-2.7	-5.9
State budget balance	CZK bn	-56.3	-97.6	-66.4	-19.4	-192.4
State budget balance/GDP	%	-1.9	-3.0	-1.9	-0.5	-5.3
General government debt	CZK bn	885.4	948.3	1,023.8	1,104.9	1,282.3
General government debt/GDP	%	29.7	29.4	29.0	30.0	35.4
State debt	CZK bn	691.2	802.5	892.3	999.8	1 178.2
State debt/GDP	%	23.2	24.9	25.2	27.1	32.5

The Czech National Bank (CNB) will continue to apply monetary policy with the help of an inflation-targeting regime. The CNB is setting a new inflation target of 2 percent from 2010, following a target of 3 percent (expressed as annual growth in the consumer price index), which applied for four years.

The Czech Republic's *Updated Euro-Area Accession Strategy*, approved by the Czech Government in August 2007, did not set a new target date for joining the euro. The date will depend on the resolution of problematic areas as part of fundamental reform of public finances and strengthening the flexibility of the Czech economy.⁹

However, the strategy and objectives could change following the Czech parliamentary elections in May 2010.

Inflow of FDI

An open investment climate has been a key element of the Czech Republic's economic transition. The country has attracted a large amount of foreign direct investment (FDI) since 1990, making it the most successful transition country in terms of FDI per capita.

⁹ Ministry of Finance of the Czech Republic, Convergence Programme, January 2010; at: http://www.mfcr.cz/cps/rde/xchg/mfcr/xsl/conv_program_53226.html

Over 138,000 Czech firms in all sectors are now foreign-owned. According to the Czech National Bank, a total of EUR 69.6 billion worth of FDI has been recorded since 1993.

Table 4: Foreign Direct Investments in the Czech Republic 2005–2009 in thousands of EUR¹⁰

Year	Equity capital	Reinvested earnings	Other capital	Total
2005	6,188,482	2,624,027	561,030	9,373,539
2006	1,496,307	3,076,203	-217,597	4,354,913
2007	1,836,882	5,062,177	735,253	7,634,311
2008	787,997	1,652,459	1,974,972	4,415,427
2009	976,683	2,856,325	-1,868,522	1,964,486

The introduction of investment incentives in 1998 stimulated a huge inflow of FDI in greenfield projects. This was further strengthened after more subsidies and various forms of tax relief were introduced. The Czech Republic has consistently attracted a high rate of foreign direct investment per capita since 2000, confirming its appeal to foreign investors. CzechInvest, the investment and business development agency of the Czech Republic, has commissioned a number of surveys to evaluate the investment climate and satisfaction of foreign companies in the Czech Republic during 2009.¹¹ Some of the agency's main findings were:

- Research and development and business support services were the leading areas in terms of new investments. Manufacturing investments, dominant in the past, declined in 2009: only a fifth of new investors focused on manufacturing.
- Investors are choosing the Czech Republic as a location for increasingly demanding projects. Three out of every 10 investments involve software development.
- The second strongest sector was mechanical engineering, followed by electronics and electrical engineering.
- With the assistance of CzechInvest, 186 new investment projects, worth CZK 17 billion, were initiated.
- Investors announced the creation of nearly 6,000 new jobs.

¹⁰ Czech National Bank; at: http://www.cnb.cz/en/statistics/bop_stat/fdi/

¹¹ Investments in 2009: Smaller projects, demanding technologies (3 February 2010); at: <http://www.czechinvest.org/en/investments-in-2009-smaller-projects-demanding-technologies>

History and government

The Czech Republic was under communist control from 1948 until November 1989, when the Velvet Revolution, so called because of its non-violent nature, signalled the end of one-party rule. Since 1989 the Czech Republic has enjoyed a multi-party democratic political system. The first free elections in over four decades were held in June 1990, and the democratic parties emerged as victors. The new Federal Parliament subsequently confirmed President Václav Havel as head of state. In January 1998 he was re-elected for another five-year term. In January 2003, Václav Klaus was elected to this position (and re-elected again in January 2008), having been leader of the right-wing Civic Democratic Party, Minister of Finance and Prime Minister. Klaus is known as a liberal economist and a follower of the "Chicago School".

Until 1993, the Czech Republic was part of a federation with Slovakia, making up the former Czechoslovakia. Peaceful negotiations concerning division of the country led to an agreement that the state of Czechoslovakia would cease to exist on 1 January 1993.

Today, the state's official name is the Czech Republic, which is a parliamentary republic. Parliament is elected by universal suffrage, on the basis of a proportional representation system. The Lower House of Parliament, the Chamber of Deputies, has 200 members; the Upper House, the Senate, has 81. Political parties must pass a 5 percent threshold to win seats in Parliament.

The main political parties are the Czech Social Democratic Party (ČSSD); Civic Democratic Party (ODS); Communist Party of Bohemia and Moravia (KSČM); Christian and Democratic Union – Czechoslovak People's Party (KDU-ČSL); the Green Party (SZ); TOP 09 and Věci veřejné (Public Affairs).

Under the right-wing government of the ODS, KDU-ČSL and SZ, the Czech Republic held the rotating Presidency of the Council of the European Union for the first half of 2009. However, during this term the government collapsed and was replaced by a non-partisan caretaker government. Headed by Jan Fischer, it will lead the country through to the parliamentary elections scheduled for May 2010. Only then can a stable government with a sound programme be expected.

In 2010, elections to the Chamber of Deputies will be held (in May), and one third of the senators in the Upper House will be chosen.

Geography and climate

The Czech Republic is located in the geographical heart of Europe, close to most major Western European economic centres, and shares borders with Austria, Germany, Poland and Slovakia. It has an area of 78,864 square kilometres, or approximately 30,500 square miles. The Czech Republic consists of three distinct regions: Bohemia in the west, and Moravia and part of Silesia in the east. The topography ranges from agricultural plains to rolling forested hills, and mountains. The climate is continental, with hot but brief summers and frequently cold winters. Rainfall is generally moderate.

Population

The population of the Czech Republic is 10.5 million. The population density is approximately 130 per square kilometre, and the majority live in towns and cities. Prague, the capital, is by far the largest city with 1.3 million inhabitants. Other major cities include:

- Brno (371,000),
- Ostrava (308,000),
- Plzeň (169,000),
- Liberec (101,000),
- Olomouc (100,000),
- České Budějovice (95,000),
- Ústí nad Labem (95,000),
- Hradec Králové (95,000),
- Pardubice (90,000).

The Czech Republic has an economically active population of 5.7 million. One of the main attractions of its economy is the skilled and well-educated labour force, which is cheaper than that of Western economies.

Educational level

The Czech education system has a very strong position in terms of upper secondary education. The percentage of the adult population that has completed at least a high school education is among the highest of all of the OECD countries. Ninety-one percent

of the Czech population aged 25–64 has completed at least an upper secondary education, compared to an OECD average of 70 percent.¹²

The Czech Republic also has a very good position with regard to higher education. There has been an increase in the number of adults qualified at university level, as measured by educational attainment. The number of university students increased from 118,000 in 1990–91, to 274,192 in 2003–4 and to 323,765 in 2006–7. This is due not only to changes in the education system but also a spike in the number of students in the 18–26 age category.

According to the OECD, the Czech Republic has one of the highest percentages of science and engineering students in the world, with more than 70,000 studying technical subjects at technical or other universities. Nearly 8,000 university graduates in technical and scientific subjects enter the workforce every year, of which approximately 5,500 have primarily studied engineering or information technology.

Language skills

The official language of the Czech Republic is Czech. In addition, many people speak English, German or Russian.

English and German dominate foreign language education. The proportion of secondary school students studying English is 95 percent, which is high by European standards. Seventy-six percent of university students learn one foreign language, 20 percent learn two and 4 percent learn three or more foreign languages.

Living and working conditions

Schengen Area

In 2007, the Czech Republic entered the Schengen Area, a group of 25 European countries that have abolished all border controls between them. Any non-Schengen citizen with a valid Schengen visa is allowed to travel freely throughout the 25 countries.

¹² Education at a Glance 2009, OECD Indicators, at: <http://www.oecd.org/dataoecd/41/25/43636332.pdf>

Visas and work permits

Citizens of the EU, European Economic Area (EEA: Iceland, Norway, Liechtenstein) and Switzerland may stay temporarily in the Czech Republic without any permit, on the basis of a passport or an identity card. Under the Act on Aliens, such citizens need only notify the police should their expected period of stay in the Czech Republic exceed three months, i.e. the relevant Foreign Police Inspectorate according to the place of their stay in the Czech Republic, within three months after entering the Czech Republic.

A foreign national who is not an EU, EEA or Swiss citizen must obtain an appropriate visa to enter the Czech Republic. However, citizens of some third countries (e.g. USA, Australia and Japan), are exempt from visa requirements during short stays of up to 90 days, unless the purpose of their stay is employment. For stays longer than 90 days, long-term visas must be applied for. If a visa is required, it must usually be obtained before arrival, by applying to a Czech embassy or consulate.

The law defines two types of long-term stay for foreign nationals in the Czech Republic:

- long-term residence, which may be applied for when staying in the country based on a visa for a stay longer than 90 days, if the applicant intends to reside temporarily in the Czech Republic for more than one year based on the same purpose of stay. The application for a long-term residence permit is filed with the Foreign Police Inspectorate having jurisdiction over the applicant's place of residence.
- permanent residence, which may be applied for after five years of continuous stay in the Czech Republic by any foreign national. Applications must be filed with the regional offices of the Department for Asylum and Migration Policy of the Ministry of the Interior.

Whereas EU, EEA or Swiss citizens may work in the Czech Republic without a permit, other foreign employees generally require the following documents if they wish to work in the Czech Republic:

- a work permit issued by the local labour office,
- a visa for the purpose of employment or a residence permit.

More information on how to apply for various types of visas and residence permits, including lists of documents to be enclosed with the applications can be found at:

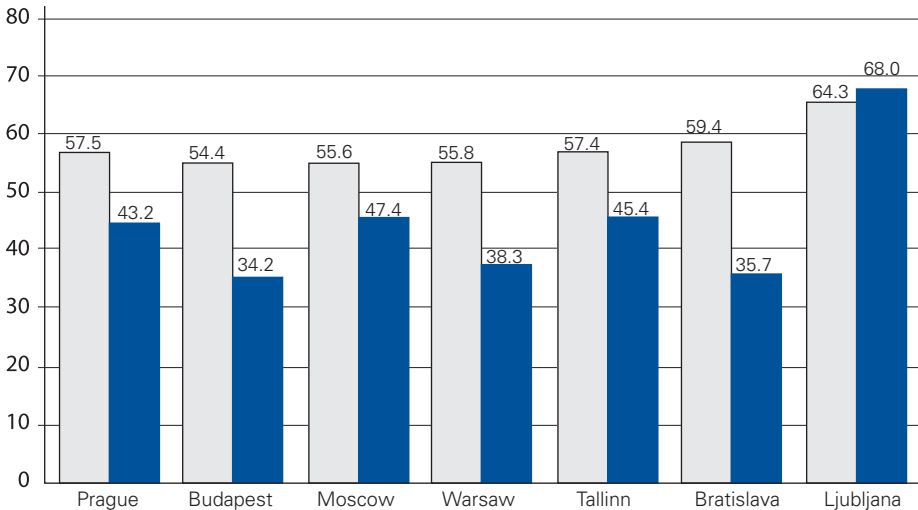
www.mzv.cz/jnp/en/information_for_alien/index.html.

Cost of living

Although in most respects the Czech Republic has rapidly approached Western living standards, costs remain substantially lower than in Western Europe. According to the Union Bank of Switzerland¹³, average prices of goods and services (excluding rent) in Prague are 57.5 percent of those in New York. Domestic purchasing power in Prague is 43.2 percent of that of New York.

With regard to prices in Prague, the cost of a weighted shopping basket geared to Western European consumer habits and containing 122 goods and services, including rents in Prague, is also relatively low. The price index is 43.6 points (including rent) benchmarked against New York (100). Wage levels (effective hourly wages for 14 professions, weighted according to distribution, after deducting tax and social security contributions) in Prague are 26.9 points benchmarked against New York (100).

Figure 1: Average prices of goods and services and domestic purchasing power in 2009 (New York = 100)¹⁴



^{13,14} Prices and Earnings. A comparison of purchasing power around the globe (2009 edition), UBS; at: http://www.ubs.com/1/e/wealthmanagement/wealth_management_research.html

Residential accommodation and office space

Prague and all of the larger cities offer a wide range of rented furnished and unfurnished housing for expatriates and their families, ranging from centrally-located apartments to spacious villas in leafy suburbs. Many estate agencies offer relocation services for a charge of one to two months' rent. The sale and rental prices of residential premises can vary widely, depending on the city, location, size and quality. The purchase price of a three-room apartment in Prague ranges from USD 700 to 4,000 per square metre, in Brno from USD 300 to 1,100 per square metre, and in Ostrava from USD 200 to 900 per square metre. The average monthly rent for a standard three-room apartment is USD 660 in Prague, USD 390 in Brno and USD 350 in Ostrava. Prices in other cities are lower than those in Prague or Brno.¹⁵

The highest office occupancy costs in the country are in the centre of Prague – approximately EUR 404 per square metre per year.¹⁶

Transport

Compared to that of Western Europe, public transport in the Czech Republic is comprehensive, efficient and reasonably priced. All large towns have excellent local networks.

With regard to driving, EU citizens can use a driving licence issued in their home countries, for driving in the Czech Republic. Citizens from non-EU countries with a residence permit or a long-term visa for a stay longer than one year must obtain a Czech driving licence: a licence from their home countries is not valid. This can be done by presenting the original licence at the municipal authority with jurisdiction over the applicant's place of residence in the Czech Republic.

The Czech Republic has 55,654 kilometres of roads in operation, of which 691 kilometres are motorways. The road network includes international routes (including motorways) indicated by the letter "E", in line with the European Agreement on Main International Traffic Arteries, with a length of more than 3,000km.

¹⁵ CzechInvest; at: <http://www.CzechInvest.org/en/life-in-the-czech-republic>

¹⁶ Office Space Across the World 2010, Cushman & Wakefield; at: <http://www.cushmanwake.com/cwglobal/jsp/kcReportDetail.jsp?Country=GLOBAL&Language=EN&catId=100003&pId=c27900002p>

With a density of 0.70km of roads and motorways per square kilometre, the Czech Republic is one of the leading countries in Europe in terms of road infrastructure.¹⁷

Motorways and major roads carry the heaviest traffic volumes and connect the most important administrative, financial and recreational centres. The centre of the road network is Prague. The main highways run from the capital to Brno (then on to Slovakia or through Ostrava to Poland), Ústí nad Labem (on to Central and Northern Germany), Plzeň (on to Southern Germany) and Hradec Králové (on to Poland).

Medical care

The Czech healthcare system is based on the European system, financed predominantly by public means. Czech doctors provide the same standard of care as their counterparts in Western European countries. Prague and other cities enjoy a wide range of public and private hospitals and clinics.

The number of private hospitals and clinics is growing, including, among others, Top Moravia Health Brno (www.tmhklinika.cz), Doctor Health Centre Prague (www.doctor-prague.cz), GHC Clinic Prague and Brno (www.ghc.cz) and Canadian Medical Care Prague (www.cmcpraha.cz/en).

Education

A number of international schools have been set up in Prague, and children can be educated in English, German, French, Japanese or Spanish. The Czech Republic offers a significant and growing choice of foreign-language education programmes, ranging from kindergartens to master of business administration (MBA) courses.

The Czech Republic has over 40 universities, both public and private, offering courses in foreign languages (primarily in English), and MBA courses are currently being offered by more than 20 institutions. Tuition fees usually must be paid, but exceptions may be made (e.g. a language course as part of a scholarship). The Institute for Language and Preparatory Studies (www.ujop.cuni.cz) offers Czech language courses for foreigners, and preparation for university studies.

¹⁷ The Road and Motorway Directorate of the Czech Republic Roads and Motorways in the Czech Republic 2009; at: [http://www.rsd.cz/rsd/rsd.nsf/0/80345976071FCBACC12575CF004E133E/\\$file/RSD2009en.pdf](http://www.rsd.cz/rsd/rsd.nsf/0/80345976071FCBACC12575CF004E133E/$file/RSD2009en.pdf)

Foreign students can receive a scholarship under bilateral international agreements on co-operation in the area of education (offered by the Ministry of Education, Youth and Sports) or through Foreign Development Aid (offered by the Czech Government). Information about these scholarships is available at Czech embassies and consulates. A number of higher education institutions offer student mobility programmes under bilateral university agreements, and grant scholarships to students with excellent examination results or those experiencing financial difficulties. European students can take advantage of a number of exchange programmes (e.g. Erasmus, EEA/Norway Financial Mechanisms, Aktion, Ceepus). The Erasmus Mundus programme also offers scholarships to non-European students for places on selected degree courses.

Culture and the arts

Prague and many cities in the Czech Republic are famous for their architectural heritage (see, e.g., the UNESCO World Heritage List at www.unesco.org, which includes 12 sites in the Czech Republic).

Thanks to its rich cultural tradition, the country also has numerous museums, theatres, cinemas, galleries and concert halls. There is a wide choice of cultural events, embracing all forms of music and a long theatrical tradition. Each May, Prague hosts the Prague Spring, a music festival that attracts top artists from all over the world and is a good example of the Czech Republic's musical tradition.

Sport – golf

The Czech Republic offers a wealth of sporting opportunities. The most popular sports are ice hockey, football (soccer), basketball, tennis, volleyball, swimming and table tennis, for which there are many clubs and venues throughout the country.

The Czech Republic has a high number of golf courses per capita and a long golfing history, dating back to the early twentieth century (1904), when golf became popular thanks to state-of-the-art golf courses built near the West Bohemian spa resorts. Today, there are 142 clubs and 124 courses. For more information, see the website of the Czech Golf Federation (www.cgf.cz).

Other leisure activities

Most embassies run clubs, groups and even bars for expatriates. There are many international cultural institutes in Prague and other cities, e.g. the British Council in Prague and Brno (www.britishcouncil.org/czechrepublic.htm), the Goethe-Institut Prag (www.goethe.de/ins/cz/prag), the American Culture and Trade Center Prague, Österreichisches Kulturinstitut Prag, L'Institut Français de Prague (www.ifp.cz), the Japanese Information and Culture Centre Prague and the Istituto Italiano di Cultura Praga (www.iicpraga.esteri.it/IIC_Praga).

The International Women's Association of Prague (www.iwa-prague.com) is a highly popular club for Czech and foreign women that organises all kinds of classes, international activities, charity and social events and children's groups.

Further information about life in the Czech Republic can be found on the www.expats.cz website.

Restaurants

Restaurants in the Czech Republic cater to a wide range of tastes. In larger cities, all kinds of international cuisine are available, alongside the country's famous Czech pubs, which offer traditional Czech food and famous Czech beer brands. Larger cities, particularly Prague, have an extensive number of pubs and restaurants aimed at foreigners, ranging from Irish pubs to Indian restaurants. More information can be found in on-line restaurant guides, e.g. www.grand-restaurant.cz.

Prague was, until recently, one of the cheapest places to eat out, but the strong Czech crown and large numbers of tourists mean that in the city centre prices are now approaching those of Western Europe.

Shopping

The retail sector in Prague and all larger cities has undergone a revolution in the past decade, and there are many large shopping centres now located within and around the cities. Local concepts of shopping and customer service are now comparable to those of Western European countries, and major international retail chains (e.g. Tesco, Billa, Makro, IKEA, OBI, Bauhaus and others) as well as boutique stores (e.g. Zara,

C&A, Marks & Spencer, Promod, H&M, Next, Max Mara and others) are present in the Czech market.

The Czech currency is the Czech crown (CZK or Kč) and is fully convertible. ATMs are widely available. Opening hours vary depending on the type of business and location. Most offices and businesses are closed all day on Sunday. Some major stores are open on Sunday, and in the larger cities an increasing number of hypermarkets are open around the clock. General opening hours are as follows:

	Monday to Friday	Saturday	Sunday
Government offices	8:00–16:30	closed	closed
Banks	8:00–17:30	closed	closed
Major stores	8:00–18:00	9:00–20:00	9:00–20:00

Chapter 2

Investment incentives in the Czech Republic

The Czech Republic offers incentives for investment in manufacturing industry. They are provided in the form of tax relief and subsidies in all regions excluding Prague. As incentives are considered state aid, they are granted in full compliance with EU state aid regulations.

Investment incentives for the manufacturing sector

Overview

Incentives are provided under Act No. 72/2000 Coll., on Investment Incentives (the “Act on Investment Incentives”), and consist of:

- income tax relief for up to five years for establishing a new manufacturing plant or expanding an existing plant;
- employment subsidies in the form of grants for job creation and training (available only in regions with high unemployment rates);
- purchase of land at a discounted price.

There is a general expectation that the law will be changed after the 2010 general election, reflecting both the current economic situation and the priorities of the new government.

General conditions

The general conditions for receiving incentives are as follows:

1. The investor must establish a new manufacturing plant, or expand an existing plant. Most manufacturing activities qualify, although the following are not regarded as manufacturing activities and are explicitly excluded:

- mineral extraction,
 - electric power generation and distribution,
 - gas distribution,
 - water treatment and distribution,
 - construction,
 - motor vehicle repairs,
 - trading in goods and services.
2. Acquisition of machinery classified under Chapters 84, 85 and 90 of the Customs Tariff. The machinery must be new (not yet used) and manufactured no earlier than two years before the acquisition. In addition, it must be purchased at market price. Production machinery must make up at least 60 percent of the total value of investment in tangible and intangible assets.
 3. The project must comply with Czech environmental standards.
 4. The minimum amount that can be invested in tangible and intangible assets is usually CZK 100 million, of which at least CZK 50 million must be financed from equity. The minimum of CZK 100 million is, however, reduced to CZK 60 million or CZK 50 million if the investment is in a district with an unemployment rate at least 25 or 50 percent above the national average, respectively, and the financing requirement is adjusted accordingly. The assets included in the investment project must be acquired through purchase: assets subject to finance leases, for example, cannot be included in the above investment amounts.
 5. The conditions must be met within three years from the date on which incentives are formally granted. This period is subject to a two-year extension in some cases, based upon a written application. An extension may be granted by the Ministry of Industry and Trade in justified cases only, e.g. unexpected delays beyond the control of the investor.
 6. The acquisition of assets for the project, including construction work, cannot start before the application for incentives (Statement of Intent) is submitted to CzechInvest and the applicant receives confirmation of project eligibility from it.

7. The investment for which state aid was claimed (at least the minimum investment amount under point 5) must be maintained for at least five years or the actual period for which it was claimed, whichever is longer. The number of new jobs created must be maintained for at least five years from the first disbursement of the job creation grant.

Income tax relief

Calculation

Calculation of the tax relief that can be claimed is the only significant area where the treatment of a new company (plant) differs from that of an expanded facility.

For a new company, the taxpayer is entitled to full tax relief, excluding tax on net interest income.

For an expanded plant, the amount eligible for tax relief is the difference between the tax relief that would be available for a new company and the higher of the tax liabilities in the two years immediately preceding the first year in which relief can be claimed. The latter figure is adjusted with reference to industrial inflation and the current tax rate.

This formula can be seen as a rough attempt to restrict the amount eligible for tax relief to the additional profits resulting from the expansion.

In both cases, relief is available only in relation to the profits shown in the original tax return submitted. If a higher tax liability is subsequently assessed, the additional tax must be paid.

Commencement and duration

The first period in which tax relief is available is that in which the incentive conditions are met, but no later than three years from the date when the incentives are granted. This is generally interpreted as meaning that the investor may choose to postpone claiming tax relief until the end of this three-year period.

The tax relief may be claimed for five consecutive tax periods, or until the maximum amount of state aid is reached, whichever occurs first.

Conditions

To be able to claim tax relief, a taxpayer must meet both the general conditions set out above and the special conditions in the Act on Income Tax:

1. The taxpayer must claim tax deductions as follows:
 - all depreciation, although the method of depreciation (i.e. straight-line, accelerated or extraordinary) is at the taxpayer's discretion;
 - tax-deductible adjustments to receivables must be created;
 - tax losses carried forward must be claimed in the first taxable period in which a profit is realised.
2. Except for immovable assets and certain assets acquired from bankrupt taxpayers, the taxpayer must be the "first owner" of tangible fixed assets acquired for a project in the Czech Republic.
3. During the period when tax relief is claimed, the taxpayer entity must not be dissolved or subject to bankruptcy proceedings, nor may another entity be merged with the taxpayer.
4. The taxpayer must not inflate profits through transactions on a non-arm's length basis with related parties, or by transfers of the assets of such parties, which would result in their taxable income being reduced.
5. The taxpayer must acquire and record in its fixed assets register tangible and intangible fixed assets in at least the amounts stated in the Act on Income Tax (see "General conditions" above).

Sanctions

If the taxpayer fails to observe the general conditions in the Act on Investment Incentives or the special conditions in the Act on Income Tax (except for the requirement to claim all available deductions), the right to claim tax relief will cease to exist, and any relief already received must be refunded. Penalties for any late tax payments must also be paid. If a taxpayer fails to claim the deductions mentioned above, the tax relief is reduced, resulting in additional tax, depending on the amount

of the deduction. This amount must then be paid to the relevant authorities, together with the appropriate penalties.

Job creation

Cash grants will be provided to an employer creating new jobs in a region where unemployment was more than 50 percent above the national average in the last two six-month periods. Employees from both the Czech Republic and other EU member states can be taken into account in this calculation. The financial support amounts to CZK 50,000 per new job. If 1,000 or more new jobs are created, the unemployment rate in neighbouring regions will also be considered. Investments in regions not seriously affected by unemployment will not qualify for this type of financial support.

Training and retraining of employees

Cash grants for training and retraining employees will be provided to an employer in the form of a partial reimbursement of the costs incurred. The subsidy covers 35 percent of the eligible costs of training and retraining of employees. Again, investments in regions not seriously affected by unemployment will not qualify for this type of financial support.

Purchase of construction sites

The actual provision of this incentive depends on negotiation with the owner of the land (state, region or municipality). The difference between market price and the actual purchase price is treated as an incentive.

Permissible level of state aid

The combined total of tax relief, job creation grants, and benefits from a discounted purchase of land must not exceed the maximum permissible level of state aid.

The maximum permissible level of state aid will be calculated for individual investment projects by the Ministry of Industry and Trade. The amount is based on the rules set by the European Union and varies according to the individual regions of the Czech Republic.

Generally, the maximum amount of state aid cannot exceed 40 percent of eligible costs. Such expenses generally comprise investment in land, buildings, machinery and equipment, and specified intangible assets. In accordance with the "Regional Map

for the 2007–2013 Period”, the permissible level of state aid is lower in certain regions (e.g. Southwest Region: 36 percent). In some cases (such as investments exceeding EUR 50 million, or production that does not come under the category of preferred manufacturing industries, as determined by a government resolution. The categories are defined as, for example, production of electronics, cars, chemicals, etc.), this maximum may be further reduced. For medium-sized enterprises, the maximum level of state aid can be increased by 10 percent, for small enterprises by 20 percent.

In the case of tax relief, the percentage is applied on an annual basis with reference to the amount invested at the end of each taxable period. It is therefore possible that in some circumstances, e.g. if profits are realised before the full investment has been made, the tax liability in a given period will exceed the amount of state aid available for such a period.

Application for investment incentives

The process of obtaining incentives entails:

- submission of an initial application by the person intending to make the investment – for a greenfield investment this would be the shareholder(s) of the Czech entity to be established;
- consideration of the application by the relevant government bodies;
- following approval, an offer of incentives is made;
- a formal application for the incentives by the person actually claiming them – this may be a person other than the investor, e.g. a Czech subsidiary of a foreign investor set up after the incentives are offered;
- final consideration and approval.

Careful attention should be paid to a number of significant issues arising from this process.

From the timing perspective, it should be borne in mind that incentives are available only for future investments, so it is imperative that the application is submitted before the project commences. This restriction has an impact not only on actual construction work or machinery purchase, but also some other steps, e.g. the issue of binding orders for machinery.

EU structural funds

The Czech Republic (excluding Prague)

Businesses set up in the Czech Republic can also obtain support from EU structural funds under several Operational Programmes. The most important programmes for businesses are:

- the Operational Programme Enterprise and Innovation,
- the Operational Programme Human Resources and Employment.

Although the majority of the programmes are focused on small and medium-sized enterprises, several programmes are aimed at large enterprises.

All Operational Programmes will run from 2007 to 2013. This, however, does not mean that they will offer similar conditions and subsidies over the whole period. A set of different subsidies is available under each programme, and conditions change periodically. In addition, new applications are accepted only in certain periods announced in advance. The availability of subsidies must be checked in the early stages of project preparation so that the timing of the application and detailed conditions can be considered.

Subsidies granted under EU Structural Funds are generally subject to the same state aid rules and limits as investment incentives.

Below are listed some of the subsidy programmes applicable to large multinational companies. However, subsidy programmes for other projects may also be relevant, e.g. infrastructure, environment, education, etc. It is therefore important to review the availability of subsidies for a particular project.

Operational Programme Enterprise and Innovation

Under the Operational Programme Enterprise and Innovation, funding is available for business projects in the manufacturing sector and related services. Projects implemented in the Czech Republic, excluding Prague, are eligible.

For the 2007–2013 period, the Ministry of Industry and Trade is introducing a total of 15 state aid programmes, including one programme for R&D (TIP), including:

- ICT AND STRATEGIC SERVICES

- The programme supports investment projects focusing on the creation of new IS/ICT solutions and applications, and the establishment and expansion of shared services and repair centres.
- The minimum investment amount is CZK 3 million.
- The minimum number of new jobs that can be created is 10/25/35.
- The maximum subsidy amount is CZK 80 million.
- The level of state aid is 36–40 percent of eligible costs.
- Eligible costs are defined as either the costs of fixed assets, or the gross wages of employees, and the lease of land and buildings.
- The obligation to maintain the investment or retain jobs for at least five years.

- POTENTIAL

- The programme supports the establishment or expansion of R&D and technology and innovation centres, whose results are subsequently used in production.
- The minimum investment amount (large enterprises) is CZK 10 million.
- The maximum subsidy is CZK 100 million.
- 36–40 percent of eligible costs can be covered by state aid.
- The costs of tangible assets (buildings, land and machinery) and intangible assets (licences and acquisition of know-how) are eligible.
- A minimum level of investment must be maintained for at least five years from the project completion date.

- INNOVATIONS

- The programme supports projects that implement product or process innovation.
- Projects must apply the results of R&D.
- The minimum investment value is not defined.
- The maximum subsidy amount is CZK 75 million (in some cases up to CZK 150 million).
- The level of state aid is 36–40 percent of eligible costs.
- The costs of tangible fixed assets (including technical improvement) and intangible fixed assets are eligible.

- TRAINING CENTRES PROGRAMME

- Support for construction, renovation, or equipping of training centres or rooms.
- The maximum subsidy amount is CZK 100 million.
- The level of state aid is 36–40 percent of eligible costs.
- The costs of fixed assets related to training centres are eligible.
- The training centre must be more than 50 percent used for training employees operating in a qualifying industry or the service sector.
- The condition of at least 30 percent use of a training centre for three years from project completion.

- REAL ESTATE PROGRAMME

- The programme supports projects establishing industrial zones, renovation of buildings in the manufacturing sector (CZ-NACE 10-33), and strategic services and technology centres.
- The maximum subsidy amount is
 - reconstruction project: CZK 500 million,
 - preparation of project documentation: CZK 50 million.
- The level of state aid is 36–40 percent of eligible costs.
- Eligible costs covered include project documentation (may form a separate project), purchase price of the building, site preparation, construction and reconstruction costs, demolition of disused buildings, utilities and roads, etc.

- TIP (TECHNOLOGY INNOVATION) PROGRAMME – FOR R&D

- The programme supports R&D projects (tender process).
- The maximum subsidy amount is not defined (proposed by the applicant and subsequently assessed).
- The maximum subsidy amount is 50 percent of the eligible costs for applied research projects, and 25 percent of eligible costs for experimental development.
- Eligible costs are defined as operating costs (wages, overheads, etc.), acquisition of intangible assets (up to 20 percent of total eligible costs).
- At least 50 percent of the project must be implemented by employees of the applicant.
- The maximum implementation period is four years.
- The results of a R&D project must be applied primarily in the Czech Republic.

Operational Programme Human Resources and Employment

Under the Operational Programme Human Resources and Employment, small and medium-sized companies and large firms can obtain support for employee training. The Ministry of Industry and Trade has introduced the EDUCA programme for the 2007–2013 period.

- EDUCA

- The programme supports specific training (a minimum of 80 percent of training activities) and general training (up to 20 percent of training activities) in manufacturing, electric power generation and distribution, gas distribution, water treatment and distribution, construction, warehousing, IT activities, etc.
- The maximum subsidy amount is approximately CZK 8 million.
- The level of state aid is 25–45 percent (small enterprises) of eligible training costs.

Prague

Businesses established in Prague can also obtain support from EU structural funds under the following programmes:

- OPERATIONAL PROGRAMME PRAGUE – ADAPTABILITY

- The programme focuses on increasing the competitiveness of Prague by strengthening the adaptability and effectiveness of human resources, and increased access to employment for all.

- OPERATIONAL PROGRAMME PRAGUE – COMPETITIVENESS

- The programme focuses on the availability of transport services and information and communication technology, improving the quality of the environment, and on promoting innovation and a knowledge-based economy.

Chapter 3

Commercial Law

General

The basic provisions governing business obligations and other specific aspects of doing business in the Czech Republic, e.g. property leases and liens or mortgages on property, are set out in the Civil Code and the Commercial Code.

The Commercial Code addresses the main aspects of Czech corporate law. It also contains detailed provisions governing contractual relationships in business transactions (e.g. purchase contracts, contracts for work, contracts for the sale of a business, lease contracts or credit contracts). Insolvency is governed by the Insolvency Act.

Types of business entity

The Commercial Code recognises the following types of business entity:

- joint-stock companies,
- limited liability companies,
- general partnerships,
- limited partnerships,
- co-operatives,
- Societas Europea (European companies),
- European Economic Interest Grouping (EEIG).

In addition, foreign persons may establish a branch in the Czech Republic. A branch is not a legal entity but must be recorded in the Commercial Register.

The Commercial Code regulates the status and activities of entrepreneurs and applies to both legal entities and individuals. An entrepreneur is:

- a person recorded in the Commercial Register, or
- a person engaged in business activity on the basis of a trade certificate (*živnostenský list* or *koncesní listina*), or
- a person engaged in business activity on the basis of an authorisation issued under a special legal regulation (e.g. attorneys, doctors, auditors or tax advisers), or
- a natural person engaged in agricultural activities and recorded in an appropriate register.

A Czech legal person is an entity that has its registered office in the Czech Republic.

Foreign persons are defined as persons (natural or legal) domiciled abroad or having their registered office outside the Czech Republic.

A foreign person's authorisation to carry out business in the Czech Republic takes effect on the date when it is recorded in the Commercial Register. The business activity must be specified in the entry. This rule does not apply to citizens of member states of the European Union, the European Economic Area or Switzerland, their family members who have Czech residence permits, citizens of other states with long-term residence in the EU and their family members with long-term residence permits.

A foreign person may participate in the establishment of a Czech legal entity or become a partner or member of an existing Czech legal entity. A foreign person may also be the sole founder of a Czech legal entity, provided that Czech law permits a company to have a sole founder or single shareholder.

The main characteristics of the various legal entities are as follows:

Joint-stock company

(akciová společnost – “a. s.”)

- The company exists independently of its shareholders, who are not liable for the debts and obligations of the company.
- The amount of registered capital and the extent to which it is paid up, the number, class, type and nominal value of shares, any restrictions applying to the transferability of shares and the names and addresses of the members of the supervisory board must be recorded in the Commercial Register. For a single shareholder joint-stock company, the shareholder details must also be recorded.
- Share capital may not be less than CZK 2 million or, in the case of a public offering of shares, CZK 20 million.
- Share capital is divided into a fixed number of transferable shares of a fixed nominal value; they may be registered shares or bearer shares.
- A reserve fund must be created, amounting to 20 percent of the net profit for the first year of profit, up to a maximum of 10 percent of the share capital. In addition, 5 percent of the net profit after tax must be transferred to the reserve fund each year until it reaches 20 percent of the share capital.
- A joint-stock company requires an audit if one or more of the following criteria are met for both the year in question and the preceding year:
 1. net turnover exceeds CZK 80 million per annum
 2. total assets exceed CZK 40 million
 3. the average number of employees exceeds 50.
- Annual financial statements must be published.
- The company must have a supervisory board and a board of directors. Each must have at least three members, appointed for terms not exceeding five years. Directors cannot be members of the supervisory board. In the case of a company with a single shareholder, the board of directors may have less than three members; however, the requirement to have at least three members of the supervisory board would still apply.
- Non-cash contributions to share capital must be valued by an independent, court-appointed expert proposed by the founders (when a company is being established) or the company (share capital increase). The valuation is binding on the company.
- Rights to receive dividends and other rights attaching to the shares may be transferred separately from the shares to which the rights are attached.
- A share's issue price may not be lower than its nominal value.

Limited liability company

(*společnost s ručením omezeným* – “*spol. s r. o.*” or “*s. r. o.*”)

- The company exists independently of its shareholders (members), who are jointly and severally liable for the obligations of the company only up to the amount of total unpaid contributions recorded in the Commercial Register.
- The name must include “*společnost s ručením omezeným*” or the abbreviation “*spol. s r. o.*”, or “*s. r. o.*”.
- The list of members, the amount of each member’s contribution and the names of the members of the supervisory board (if one is established) must be recorded in the Commercial Register.
- The company must have a registered capital of at least CZK 200,000.
- Each member must contribute at least CZK 20,000.
- The maximum number of members is 50.
- A reserve fund must be created, amounting to 10 percent of the net profit in the first year of profits, up to a maximum of 5 percent of the registered capital. 5 percent of the net profit after tax must be transferred to the reserve fund each year, until it reaches 10 percent of the registered capital.
- A supervisory board is only necessary if required by the memorandum of association.
- The general meeting appoints an executive (*jednatel*) or executives, who are legally responsible for the management of the company.
- A limited liability company does not require an audit unless two or more of the following criteria are met, for both the year in question and the preceding year:
 1. net turnover exceeds CZK 80 million per annum
 2. total assets exceed CZK 40 million
 3. the average number of employees exceeds 50.

General partnership

(*veřejná obchodní společnost* – “*veř. obch. spol.*” or “*v. o. s.*”)

- A general partnership is formed by two or more persons (natural persons or legal entities).
- The partners in a general partnership are liable for the debts of the company.
- The names and addresses or registered offices of the partners must be recorded in the Commercial Register.
- Each partner is entitled to act on behalf of the partnership and is jointly and severally liable for the partnership obligations to the extent of its entire property.
- The audit requirements are the same as for a limited liability company.

Limited partnership

(komanditní společnost– “kom. spol.” or “k. s.”)

- A limited partnership is formed by two or more persons (natural persons or legal entities). At least one of the partners must be a general partner, who has unlimited liability for the debts of the partnership. At least one partner must be a limited partner, who is liable for the partnership’s debts only up to the amount of unpaid contributions recorded in the Commercial Register.
- The names and addresses or registered offices of the partners, a statement on whether they are limited or unlimited partners, the amount contributed by each limited partner and the amount of their paid up contributions must be recorded in the Commercial Register.
- Only unlimited partners are permitted to manage the partnership.
- The audit requirements are the same as for a limited liability company.

Co-operative

(družstvo)

- Co-operatives are formed by at least five members (or by at least two legal entities) to undertake business activities for the economic or social benefit of their members.
- The amount of registered capital and the amount of the members’ “basic investments” must be entered in the Commercial Register.
- Members are not liable for the obligations of the co-operative.
- A co-operative must have a registered capital of at least CZK 50,000.
- A fund of at least 10 percent of the registered capital must be created upon incorporation. At least 10 percent of the profits after tax must be transferred annually to the fund until it reaches at least 50 percent of the registered capital.
- The statutory representatives of the company must either be Czech citizens or have Czech residence permits.
- The audit requirements are the same as for a limited liability company.

Branch of a foreign person

(organizační složka zahraniční osoby)

- Branches of foreign businesses can conduct business activities in the Czech Republic if they are recorded in the Commercial Register.
- The entry should include details of the foreign business and its office in the Czech Republic, the scope of business activities and the name and address of its director (general manager).
- A branch must obtain a trade licence from the regional trade licensing (business registration) office.
- A branch does not have limited liability.
- The audit requirements are the same as for a limited liability company.

Company formation

The legal documents required to form a company include:

- a draft of the company's memorandum of association and articles of association or deed of formation (for companies with a single founder);
- for joint-stock and limited liability companies, expert valuations of any non-monetary contributions;
- the minutes of the first general meeting of the shareholders;
- the licence for trading activities, issued by the regional trade licensing (business registration) office;
- proof that capital contributions are paid up;
- documentary evidence of the person authorised to sign documents in the name of the company or the members;
- proof of identity of the shareholders (members);
- an extract from the criminal register in respect of executives or responsible persons;
- a lease contract or a similar document confirming the right to use premises as the registered office;
- evidence of a bank account and payment of the required minimum of contribution to the share capital (usually after formation but before registration in the Commercial Register).

The Commercial Register

Commercial Registers are maintained by the courts. A company has legal status and is entitled to commence business activity in the Czech Republic only after it is recorded in the Commercial Register.

An entry in the Commercial Register includes the following information:

- the name of the entity and the address of its registered office;
- its identification number;
- the scope of business activities;
- the type of entity;
- the names and addresses of the executives or directors, together with details of their authorisation to act on behalf of the entity;
- details of any branches and the branch directors;
- for a joint-stock company: the nominal capital, number and nominal value of the shares of each class, names and addresses of the supervisory board members. If a joint-stock company has a single shareholder, the shareholder name;
- in the case of a limited liability company: the names and addresses of the members, the proposed nominal capital, the amount of each individual member's contribution and the names and addresses of the supervisory board members (if relevant);
- for a general or limited partnership: the names and addresses of the partners;
- in the case of a co-operative: the proposed registered capital, and the amount of each member's contribution;
- in the case of a branch: its business name and address in the country of incorporation, the scope of its business activities, the legal form of the company in its country of origin, the business address in the Czech Republic, and the name and address of the branch director.

Access to the Commercial Register is freely available on the Internet (www.justice.cz).

Statute of limitations

The Commercial Code generally sets the deadline for submission of business-related claims (i.e. the point at which they become time-barred) at four years, although claims against carriers or forwarding agents must be filed within one year. The period for claiming for compensation for damages expires 10 years after the breach of duty occurs. A party against whom the claim becomes time-barred may repeatedly extend the limitation period, for up to a maximum of 10 years, by providing a written statement to the other party.

Liquidation

Voluntary liquidation is governed by the Commercial Code and decided on by a resolution of the shareholders (members) of the company. Executives or directors are responsible for appointing and setting the remuneration of liquidators, who then assume the powers of the executives or directors. The liquidator is obliged to publish a notice of liquidation to enable creditors to submit claims. Except for bankruptcy cases, employee claims have priority.

The liquidator's powers are restricted to acts necessary to complete the liquidation. If he or she establishes that the company is insolvent, the liquidator must file for bankruptcy.

Upon settlement of all liabilities, the liquidator must produce a report indicating how any surplus assets are to be distributed, subject to approval by the shareholders.

The acts of the liquidator may be challenged in the courts by any interested party. Under certain circumstances, the courts may dismiss the liquidator and appoint a successor.

Insolvency

The Act on Insolvency applies to both individuals and legal entities. A petition for insolvency can be submitted by either the debtor or any creditor. Proceedings are held at the regional or municipal court.

The debtor is obliged to submit a petition for insolvency where there is more than one creditor, liabilities are more than 30 days overdue, and the debtor either is not capable of paying these debts, or where the liabilities are higher than assets, taking into account any future profits and other factors influencing the debtor's solvency. If this obligation is not met, civil liabilities may ensue.

Insolvency can be resolved by:

- Bankruptcy proceedings (*konkurs*), involving a proportional rate settlement of debts. If the bankrupt's turnover does not exceed CZK 2 million and there are no more than 50 creditors, simplified proceedings can be used. The bankruptcy de facto leads to the liquidation of the bankrupt.
- Reorganisation, consisting of settlement of debts over time, and continuation of the bankrupt's business activities. Reorganisations are automatically available only for bankrupts with turnover exceeding CZK 100 million or at least 100 employees. Reorganisation for smaller enterprises requires the approval of more than 50 percent of the creditors.
- Debt forgiveness (*oddlužení*): similar to reorganisation, but only applying to persons not carrying on business activities.
- Special proceedings if certain conditions are met.

Once an insolvency order has been granted, the court appoints an administrator, who then has the authority to handle the assets. The court will also convene a meeting of creditors.

The Act on Insolvency allows a trustee in bankruptcy to contest acts that restrict its ability to recover funds from the debtor. This action has to be granted within one year of commencement of the insolvency proceedings. It is possible to override transactions that were carried out, up to three years before submission of the petition for insolvency, if the transaction was with related parties, or up to one year in other cases. In certain cases, transactions can be contested up to five years later.

Chapter 4

Accounting and audit

Accounting requirements

Over the last few years, changes in Czech accounting rules have moved Czech accounting closer to International Financial Reporting Standards (IFRS), although there are still some significant differences.

The Act on Accounting serves as the main framework, and detailed guidance is provided in the Decrees on Double-Entry Accounting and the Czech National Accounting Standards. The Decrees and Czech National Accounting Standards specify the rules and standards for the various types of accounting unit, e.g. companies, entrepreneurs, banks, insurance companies and non-profit organisations, as well as municipalities and institutions financed by the state.

The main features of the accounting regulations are as follows:

- All accounting records must be in Czech.
- Standard rules and accounting principles must be observed.
- The general structure of the accounts must be in accordance with a standard chart of accounts, although the specific details may vary according to individual organisational needs.
- All businesses recorded in the Commercial Register are obliged to use double-entry bookkeeping. Single-entry accounting can no longer be used. Accounting units that are not recorded in the Commercial Register and whose annual turnover does not exceed CZK 25 million are permitted to keep simplified accounting records (“tax evidence system”).
- The depreciation of assets for accounting purposes is determined by the individual accounting unit, based on the estimated useful life of the assets.
- A physical count of inventory and fixed assets is required annually.

- Statutory financial statements consist of a balance sheet, a profit and loss account (at a minimum classified by nature) and notes. Financial statements may also include a cash-flow statement and a statement of changes in equity. The layout and headings of the balance sheet and the profit and loss account are prescribed in the Appendix to the Decrees.
- A separate annual report must be prepared by all accounting units that are subject to a mandatory statutory audit.
- All accounting units with listed shares or bonds must maintain their accounting and prepare their financial statements (and consolidated financial statements) in accordance with IFRS as adopted by the EU.
- The Act on Accounting requires that consolidated financial statements must be prepared for an accounting unit that is a managing or controlling entity. Subsidiaries and accounting units over which significant influence (20 percent of the voting rights) is exercised are deemed consolidated accounting units. This applies to consolidated groups that meet at least two of the following criteria as at the balance sheet date:
 1. the combined turnover exceeds CZK 700 million
 2. the combined assets (without elimination) of the parent company and the subsidiaries exceed CZK 350 million, and
 3. the average number of employees during the accounting period was more than 250.

The exemption from the duty to prepare consolidated financial statements does not apply to banks, insurers and reinsurers, and listed securities issuers.

Consolidation is also not obligatory where the consolidating entity is a part of another consolidating entity that is governed by Czech law or the law of an EU member state, and where specific conditions prescribed by the relevant decree have been met.

It is possible to specify a business year-end other than 31 December, provided there are valid reasons.

Accounting principles and policies

The going concern, materiality, prudence, matching and consistency principles must all be observed during the preparation of Czech statutory financial statements. In recent years, the true and fair view concept has been fully introduced, whereas the fair value accounting concept has been implemented only in certain specific areas, and in the same scope as in IFRS. The legal form, however, frequently overrides substance.

Common accounting policies followed in the Czech Republic include:

- Fixed assets are stated at acquisition cost and are depreciated over their expected useful lives in accordance with accounting methods.
- The option to value an investment at amortised cost or at fair value. In this particular case, fair value is defined as the market price. The net asset amount can be used if the market price is not available.
- Inventories may be accounted for using standard, average, or first-in, first-out (FIFO) principles. The last-in, first-out (LIFO) method is not permitted.
- Goodwill (intangible asset) or an adjustment to acquired fixed assets (tangible asset) arises on acquisitions and re-organisation of businesses: the classification depends on the precise nature of the transaction. Goodwill is amortised over 60 months from the date of acquisition, and an adjustment to acquired fixed assets over 180 months.
- Both realised and unrealised exchange gains and losses arising from monetary assets and liabilities denominated in foreign currency are recognised in the profit and loss account.

Under Czech accounting legislation, there is no concept of finance lease (leased assets are generally treated as fixed assets by the owner, not by the lessee.)

A provision for deferred income tax should be made for all timing differences arising between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which it can be utilised.

Auditing requirements

Audits are compulsory for:

- all banks and mutual funds;
- foundations and certain other non-profit organisations;
- joint-stock companies that in both the current and the previous accounting period meet at least one of the following criteria:
 1. net turnover exceeds CZK 80 million per annum
 2. total assets exceed CZK 40 million
 3. the average number of employees exceeds 50;
- other accounting units that meet at least two of the above criteria.

The Act on Auditors defines the responsibility of the Chamber of Auditors, which is responsible for the authorisation of auditors and for setting the standards for audits. Audits are carried out in accordance with the International Standards on Auditing issued by the International Federation of Accountants (IFAC) and the relevant guidance (*aplikační doložky*) of the Chamber of Auditors of the Czech Republic.

A new Act on Auditors came into effect in April 2009, which implements the provisions of the EU 8th Directive. The main change for companies is that there are now detailed rules regarding the appointment of auditors: auditors must be appointed by the general meeting, an oversight board is responsible for audit quality supervision, and public interest entities are defined. New responsibilities for both public interest entities and their auditors are stipulated in the Act, e.g. Audit Committee, lead partner rotation, transparency report, etc.

There are currently approximately 2,000 state-registered auditors in the Czech Republic.

Chapter 5

Direct taxes

Taxation of legal entities

Corporate income tax is levied on the profits of legal entities, primarily limited liability companies (*s. r. o.*) and joint-stock companies (*a. s.*). Although partnerships are legal entities according to the Commercial Code, the profits of a general partnership (*v. o. s.*) are not subject to corporate tax; instead, each partner's share of the profits is taxed in his or her hands.

In the case of a limited partnership (*k. s.*), the limited partner's share of the profits is subject to corporate income tax at the level of the limited partnership, while the general partner's share is taxed in the same way as in the case of a general partnership.

A branch or permanent establishment of a foreign company is generally subject to tax on the same basis as a company. It is also possible to tax them on a deemed profit basis, which is usually a percentage of revenues generated in the Czech Republic, or a percentage of costs.

Since most of these legal entities by definition exist for the purpose of carrying on a business, virtually all the income and gains which they realise are included in the calculation of their business profits (see "Taxation of business income" below). There are special rules for entities not established for the purpose of making profits. These enjoy certain restricted tax privileges.

The corporate income tax rate is 19 percent in 2010.

Capital gains are generally included in income and taxed at the same rate. However, if at least 10 percent of the shares of a company is held by a parent company

for 12 months, income from the sale of the shares is tax-exempt if the parent is a Czech tax resident company and the subsidiary is resident in an EU member state or a non-EU member state with which the Czech Republic has concluded a double taxation treaty (subject to certain conditions). Income derived by non-residents from the sale of shares in a Czech company is taxable, unless the seller is a company resident in the EU, Norway or Iceland, and at least 10 percent of the shares has been held for 12 months.

There is no tax consolidation in the Czech Republic. Each company within a group is taxed individually, with no set-off of losses against profits between different companies. However, virtual tax consolidation can be achieved through a partnership structure.

Dividends received by Czech resident companies are taxed at a rate of 15 percent. They are exempt from tax if the payer is a company resident in an EU member state, provided that at least 10 percent of the shares has been held for 12 months.

The exemption also applies if all of the following criteria are met:

- the payer is a tax resident of a state with which the Czech Republic has concluded a double taxation treaty;
- the payer has a similar legal form to a limited liability company (*s. r. o.*), joint-stock company (*a. s.*) or co-operative (*družstvo*);
- the recipient has held at least 10 percent of the shares for 12 months;
- the payer is subject to a tax similar to Czech corporate tax, and the rate is at least 12 percent.

The exemption only applies where the recipient is the beneficial owner of the income.

Mergers and divisions of companies can generally be carried out on a tax neutral basis, although any pre-2004 tax losses of the company which ceases to exist are forfeited. The EU Mergers Directive and the EU Directive on Cross-border Mergers have been broadly assimilated into Czech law. In general, domestic legislation maintains the tax neutrality of mergers, and allows the transfer of unused tax losses for transactions satisfying certain legal conditions (transfers of business and mergers), provided that tax avoidance is not the main purpose of the transaction. Additionally, there is a “same activity” rule, under which tax losses can only be offset against income earned from the economic activity that generated the tax loss.

Taxation of business income

The starting point for computing the taxable profit is the profit before tax disclosed by the accounts. This is then subject to adjustments under the Income Tax Act. Unless this act contains a provision to the contrary, income and expenses booked for accounting purposes are taxable/deductible. Where capital gains form part of business profits, they are taxable as normal income or are exempt under the participation exemption rules.

For companies the tax year is generally the same as the financial year. It is possible to adopt a financial year ending on a date other than 31 December provided that it is the last day of a calendar month. If the financial year-end changes, there are provisions in the Income Tax Act for dealing with the resultant long or short period. However, these are not perfectly drafted and numerous issues can arise in such cases. Individuals are always taxed on a calendar year basis.

The Income Tax Act attempts to define in some detail which expenses are deductible and which are not. The general rule is that expenses incurred for the purpose of generating, assuring or maintaining taxable income are tax-deductible.

Disallowable expenses include:

- capital expenditure;
- most reserves (including adjustments to the realisable value of inventory);
- most valuation differences intended to show assets at fair value rather than cost;
- accounting depreciation of tangible and intangible assets;
- gifts and entertainment;
- expenses incurred to generate non-taxable income;
- profit distribution;
- expenses limited by the thin capitalisation rules (see below);
- expenses of a parent company relating to holding shares in a subsidiary; interest on credits and loans taken less than six months before acquisition of the shares is considered to be an expense directly attributable to the shareholding in a subsidiary unless the payer can prove otherwise.

Indirect expenses relating to the holding of shares in a subsidiary are restricted to 5 percent of income from dividends and other profit shares paid out by the subsidiary unless the taxpayer can show that the actual indirect expenses are lower.

Deductible items include:

- tax depreciation of tangible and intangible assets;
- lease payments, subject to certain restrictions;
- certain reserves, as set out in the Act on Reserves;
- expenses on the liquidation of raw material, goods, work-in-progress and products; the reason for liquidation, means, time, place and the nature of the items should be documented.

A special deduction equal to deductible expenditure on research and development can be claimed which effectively means that such expenditure is deducted twice; this deduction, if not used in the period in which it arises, may be carried forward to the next three tax periods.

Lease rentals are generally deductible in accordance with their treatment in the accounts, except for finance leases (“finance lease with subsequent purchase of the leased asset”), where:

- the lease term must be at least equal to 36 months for assets in the first depreciation category, 54 months for assets in the second depreciation category, 114 months for the assets in the third depreciation category or 30 years for real estate;
- the sales price must not exceed the tax residual value calculated using straight-line depreciation.

For leases that do not qualify, if the asset is sold to the lessee at the end of the lease term, the sale price must not be lower than the tax residual value as calculated above.

If the lease term is shorter than stated above, the lease expenses are tax-deductible (provided that other relevant conditions are met), as long as the sales price is not lower than tax residual value.

The Act on Reserves allows restricted deductions for bad debt reserves and write-offs. It also allows taxpayers to create tax-deductible reserves for future repairs, subject to the existence of supporting evidence in the form of project plans, etc. However, reserves created from 2009 are only tax-deductible if funds are transferred to a separate bank account by the due date for filing the annual tax return.

The Act on Reserves contains special rules for loan provisions for banks and reserves for insurance companies.

Tax depreciation can be claimed on fixed assets. Tangible fixed assets are divided into six categories broadly reflecting the expected useful life, as follows:

Depreciation category	Depreciation period
1 IT equipment, certain machinery, etc.	3 years
2 Personal cars, office equipment, certain machinery, etc.	5 years
3 Heavy machinery, etc.	10 years
4 Pipelines, etc.	20 years
5 Buildings other than those in category 6	30 years
6 Administrative and commercial buildings, hotels, department stores	50 years

The depreciation period has been shortened for assets in groups 1 and 2 acquired between 1 January 2009 and 30 June 2010. For assets in depreciation group 1, the depreciation period is reduced to one year; for assets in depreciation group 2, the period is reduced to two years. To ensure equal conditions, a similar adjustment is made to the lease term for assets acquired under finance leases.

Depreciation may be claimed on either a straight-line or an accelerated basis. The accelerated depreciation method applies a series of co-efficients to the input price of the asset. For example, the co-efficients for industrial buildings (category 5) are:

- year 1: 30,
- subsequent years: 31.

In other words, the co-efficient for the first year is the depreciation life, and for the subsequent years it is the depreciation life plus 1.

The depreciation is calculated as follows:

- in the first year the amount of tax depreciation is the input price divided by the coefficient;
- in subsequent years the depreciation is twice the residual value, divided by the appropriate co-efficient less the number of years for which depreciation has been claimed.

A special accelerated rate may be used in the first year of depreciation (provided that other relevant conditions are met) which reduces the depreciation base.

The tax depreciation periods for intangible assets are:

- audiovisual products: 18 months;
- software and research and development: 36 months;
- incorporation expenses: 60 months;
- other intangibles: 72 months.

Goodwill is not an intangible asset for tax purposes. For tax purposes, goodwill is defined as the difference between the value of an enterprise or a part of an enterprise, acquired by purchase, and the aggregate of the market value of its individual assets, reduced by liabilities taken over. Up to 2003, purchase goodwill was depreciated for both accounting and tax purposes over 15 years. In 2003, this was reduced to five years.

From 1 January 2004, however, the tax depreciation period of goodwill was set at 180 months, while the accounting depreciation period remains five years. Goodwill that does not arise on a purchase, e.g. on a merger, is not depreciable for tax purposes. Instead of accounting for goodwill, the difference between the aggregate of accounting residual values of an enterprise (decreased by liabilities) and the market value of the enterprise can be accounted for as a single revaluation difference without revaluation of the individual assets and liabilities. The accounting and tax depreciation period for this is 180 months.

Tax losses incurred up to 31 December 2003 may be carried forward for up to seven years. Those incurred after 1 January 2004 may be carried forward for five years.

Losses may not be carried forward following a substantial change in the ownership of a company unless it can be shown that at least 80 percent of the company's revenues are derived from the same activities as those carried on in the period when the loss arose. A change of at least 25 percent in the ownership of the registered capital or the voting rights, or a change resulting in a person obtaining a controlling influence in the company, is always a substantial change.

A taxpayer can apply to the authorities to confirm the availability of the carried forward losses after the end of the taxable period in which the losses are to be used.

Transfer pricing/thin capitalisation

The Income Tax Act contains two basic provisions relating to transfer pricing and thin capitalisation.

Transfer pricing is dealt with in a short provision that states that if prices agreed in transactions between related parties are not at arm's length and the difference is not properly justified, the tax authorities will adjust the tax base. It is possible to request an advance pricing agreement from the tax authorities on the method of setting the transfer price between related parties. No retroactive agreements are possible. An administration fee of CZK 10,000 is charged per transaction.

In addition to the provisions of the Income Tax Act, the Ministry of Finance has issued the following Guidelines:

- D-258 (January 2004) confirms that the OECD transfer pricing guidelines are applicable;
- D-292 (December 2005) provides detailed information about the procedure of advance pricing agreements;
- D-293 (December 2005) recommends transfer pricing documentation. It is based on the Code of Conduct issued by the EU Joint Transfer Pricing Forum in November 2005.

These Guidelines are not legally binding measures, but given that the tax authorities should follow them, they represent useful guidance for taxpayers.

The thin capitalisation provisions act to restrict the deductibility of interest and other loan expenses where the borrower has insufficient equity. Until the end of 2007 the provisions only applied to related party loans and restricted deductibility of interest if the debt:equity ratio exceeded 4:1. The law has changed several times since then, but the current provisions are similar to those in force earlier.

The rules can be summarised as follows:

- Financial expenses arising from loans and credits received from related parties in excess of four times (six times for banks and insurance companies) the borrower's equity are not tax deductible.
- Interest on loans and credits received from unrelated parties, or those secured by a related party, is fully deductible on general principles, except for interest on "back-to-back" loans (i.e. where a related party provides a loan, credit or deposit to an unrelated party, which then provides the funds to the borrower) which is treated as interest on related party debt.
- Where the interest or other revenue is derived from the borrower's profit, all financial expenses on the loans on credits received are non-tax deductible.

Notwithstanding the thin capitalisation provisions, financial expenses incurred which directly relate to taxable income (e.g. interest income) can be deducted up to the amount of that income.

Interest paid based on loan contracts concluded before 1 January 2008 does not fall within the ambit of the new regulation for tax periods commencing in 2008 and 2009. From the tax period commencing in 2010, all loans will be subject to the new rules.

Any upward adjustment of profit resulting from a transfer pricing or thin capitalisation adjustment relating to a non-EU or EEA resident counterparty may be treated as a dividend, i.e. is subject to dividend withholding tax, as reduced by the provisions of any applicable double taxation treaty.

Taxation of individuals

Individuals are subject to income tax, social security, health insurance, inheritance and gift taxes, and taxes on land and buildings. The taxation of individuals depends primarily on their residence status. Residents of the Czech Republic are subject to tax on worldwide income, whereas non-residents are subject to tax on Czech source income only.

Residence is defined as:

- having a permanent home in the Czech Republic, or
- spending 183 days or more in the Czech Republic during the tax year (the year to 31 December).

Personal income tax is charged on:

- employment income,
- business income,
- investment income,
- rental income,
- capital gains,
- any other income not within the above categories.

There are numerous exemptions, of which the most important are the exemptions from tax on gains from the sale of securities. The exemptions apply to sales of all securities acquired on or before 31 December 2007 if held for more than six months. For securities acquired on or after 1 January 2008, the exemption conditions became stricter and the exemption only applies if the securities are held for more than six months and do not represent more than 5 percent of registered capital and voting rights for 24 months preceding the sale. If these conditions are not met, the gains on the sale of the securities are tax-exempt after exceeding a holding period of five years. Gains on holding shares in a limited liability company are also tax-exempt if held to five years.

Gains from the sale of non-business real estate are exempt if the property has been held by the taxpayer for at least five years prior to the sale. Gains from the sale of a dwelling are also exempt if the dwelling was used as the taxpayer's main residence for at least two years prior to the sale. If the dwelling was used for less than two years, the exemption applies if the gains are used for the taxpayer's housing in the future.

The income of individuals is subject to a flat rate tax of 15 percent. The tax on employment income is calculated on the "super-gross" salary, which is the gross salary increased by social security and health insurance contributions payable by the employer. Foreign employment income that is taxable in the Czech Republic is increased by deemed contributions of 34 percent regardless of the amount of social

security and health insurance contributions actually paid. Thus, the effective tax rate is not 15 percent but a higher rate depending on the income level.

Dividends and other income are taxed separately and are subject to final withholding tax at source.

Foreign source investment income should be included in the tax base and is subject to a flat tax rate of 15 percent.

Rental income may be reduced by actual expenses or by an optional lump-sum deduction equal to 30 percent of the gross income.

Employees are subject to tax on income in all forms, whether in cash or in kind. In particular, benefits, such as the provision of a car which is available for private use, are taxable.

It is not possible to deduct an employee's social security and health insurance contributions from the tax base. However, items such as mortgage interest, payments for supplementary pension insurance with state support, private life insurance premiums, and donations can be deducted if certain conditions are met.

There is little provision for private pension schemes in the Czech Republic. As a result, contributions paid by the employer are, with restricted exceptions, taxable benefits.

Similarly, there are no special provisions dealing with employee share option schemes, so that gains realised on the exercise of an option are regarded as taxable income. It is generally accepted, however, that no gain arises on the grant of an option.

The salaries of employees of Czech persons or registered branches of foreign persons are subject to deduction of tax at source on a monthly basis, with annual reconciliations. It is also possible to second expatriate staff through a permanent establishment of a foreign employer that, although taxable, is not registered in the Commercial Register. In such a case, there is no liability to withhold tax. Instead, the employees themselves are liable to make tax returns and pay the tax, normally in quarterly instalments.

There is a further possible tax treatment of employees of foreign companies – the “deemed employer” rule which is essentially an anti-avoidance provision. The rule may apply where employees of a foreign employer work in the Czech Republic under the control of a Czech person which pays a fee to the foreign employer for their services. In such a case, the Czech person is regarded as the employer for tax purposes and has to account for the employees’ income tax. In practice, this rule is rarely applied to employees of bona fide foreign investors, unless they choose to use it as an alternative to the permanent establishment described above.

Resident and non-resident individuals may claim a basic personal tax allowance of CZK 24,840. Various other credits are granted to a resident, such as a tax credit of CZK 24,840 for a spouse living in the taxpayer’s household if the spouse’s annual income does not exceed CZK 68,000 and CZK 10,680 for a dependent child. These are also granted to non-residents if at least 90 percent of their income comes from sources in the Czech Republic.

Social security contributions, where payable, amount to 45 percent of an employee’s salary. This consists of an employee’s contribution of 11 percent and an employer’s contribution of 34 percent, made up as follows:

	Employer (%)	Employee (%)
Pension	21.50	6.50
Sickness insurance	2.30	0.00
Unemployment insurance	1.20	0.00
Health insurance	9.00	4.50
	34.00	11.00

The maximum annual assessment base (social security and health insurance cap) for 2010 is CZK 1,707,048. Social security and health insurance contributions must be paid on a monthly basis until the aggregate of the monthly assessment base exceeds the maximum annual assessment base. Upon achieving this maximum limit, the employer should stop paying social security and health insurance contributions. The assessment base is very similar to the tax base.

If an employee changes employer during the calendar year, a new “cap” of CZK 1,707,048 will apply to the employee’s new salary, but if the aggregate of the assessment bases exceeds the maximum, the health insurance and social security authorities will return to the employee, upon request, any excess contributions of the employee.

Foreign persons under local employment contracts are subject to normal social security contributions. If a foreign person is employed by a non-Czech employer and there is a social security treaty between the Czech Republic and the country of the employer, he or she is subject to Czech social security, unless under the terms of the treaty they can remain in the social security system of the home state. From 1 May 2004, the authorities take the view that expatriate employees of EU employers are subject to Czech social security based on the EU social security rules. In practice this means that expatriates are liable to Czech contributions, unless they remain in their home state system under the EU rules.

International tax issues

Companies having their “seat” in the Czech Republic are subject to Czech tax on their worldwide income. The company’s seat is defined as the registered office or where is the place of the effective management of the company. Such companies are referred to as “Czech resident”.

Other companies (non-residents) are only subject to tax on their Czech source income, subject to the provisions of any double taxation treaties.

Foreign source income of Czech resident companies is generally taxable in the Czech Republic, subject to the provisions of any double taxation treaties. The income of foreign branches or permanent establishments of Czech residents is included in taxable profit. Dividends from foreign companies are a separate source of income which is taxable at a special rate, currently 15 percent, unless the Parent/Subsidiary Directive applies.

Under certain double taxation treaties, however, the foreign income of Czech residents is exempt from Czech tax. In such cases, expenses related to that income are not tax-deductible. Credit for foreign taxes on income that is also subject to Czech tax is only available if there is a double taxation agreement with the other state. Otherwise, the foreign tax can only be treated as an expense.

The main types of Czech source income for non-residents are:

- income of a permanent establishment in the Czech Republic;
- income from dependent activity (employment) performed in the Czech Republic;
- income from services performed in the Czech Republic;
- income from the sale or use of real estate situated in the Czech Republic;
- income from performance and sporting activities in the Czech Republic;
- royalties, dividends and other profit distributions, interest, and lease rentals;
- lottery and gambling winnings in the Czech Republic;
- alimony and pensions arising in the Czech Republic;
- income arising from a reduction of share capital;
- income from payment of a receivable acquired by assignment;
- penalties from contractual relationships;
- income from transfer of shares in Czech resident companies, which is not tax-exempt under domestic legislation.

These tax liabilities are to some extent mitigated by tax treaties, where applicable. In particular, where there is a treaty:

- income from services can usually be taxed only if the service provider has a permanent establishment in the Czech Republic,
- income from employment can usually be taxed only if the employee is employed by a Czech company or a permanent establishment, or if he or she spends more than 183 days in the Czech Republic.

Income liable to tax is generally subject to withholding taxes, for example:

- dividends – 15 percent,
- royalties (normally including lease rentals) – 15 percent,
- services provided in the Czech Republic – 15 percent,
- activities of entertainers and sportspersons – 15 percent.

Withholding tax is a final tax that is generally reduced by double taxation treaties.

Residents of other EU and EEA countries can file a tax return in respect of other types of income (e.g. interest, royalties, freelance work) subject to withholding tax and claim a deduction for any related expenses (this does not apply for withholding tax from dividends). In such a case, the withholding tax is considered an advance payment. This may result in a reduction in the tax burden as withholding tax is calculated on a gross basis.

The EU Parent-Subsidiary Directive has been implemented in the Czech Republic which means that dividends paid by a Czech subsidiary to a parent company that is tax resident in an EU member state may be exempt from withholding tax. These provisions also apply to dividends paid between Czech companies and dividends paid to Swiss, Norwegian and Icelandic corporate shareholders.

The EU Interest and Royalties Directive has also been implemented in the Czech Republic, but the Czech Republic has been granted a derogation until 2011 in respect of royalties. As a result, interest paid to associated companies resident in the EU, Switzerland, Norway and Iceland is generally exempt from withholding tax (subject to advance clearance procedures). Royalties remain subject to tax at a maximum rate of 15 percent.

The Czech Republic has implemented the EU Savings Directive, which allows the provision of information about interest paid by Czech financial institutions to non-residents.

Other types of income paid to non-EU or non-EEA residents, notably from permanent establishments, real estate and sales of securities, etc., are subject to withholding tax which is not the final tax, but is a prepayment in respect of the ultimate tax liability. This tax is generally levied at the rate of 10 percent (1 percent for sales of securities or payments for receivables purchased from third parties), but may be reduced by prior negotiation with the tax authorities.

The Czech Republic's numerous Double Taxation Treaties are listed below:

No.	Country of Residence of recipient	Effective Date	Dividends	Lower Rate on Dividends (min. percent holding)	Interest	Royalties
			(%)	(%)	(%)	(%)
1.	Albania	1. 1. 1997	15	5 [25]	5/0 ¹	10
2.	Armenia	1. 1. 2010	10	-	10/5 ⁸ /0 ¹	10/5 ²
3.	Australia	1. 1. 1996	15	5 [20]	10/0 ¹	10
4.	Austria	1. 1. 2008	10	0 [10]	0	5/0 ²
5.	Azerbaijan	1. 1. 2007	8	-	10 ¹	10
6.	Belgium	1. 1. 2001	15	5 [25]	10/0 ¹	5/5 EQ /0 ⁴

No.	Country of Residence of recipient	Effective Date	Dividends	Lower Rate on Dividends (min. percent holding)	Interest	Royalties
7.	Belarus	1. 1. 1999	10	-	5/0 ¹	10
8.	Brazil	1. 1. 1991	15	-	15/10/0 ¹	25TM /15
9.	Bulgaria	1. 1. 2000	10	-	10	10
10.	Canada	1. 1. 2003	15	5 [10]	10/0 ¹	10
11.	China	1. 1. 1988	10	-	10/0 ¹	10
12.	Croatia	1. 1. 2001	5	-	0	10
13.	Cyprus	1. 1. 2010	5	0 [10]	0	10/0 ²
14.	Denmark	1. 1. 1983	15	-	0	5/0 ²
15.	Egypt	1. 1. 1996	15	5 [25]	15/0 ¹	15
16.	Estonia	1. 1. 1996	15	5 [25]	10/0 ¹	10
17.	Ethiopia	1. 1. 2009 ⁷	10	-	10/0 ¹	10
18.	Finland	1. 1. 1996	15	5 [25]	0	10/5OL/1FL/0 ²
19.	France	1. 1. 1975	10	0 [25]	0	10/5 EQ /0 ²
20.	Georgia	1. 1. 2008	10	5 [25]	8/0 ¹	10/5 EQ /0 ²
21.	Germany	1. 1. 1984	15	5 [25]	0	5
22.	Greece	1. 1. 1990	15	-	10/0 ¹	10/0 ²
23.	Hungary	1. 1. 1995	15	5 [25]	0	10
24.	Iceland	1. 1. 2001	15	5 [25]	0	10
25.	India	1. 1. 2000	10	-	10/0 ¹	10
26.	Indonesia	1. 1. 1997	15	10 [20]	12.5/0 ¹	12.5
27.	Ireland	1. 1. 1997	15	5 [25]	0	10
28.	Israel	1. 1. 1995	15	5 [15]	10/0 ¹	5
29.	Italy	1. 1. 1985	15	-	0	5/0 ²
30.	Japan	1. 1. 1979	15	10 [25]	10/0 ¹	10/0 ²
31.	Jordan	1. 1. 2008	10	-	10/0 ¹	10
32.	Kazakhstan	1. 1. 2000	10	-	10/0 ¹	10
33.	Kuwait	1. 1. 2005	5	-	0	10

No.	Country of Residence of recipient	Effective Date	Dividends	Lower Rate on Dividends (min. percent holding)	Interest	Royalties
34.	Latvia	1. 1. 1996	15	5 [25]	10/0 ¹	10
35.	Lebanon	1. 1. 2001	5	-	0	5EQ/10
36.	Lithuania	1. 1. 1996	15	5 [25]	10/0 ¹	10
37.	Luxembourg	1. 1. 1993	15	5 [25]	0	10/0 ²
38.	Macedonia	1. 1. 2003	15	5 [25]	0	10
39.	Malaysia	1. 1. 1999	10	-	12/0 ¹	12
40.	Malta	1. 1. 1998	5	-	0	5
41.	Mexico	1. 1. 2003	10	-	10/0 ¹	10
42.	Moldova	1. 1. 2001	15	5 [25]	5	10
43.	Mongolia	1. 1. 1999	10	-	10/0 ¹	10
44.	Morocco	1. 1. 2007	10	-	10 ¹	10
45.	Netherlands	1. 1. 1975	10	0[25]	0	5
46.	New Zealand	1. 1. 2009	15	-	10 ¹	10
47.	Nigeria	1. 1. 1991	15	12.5 [10]	15/0 ¹	15
48.	Norway	1. 1. 1980	15	0 [10]	0	5/0 ²
49.	People's Republic of Korea	1. 1. 2006	10	-	10/0 ¹	10
50.	Philippines	1. 1. 2004	15	10[10]	10/0 ¹	10/15 ⁵
51.	Poland	1. 1. 1994	10	5 [20]	10/0 ¹	5
52.	Portugal	1. 1. 1998	15	10[25]	10/0 ¹	10
53.	Romania	1. 1. 1995	10	-	7/0 ¹	10
54.	Russia	1. 1. 1998	10	-	0	10
55.	Serbia and Montenegro	1. 1. 2006	10	-	10/0 ¹	10/5 ²
56.	Singapore	1. 1. 1999	5	-	0	10
57.	Slovakia	1. 1. 2004	15	5 [10]	0	10/0 ²
58.	Slovenia	1. 1. 1999	15	5 [25]	5/0 ¹	10
59.	South Africa	1. 3. 1998	15	5 [25]	0	10
60.	South Korea	3. 3. 1995	10	5 [25]	10/0 ¹	10/0 ²

No.	Country of Residence of recipient	Effective Date	Dividends	Lower Rate on Dividends (min. percent holding)	Interest	Royalties
61.	Spain	1. 1. 1982	15	5 [25]	0	5 ³ /0 ² /5 ⁵
62.	Sri Lanka	1. 1. 1979	15	-	10/0 ¹	10/0 ²
63.	Sweden	1. 1. 1981	10	0 [25]	0	5/0 ²
64.	Switzerland	1. 12. 1996	15	5 [25]	0	5 SPEC
65.	Syrian Arab Republic	1. 1. 2010	10	-	10/0 ¹	12
66.	Tajikistan	1. 1. 2008	5	-	7/0 ¹	10
67.	Thailand	1. 1. 1996	10	-	10/0 ¹	15/10 ³ /5 ² /15 ⁵
68.	Tunisia	1. 1. 1992	15	10 [25]	12/0 ¹	15 ³ /5 ²
69.	Turkey	1. 1. 2004 ¹	10	-	10/0 ¹	10
70.	Ukraine	1. 1. 2000	15	5 [25]	5/0 ¹	10
71.	United Arab Emirates	1. 1. 1998	5	0[25] ⁶	0	10
72.	United Kingdom	1. 1. 1992	15	5 [25]	0	10/0 ²
73.	United States	1. 1. 1994	15	5 [10]	0	10/0 ²
74.	Uzbekistan	1. 1. 2001	10	-	5/0 ¹	10
75.	Venezuela	1. 1. 1998	10	5 [15]	10/0 ¹	12
76.	Vietnam	1. 1. 1999	10	-	10/0 ¹	10
77.	Yugoslavia (only for Bosnia and Herzegovina)	1. 1. 1984	15	5 [25]	0	10

1 Exemption for certain government loans or investments

2 Cultural royalties

3 Industrial licence fees

4 Cultural royalties are exempt as of 1 January 2004 (a 10 percent rate was applied from 1 January 2001 to 31 December 2003)

5 Royalties arising from any copyright of cinematographic films and films or tapes for television or radio broadcasting

6 The recipient of dividends is a government or company which is at least 25 percent government-owned

7 For Ethiopia – effective date 8 July 2008

8 Exemption for interest on bank loans and credits

TM Trademark royalties only

FL Financial lease

OL Operating lease

EQ Royalties for using equipment

SPEC 5 percent withholding tax under Article 2 of the Protocol to the Czech-Swiss Double Taxation Treaty

Beneficial ownership concept

A number of double taxation treaties concluded by the Czech Republic expressly limit their benefits to beneficial owners of income.

In situations where an investor in the Czech Republic is a foreign entity or a trust that is tax transparent under its own tax laws, the Czech Republic will generally honour its transparency for the application of the Income Tax Act and double taxation treaties. The income paid from the Czech investment will normally be treated as the income of the ultimate beneficial owner of the investment via the transparent entity.

Tax administration

Tax administration is governed mainly by the Administration of Taxes Act with specific procedures provided by other acts.

All Czech resident companies, limited partnerships, and permanent establishments of non-resident companies must file tax returns. This does not apply to general partnerships where the partners declare their share of the partnership profits.

All individuals with a monthly taxable income exceeding CZK 15,000 must file tax returns unless the income is tax-exempt or subject to withholding tax. This means that, in general, employees of Czech companies or branches of foreign entities are not required to file returns unless they have other taxable income. Anyone who claims a tax loss must file a return.

The deadline for submission of a tax return is three months from the end of the taxable period. For all taxpayers, with the exception of legal entities that have adopted a non-calendar year-end, the taxable period is the calendar year, and the tax return deadline is therefore 31 March. This deadline is extended by a further three months if:

- the taxpayer is subject to a statutory audit, or
- the taxpayer engages a registered tax advisor to submit the tax return on its behalf.

Except for withholding tax, income tax is collected during the year by a system of prepayments based on the previous year's liability. The final deadline for settling the liability is the same as for the submission of the return. The tax is treated as paid when it is received by the tax authority.

The tax authority has the power to carry out tax inspections in order to establish or examine the tax base or other circumstances decisive for the correct determination of the tax liability. Tax may not be assessed or additionally assessed after three years have elapsed from the taxable period in which the tax liability arose. However, if an activity directed at assessment of tax (e.g. tax inspection) is carried out within this period, the deadline for assessment of tax is extended by a further three years, up to a maximum of 10 years. If an appeal is lodged against an assessment, the payment of any additional tax is deferred until the tax directorate has issued a decision, but interest continues to be calculated on the outstanding amount.

Where a taxpayer has declared a loss, the period in which an inspection may be carried out is extended by the period during which the loss may be utilised. Since losses may be carried forward for up to five years, theoretically an inspection could be carried out up to 15 years after the period.

Interest on overdue tax due on or after 1 January 2007 is assessed at the CNB Repo rate plus 14 percent for the first five years; no interest accrues after this date. Where additional tax is assessed by the tax authorities, a penalty of 20 percent of the additional tax will be levied. If a VAT refund is reduced, the penalty is 20 percent of the reduction. If the tax loss is reduced, 5 percent of the reduction is payable as a penalty. If the taxpayer corrects the tax base in an additional tax return, only interest on overdue tax will be payable. Different rates apply for tax with an earlier due date.

Chapter 6

Indirect taxes

Value Added Tax

The Czech Act on VAT is based on the general principles of EC Directive 2006/112.

VAT is generally due on any supply of goods or services made by taxable persons during their business activities for a consideration where the place of supply is in the Czech Republic. However, certain transactions carried out for no consideration, such as the provision of certain business gifts or the private use of business assets, are also subject to VAT.

The following transactions are subject to Czech VAT:

- delivery of goods and transfer of immovable assets whose place of supply is in the Czech Republic;
- provision of services whose place of supply is in the Czech Republic;
- intra-Community acquisitions of goods whose place of supply is in the Czech Republic;
- goods imported into the Czech Republic.

Generally, goods acquired from VAT payers in other EU member states by a person who is registered for Czech VAT are subject to Czech VAT. VAT should be self-assessed by the individual/entity acquiring the goods. If the goods are supplied by a supplier from another EU member state, a “deemed” Intra-Community Acquisition of goods must be declared by the acquirer. Subject to the general VAT principles, the individual/entity acquiring the goods can deduct the related input VAT in the same VAT return.

The import of goods from outside the EU is subject to Czech VAT which is payable by the importer. If the importer is registered for Czech VAT, import VAT should be declared

using the standard VAT return. Subject to the general principles for VAT deduction (see below), the importer can deduct the import VAT in the same VAT return.

From 1 January 2010, the following rules for determining the place of supply of services are applicable:

- the place where the service recipient has registered its office or place of business, if the recipient is an entity liable to tax (B2B services);
- if the recipient is from a third country (outside the EU) and is registered for VAT in the Czech Republic, the above rule applies only if the service is consumed outside the Czech Republic. For services consumed in the Czech Republic, the place of taxable supply is in the Czech Republic;
- the place where the service provider has its registered office, if the recipient is a person not liable to tax (B2C services).

There are a number of exceptions to the above general rule, the most important of which are:

- services connected with immovable property: the place of supply is in the state where the property is located;
- transport of passengers: the place of supply is in the state where the transport is provided;
- services in the areas of health, culture, sport, science, education, entertainment, trade fairs, etc.: the place of supply is in the state where the service is carried out/the event takes place;
- catering and restaurant services: the place of supply is in the state where the service is provided;
- short-term lease of a means of transport: the place of supply is in the state where the vehicle is handed over;
- special conditions are set for a number of services if they are provided to persons not liable to tax.

VAT Registration

If an entity/individual has a registered office, place of business or VAT establishment in the Czech Republic, it is treated as a Czech entity for VAT purposes. A Czech entity making taxable supplies in the Czech Republic that exceed the VAT registration threshold of CZK 1 million in 12 consecutive calendar months is required to register and account for Czech VAT.

Even if the registration threshold is not exceeded, Czech entities can still choose voluntarily to register for VAT.

Foreign and EU entities/individuals without a registered office or place of business in the Czech Republic are obliged to register for Czech VAT if they make a taxable supply in the Czech Republic on which they have to account for VAT, provided that the reverse-charge principle cannot be applied. This applies specifically to local supplies of goods, and the provision of certain services to individuals/entities not registered for VAT in the Czech Republic. There is no VAT registration threshold for such individuals/entities, which means that VAT registration is obligatory if a Czech taxable supply of any value is made. Non-Czech entities are not obliged to appoint a fiscal representative in the Czech Republic.

Permanent establishments of foreign and EU entities in the Czech Republic must register for VAT upon establishment.

A non-Czech entity can avoid registering for Czech VAT if the obligation to account for the VAT due can be transferred to a Czech customer, provided that the customer is registered for VAT, or if any simplification can be applied. Simplification procedures have been specifically implemented in the following areas:

- triangulation supplies,
- call-off stock sales,
- supply and installation of goods.

As these provisions and a number of other supply categories are subject to particular requirements, non-Czech suppliers should check carefully whether they comply with them.

A group of related parties with a registered office or place of business in the Czech Republic can register as a single VAT payer.

Format of VAT registration number

The format of a Czech VAT registration number is as follows: CZ1234567890 (the number of digits may vary).

Reporting requirements

VAT returns

If the annual turnover of a Czech entity/individual is higher than CZK 10 million, VAT returns must be submitted on a monthly basis. If the annual turnover is lower than CZK 2 million, VAT returns must be submitted quarterly. If the turnover is between CZK 2 million and CZK 10 million, the taxable person can choose whether to file monthly or quarterly VAT returns.

Non-Czech entities that do not have a permanent establishment in the Czech Republic may only file VAT returns quarterly, i.e. monthly filing is not allowed.

VAT returns must be submitted by the 25th day of the month following the tax period, even if no tax liability arises. VAT must be paid by the due date for submitting the VAT return. The date the liability is considered settled is the date when the payment is credited to the bank account of the tax authority.

If there is an excess of input VAT, the VAT refund is paid to the VAT payer within 30 days of the deadline for submitting the VAT return without any need to request the refund. If a tax audit is initiated before the VAT is refunded, the time limit is extended. In such cases, the VAT will be refunded within 30 days of the audit being finalised.

EC Sales Lists

An EC Sales List ("ESL") must be completed if a VAT registered business:

1. supplies goods from the Czech Republic to another EU member state to a person registered for VAT in another EU member state, or
2. moves its own goods from the Czech Republic to another EU member state, or
3. acts as the intermediary in a triangular transaction between VAT registered traders in other EU member states, or
4. provides a service to a customer established in another EU member state where the place of taxable supply is and where the customer is established, and the supply is not exempt from VAT (general rule).

The EC Sales List should be submitted electronically by the deadline for the submission of the VAT return for the period in which the transaction takes place. Quarterly VAT payers only provide services as described in point 4 above, the EC Sales List may be

submitted on a quarterly basis. A penalty of up to CZK 2 million may be imposed for failing to submit the EC Sales List.

Intrastat declarations

VAT registered businesses that dispatch goods to or receive goods from other EU member states that exceed the relevant annual thresholds (CZK 8 million for dispatches or CZK 8 million for goods received) must complete and file an Intrastat declaration.

Intrastat declarations are submitted on a monthly basis by the 10th working day of the month following the month for which the declaration is filed (by the 12th working day if the Intrastat declaration is submitted electronically). A penalty of up to CZK 1 million may be imposed for failing to submit the Intrastat declaration. Electronic filing is obligatory for forms with more than 15 items.

VAT rates

The standard rate of VAT, which applies to most taxable supplies, is 20 percent. In addition, there is a reduced rate of 10 percent, which applies to a number of goods and services including:

- construction services in respect of residential buildings and flats intended for social housing (a specific definition of flats and houses intended for social housing applies);
- reconstruction and repairs of residential buildings and flats;
- sewerage services and water supplies;
- health and social services;
- public transport services;
- food products;
- books, brochures, newspapers and magazines, where advertisements do not exceed 50 percent of the contents, picture books, and books for children;
- certain health products and services and aids for the disabled;
- firewood.

The VAT payer can request the tax administrator for information about the correct VAT rate to be used in a specific case.

Exempt (zero-rated) supplies

The supplies mentioned below are generally exempt from VAT but the supplier has the right to deduct any related input VAT.

Intra-community supplies of goods

If goods are sold to a customer registered for VAT in another EU member state, and the sale involves the transfer of the goods from the Czech Republic (either by the supplier or the customer) to another EU member state, the supply is a zero-rated (exempt with credit) intra-Community supply. The supplier should obtain the customer's VAT number and include it on the invoice. Documentation verifying the removal of the goods from the Czech Republic should be obtained for tax audit purposes.

If goods are sold and delivered to a customer who is not registered for VAT in another EU member state, Czech VAT should be accounted for unless the "distance selling" threshold in the destination EU member state is exceeded. Once the limit is exceeded, the supplier may have to register for VAT in the other member state.

Export of goods

The export of goods to customers outside the EU can be zero-rated, provided that the following conditions are met:

- the goods are released under the customs procedures of export, outward processing or transit, or the goods are released under a customs-approved treatment of re-export of goods from the EU customs territory, or the goods are placed in a customs-free warehouse or zone in the Czech Republic;
- transport is arranged either by the Czech exporter or by a third party authorised by the exporter; or
- transport is arranged by the customer (if the customer does not have a registered office, place of business or permanent establishment in the Czech Republic), or by a third party authorised by the customer.

As proof of export of the goods, the VAT payer should be able to provide an official document from the customs authority confirming the export of goods to a third country or the placement of goods into a customs-free warehouse or zone in the Czech Republic.

Exempt supplies

The items listed below are exempt from VAT:

- insurance services;
- financial services;
- postal services;
- betting, gaming and lotteries;
- education;
- health and welfare services;
- TV and radio broadcasting;
- certain other supplies of goods and services specified by the Act on VAT;
- transfers of land (excluding land for development);
- transfers (including finance leases) of immovable property (buildings, flats and non-residential premises) three years after the first approval for use was issued by the building authorities or the first use of the property (whichever is earlier);
- lease of land and buildings (apart from the short-term lease of buildings, the lease of parking spaces and the lease of safe deposit boxes).

The taxpayer may opt to charge VAT on the rent of land and buildings to other entities/ individuals registered for VAT.

Recovery of input VAT

A Czech VAT payer is entitled to recover input VAT in respect of taxable supplies from another VAT payer or in respect of imported goods, if they are used for its business activity.

Full recovery of input VAT

A VAT payer is only entitled to recover all input VAT on taxable supplies in respect of:

- taxable supplies liable to Czech output VAT;
- zero-rated (exempt with credit) supplies, such as the dispatch of goods to other EU member states and the export of goods to third countries;
- supplies with a place of supply outside the Czech Republic, as long as the input VAT would have been recoverable if they had been made within the Czech Republic;
- certain exempt supplies to which the right to deduct VAT does not apply if they are supplied to a non-EU entity/individual (non-EU) that does not carry out business activity in the Czech Republic, or if the supplies are directly linked to the export of goods;
- certain non-VATable supplies specified in Czech VAT law (e.g. sale of an enterprise or supply of advertising material).

A VAT payer must prove its right to recover VAT through an invoice (VAT document). The Act on VAT contains a detailed description of the required content of invoices.

The VAT payer can recover input VAT in the VAT return for the taxable period in which the taxable supply was received or in which a related payment was received (including advance payments). However, input VAT cannot be recovered more than three years after the end of the tax period in which the taxable supply was made.

No recovery of input VAT

A VAT payer is generally not entitled to recover input VAT on:

- taxable supplies used to make VAT-exempt supplies, such as financial services, insurance, lease of real estate, education, health services, etc., except where certain financial services are provided to non-EU residents;
- taxable supplies used for representation (entertainment) to the extent that they are not tax-deductible for income tax purposes.

Partial recovery of input VAT

A VAT payer is entitled to partial VAT recovery in respect of inputs related to both types of supplies, i.e. those qualifying for full recovery of input VAT and those not qualifying for recovery. The recoverable amount is based on the ratio of VATable supplies to total supplies.

With regard to fixed assets, a VAT payer is obliged to amend the input VAT claim if the purpose for which the asset is used (full/partial/no deduction of input VAT) changes during the five years following the year of acquisition.

VAT refunds for foreign persons

The Czech Republic has implemented the general provisions of the EU 9th and 13th Directives in respect of VAT refunds for entities registered for VAT purposes in other EU member states or non-EU businesses.

The conditions for a Czech VAT refund for an EU entity are as follows:

- The entity is established and registered for VAT in another EU member state.
- During the period for which the VAT claim is submitted, the claimant did not have a registered office, place of business or permanent establishment in the Czech Republic, and did not make any supplies in the Czech Republic, except for zero-rated or reverse-charge supplies (e.g. imports of goods, exempt supplies to which the right to deduct VAT does not apply, provision of transport, services directly related to the export of goods, and supplies subject to the reverse charge).
- The goods or services were purchased in the Czech Republic for the purpose of the claimant's business.

A VAT refund can be claimed on the same conditions that apply to a Czech VAT payer. Therefore, a refund cannot be claimed on goods and services for which input VAT cannot normally be recovered.

The VAT refund should be claimed electronically in the state where the entity/individual has a registered office or place of business. The application must be submitted by 30 September of the year following the year in which the VAT was incurred. The application must be:

- in Czech;
- supported by electronic copies of tax documents issued by a Czech VAT payer, proving the supply of goods or services; this does not apply to supplies not exceeding EUR 250 in the case of hydrocarbon fuels, or EUR 1,000 in the case of other goods or services;
- accompanied by a written declaration (in Czech) that the applicant has not supplied goods or provided services in the Czech Republic (apart from the exceptions referred to above);
- accompanied by additional documentation, such as official confirmation of the claimant's bank accounts, etc.

If the conditions are met and the application is submitted with the requisite documents, the VAT should be refunded within four months from submission of the application and resolution of any queries raised by the related tax authority. If the tax authority requests any additional data, it should issue the decision within six to eight months from submission of the application. However, as the system has changed from the beginning of 2010, it is not known whether the tax authorities will meet this deadline in practice.

A VAT refund can normally be claimed only if the period covered by the refund is at least three months, but less than or equal to a calendar year, and the amount involved is at least EUR 400.

A refund of less than EUR 400 may be claimed if it relates to the entire calendar year, and the amount claimed is at least EUR 50.

Non-EU businesses can claim refunds of Czech VAT by submitting a written application to the Tax Authority for Prague 1. A refund cannot be claimed for VAT on telecommunication charges, fuel, taxi services, entertainment, travel or accommodation. However, as refunds are only made on the basis of reciprocity, they can only be claimed by businesses based in Macedonia, Norway and Switzerland.

The application must be:

- in Czech;
- supported by original tax documents issued by a Czech VAT payer, proving the supply of goods or services for supplies. This does not apply to simplified tax documents;
- accompanied by a confirmation that the applicant is registered for VAT in the third country, issued by the tax authority in the state where the registration is made;
- accompanied by a declaration that the applicant has not supplied goods or provided services in the Czech Republic (apart from the exceptions referred to above);
- accompanied by additional documentation, such as an official confirmation of the claimant's bank accounts, etc.

A refund of less than CZK 7,000 may be claimed if it relates to the entire calendar year and the amount claimed is at least CZK 1,000.

Customs duties

The Czech Republic has been a member of the European Union since 1 May 2004, and customs matters are therefore governed by EU law.

The Czech Republic has an inward processing regime ("IPR"), which effectively allows a Czech manufacturer to import, process and export goods exempt of customs duty and VAT.

The IPR has two forms:

1. the "drawback system", under which imported components are released for free circulation; this entails the payment of customs duty and VAT on import; the customs duty is subsequently repaid (and the VAT recovered in the same way as any Czech input VAT) if the imported goods are exported from the Czech Republic in the form of upgraded products; or
2. the "suspension system", under which imported components destined for export from the Czech Republic in the form of upgraded products are, from the beginning, exempt from customs duty and VAT.

In both cases, the importer of records is the manufacturer to whom the material is released. Ownership of the goods is irrelevant. Under the IPR, Czech materials can be added to processed foreign components. The application of the IPR must be negotiated

with the local customs authority. Given the complexity of the regime, each case should be carefully analysed to ensure the optimum customs and VAT treatment.

Excise duties

Excise duty is payable on hydrocarbon fuels and lubricants, wine, spirits, beer, and tobacco products. Excise duties are fixed at a set amount per unit for each group of products.

The Act on Excise Duty implements the EU rules governing the production of excise goods and their release into free circulation. They must generally be produced in a tax warehouse. Once removed from the tax warehouse, they must be released into free circulation and excise duty must be paid, or they can be transported under a suspension exemption to a licensed trader in another EU member state, or to another tax warehouse. They can also be exported outside the EU under the suspension system. Excise duty is paid upon termination of the suspension regime. A licensed trader cannot store or sell the products under the suspension system and is obliged to pay excise duty upon receipt of the goods.

Excise duty is administered by the customs authority.

Energy taxes

Energy taxes include tax on natural gas and other gases, electricity and solid fuels. Only supplies of such products delivered within the Czech Republic are subject to tax. These taxes were introduced in order to implement EC Directives 2003/96/EC and 2004/74/EC.

The tax rates are:

Natural gas and other gases	for engines, from CZK 0 to CZK 264.80/MWh; for other purposes CZK 30.60/MWh
Solid fuels	CZK 8.50 per gigajoule, gross calorific value
Electricity	CZK 28.30/MWh

An exemption from energy tax may be claimed for energy used in metallurgical or mineralogical processes. Metallurgical processes involve the heated processing of ores or concentrates, and the production of basic metals and metallurgical products

classified under DJ 27 in the NACE nomenclature. Mineralogical processes involve the production of other non-metal mineral products classified under DI 26 in the NACE nomenclature. As a result, numerous activities of metallurgical plants and metal processors, producers of mineral insulation materials, glassworks and producers of building materials are exempt.

In order to claim the exemption, approval must be obtained from the customs authority.

Traders in electricity, gas or solid fuels may also purchase these products excluding the tax, but prior approval of the customs authority is necessary.

Electricity or raw materials used in the production of energy are tax-exempt as long as they are not used as motor or heating fuel. Examples of such purposes include:

- chemical reduction processes in blast furnaces (solid fuels);
- electrolytic processes (electricity);
- electricity production (natural gas, other gases, solid fuels);
- combined production of electricity and heat, using generators with a minimum efficiency level, provided that the heat is supplied to households (natural gas, other gases, solid fuels);
- coke production (solid fuels);
- technological purposes necessary for the production of electricity or for the combined production of heat and electricity (electricity);
- technological purposes necessary for maintaining the ability to produce electricity or combined heat and electricity production (electricity);
- cover of the losses of a transfer or distribution network (electricity);
- operation of railways, including transportation of persons and freight by tramways and trolleybuses;
- fuel used for navigation within the Czech Republic, except by private recreational boats (natural gas, other gases and solid fuels);
- technological purposes in a business producing solid fuels (solid fuels).

In addition, supplies of natural gas and certain other gases are tax-exempt if they are used for the production of heat for households and heating facilities. Electricity is also tax-exempt if it is generated from renewable sources. No approval is required to claim the tax exemption in these cases.

Real estate tax

Real estate tax is payable by the owners of immovable property situated in the Czech Republic. Different rates apply to undeveloped land, agricultural land and buildings.

The property tax on buildings used for business purposes is based on the area of the buildings, using the rates below:

	CZK/m ²
Residential and agricultural	2
Industrial	10
Other business	10

An additional charge of CZK 0.75 per square metre is levied for each storey (first floor upwards) of a building.

Real estate tax on agricultural land is 0.75 percent of the deemed value. Special rates apply for forests, lakes and ponds.

For other types of land, the tax is based on the area, and the rate is CZK 1 per square metre for building plots and CZK 0.20 per square metre in other cases.

The rates are multiplied by a co-efficient ranging from 1 to 5 depending on the location of the property. In addition, the tax can be increased by another co-efficient, varying from 2 to 5, based on the decision of the relevant municipality.

Real estate tax is deductible for corporate income tax purposes.

Real estate transfer tax

A transfer tax of 3 percent of the higher of the purchase price or the appraised value is payable by the seller on all sales of land and buildings and other immovable assets. A special return must be submitted, and the tax must be paid within 30 days of registering the sale. Where the seller does not pay the tax, the liability is transferred to the buyer. The tax is deductible for corporate income tax purposes.

Inheritance and gift tax

Inheritance tax is payable by deceased persons' heirs who are not spouses or close relations. Subject to certain exemptions, if the deceased person was a Czech citizen with permanent residence in the Czech Republic, the tax is charged on the net value of all assets (except real estate abroad). Otherwise, it is charged only on assets in the Czech Republic.

Gift tax is charged on the gratuitous acquisition of property by a company or a person who is not a qualifying spouse or a close relation. The taxpayer is normally the donee, but if the donor is a Czech resident and the donee is not, the tax is payable by the donor. The gift tax rates are:

Value (CZK)	Rate
up to 1 million	7%
1 million to 2 million	9%
2 million to 5 million	12%
5 million to 7 million	15%
7 million to 10 million	18%
10 million to 20 million	21%
20 million to 30 million	25%
30 million to 40 million	30%
40 million to 50 million	35%
over 50 million	40%

For inheritance tax, the rates are reduced by 50 percent.

Chapter 7

Banking and finance

Local banking system

The Czech National Bank (CNB) is the central bank of the Czech Republic. Its function is to determine monetary policy, issue banknotes and mint coins, and to manage the circulation of notes and coins, the payment system, and settlement between banks. For more details, see www.cnb.cz.

The CNB also co-ordinates supervision of the Czech financial market, which includes the banking sector, capital market, insurance and pension funds sector, credit institutions, the foreign exchange market and electronic money institutions.

To supervise the market effectively, the CNB lays down rules safeguarding the stability of the financial market. It systematically carries out regulation, examinations and assessments and, where appropriate, issues penalties for non-compliance with these rules.

The responsibility for preparing primary legislation for the financial market sector lies mainly with the Ministry of Finance, and the CNB assists in this process.

As an EU member, the Czech Republic has the obligation to adopt Directives issued by the European Community. They are concerned with the stability of the European financial market and are thus focused on measuring risks more accurately, improving internal control systems, and on increased transparency and customer protection. On the other hand, introducing such changes may also mean increased costs or uncertainty for financial institutions (Basel II and MiFID).

The licensing of banks or branches of banks (from countries outside the European Economic Area) and some matters connected with mergers, transfer of assets to partners, etc., are fully within the responsibilities of the CNB.

A foreign bank can enter the Czech banking sector in the following four ways:

- as a new company, with up to 100 percent foreign ownership;
- by acquiring an equity stake in an existing commercial bank;
- by establishing a branch of the parent bank, with a banking licence;
- by establishing a branch of the parent bank, based on the banking licence of the parent bank (applicable to banks with a registered office in the European Union) – the “single banking licence principle”.

Before it grants a banking licence, the Czech National Bank requires:

- a minimum registered capital of CZK 500 million (not applicable to a branch), which is fully paid up (the CZK 500 million minimum must take the form of monetary investments);
- a detailed business plan based on a comprehensive economic analysis;
- information about the founders, and the amount, structure and source of equity capital;
- a detailed description of related parties of the bank;
- details of the registered office of the bank in the Czech Republic;
- information about the scope of the bank’s intended activities; and
- information regarding the organisation and management of the bank, and its internal control system.

Foreign-owned banks have the same rights and obligations as Czech banks. The above requirements must therefore be fulfilled in connection with setting up a branch office of a foreign bank. In addition, the branch office must obtain approval from the regulatory body of the parent bank in the home state.

Branches operating under the single banking licence principle must fulfil the following requirements:

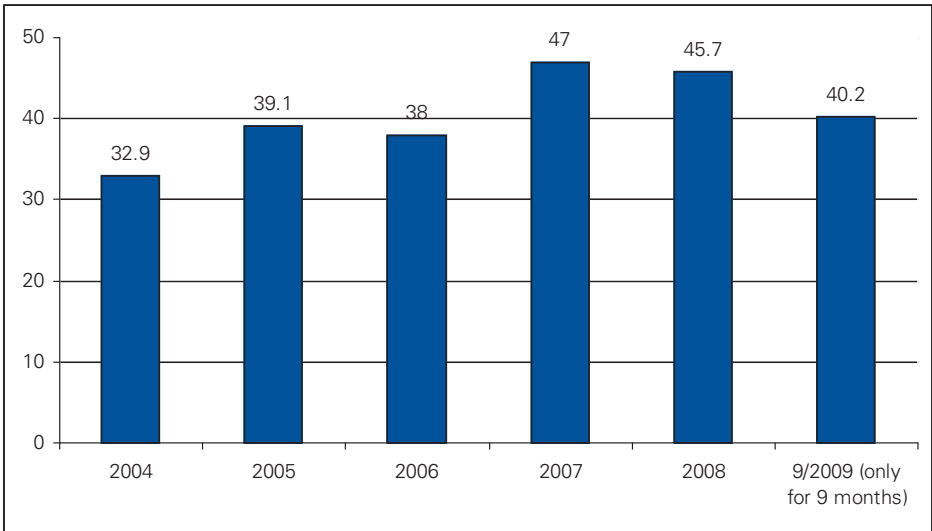
- the parent bank must hold at least 90 percent of the voting rights and registered capital of the branch;
- activities intended to be carried out in the local market by the branch must also be carried out in the domestic market of the parent bank;
- the local branch must be included within the scope of the consolidated supervision of the parent bank, for regulatory supervision purposes;
- the parent bank must jointly and severally guarantee the commitments entered into by the branch;
- the parent bank must satisfy the home supervisory authority requirements regarding the prudent management of the branch.

A bank wishing to establish a branch in a host state must notify the supervisory authority of the home state and provide it with information regarding activities, organisational structure and addresses. Within three months of the receipt of such information, the home state supervisory authority will notify the host state supervisory authority of the bank's intention, unless the supervisory authority of the home state has reason to doubt the adequacy of the administrative structure and financial situation of the bank.

Within two months of the information being received, the supervisory authority of the host state will prepare for the supervision of the bank. The branch may commence its activities in the host state upon receipt of the information about the host state's legal provisions applying to the branch's activities in the host state or if the two months have elapsed without such information being received.

As at 30 September 2009, there were 38 banks (foreign branches included) offering banking services to clients in the Czech Republic. Thirty-one banks were controlled by foreign investors and seven were controlled by domestic owners. In addition, in that year a predominant role was played by a group of three large banks (banks with total assets greater than CZK 600 billion) in the banking sector. As at 31 December 2008, their share of total assets equalled 57 percent. The banking sector remained profitable in 2009. As at 30 September 2009, net profit totalled CZK 40 billion (for the whole of 2008 it was CZK 46 billion).

Figure 2: Net profit of Czech banking sector, in billions of Czech crowns¹⁸



Since December 2008, the Deposit Insurance Fund (the “Fund”) has been providing insurance protection for 100 percent of deposits, including interest accrued, up to a maximum balance of EUR 50,000 per client at a single bank. Bank deposit claims, foreign banks, financial institutions, health insurance companies and state funds are not insured. All banks and branches of foreign banks (excluding branches of parent banks participating in the deposit insurance scheme in the parent country) are obliged to participate in the scheme and to contribute to the Fund, to the extent specified in the Act on Banking.

The annual contribution of a bank to the Fund is 0.1 percent of the average volume of insured deposit claims for the previous year, including interest accrued.

In addition, a Central Credit Register has also been established to decrease the credit risk of the banks. The Register is an information system that pools information on the credit commitments of individual entrepreneurs and legal entities, and facilitates

¹⁸ Source: Czech National Bank

the efficient exchange of such information between those who provide details of debtors listed in the Register.

The Czech National Bank issued a decree on prudential rules for banks, credit unions and investment firms in 2007. It introduced the principles of Basel II into Czech banking regulations. Banks in the Czech Republic are required to maintain a capital adequacy ratio of 8 percent. The Act on Financial Conglomerates tightens up prudential rules, mainly capital requirements for financially-related groups that fulfil the definition of financial conglomerates.

Prague Stock Exchange

The Prague Stock Exchange (PSE) began trading in April 1993. Currently it is possible to trade on the regulated Main and Free markets, which are both regulated by the PSE and, from December 2008 onwards, the non-regulated Multilateral Trading Facility market. The basic criteria for trading on each market are as follows:

- Only companies that offer at least 25 percent of their share capital to the public within the EU, have existed for at least three years and whose market capitalisation of issued shares is at least EUR 1 million for shares or EUR 200,000 for bonds are allowed to trade on the Main Market. The main obligation is, however, the issuer's obligation to make its financial information publicly available on a regular basis. The issuer also must prepare its audited financial statements according to IFRS.
- Companies that apply for trading on the regulated Free Market do not have to fulfil criteria in terms of public trading of their shares, existence, or market capitalisation. However, they are required to meet information requirements, such as preparation of IFRS financial statements. The PSE also organises trading on a special market for investment instruments other than securities (e.g. futures and emission rights).
- For companies that apply for trading on the non-regulated Multilateral Trading Facility market, the basic information requirements are much less strict in comparison to the regulated markets, i.e. preparation of IFRS financial statements is not required, and financial information is submitted on an annual basis only.

Exchange deals are cleared by the Securities Centre. Trading and exchange trading licences are issued by the CNB.

In 2004 a complex regulatory framework for the capital markets was introduced, the Act on Capital Markets. This act defines investment instruments and investment services, as well as the capital adequacy requirements for brokers, who are required to maintain a capital adequacy ratio of 8 percent. The calculation of the capital adequacy ratio is similar to the ratio calculation for banks.

The Czech National Bank issued a decree on prudential rules on providing investment services for securities traders in 2008. This decree introduced the principles of MiFID into Czech regulations.

The Act on Business Activities on the Capital Market allowed trading off-exchange, primarily for small shareholders, until 2008. The main off-exchange market in the Czech Republic was the RM System. It formerly matched buyers and sellers, either through online trading or through intermediaries located throughout the Czech Republic.

In compliance with the implementation of MiFID requirements in local legislation and the relevant amendment of the Act on Business Activities on the Capital Market, the RM System was transformed into the PSE as of 1 December 2008. As a result, securities trading on the RM System is allowed for individual investors or shareholders, primarily through licensed intermediary brokers.

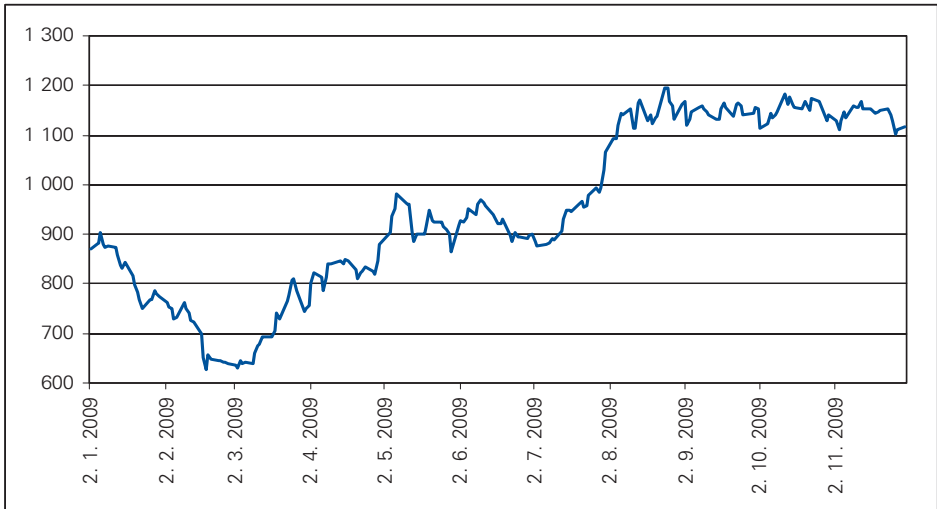
In the RM System both the security and the related cash consideration must be delivered on the trade date.

The regulatory and reporting requirements for companies listed on the RM System are also less stringent than for companies listed on the PSE. For more details, see: www.rmsystem.cz

The main index of the Prague Stock Exchange – called the PX Index – closed on 30 September 2009 at 1.157 points (30 September 2008: 1.204) and dropped year-on-year by 4 percent. The overall trade volume of stocks for nine months in 2009 reached CZK 439,539 million (2008: CZK 852,043 million). The market capitalisation of the stock increased from CZK 1,091,731 million as at 31 December 2008 to CZK 1,293,636 million as at 30 November 2009, of which CZK 821,772 million related to domestic issues and CZK 471,864 million to foreign issues. Market capitalisation increased by 18.5 percent

compared to the end of 2008. During 2008 there was only one IPO on the Main Market of the PSE; no IPOs occurred during 2009.

Figure 3: Movement in the PX index during 2009¹⁹



Foreign exchange

The Act on Foreign Exchange, as amended in July 2009, fully implemented the obligations that the Czech Republic accepted under international agreements that have a substantial influence on the free movement of capital and payments. The Czech Republic has concluded many agreements with other countries on the promotion and reciprocal protection of investments.

If granted a foreign exchange licence, a bank may trade freely in foreign currencies and is not subject to foreign exchange regulations.

¹⁹ Source: PSE

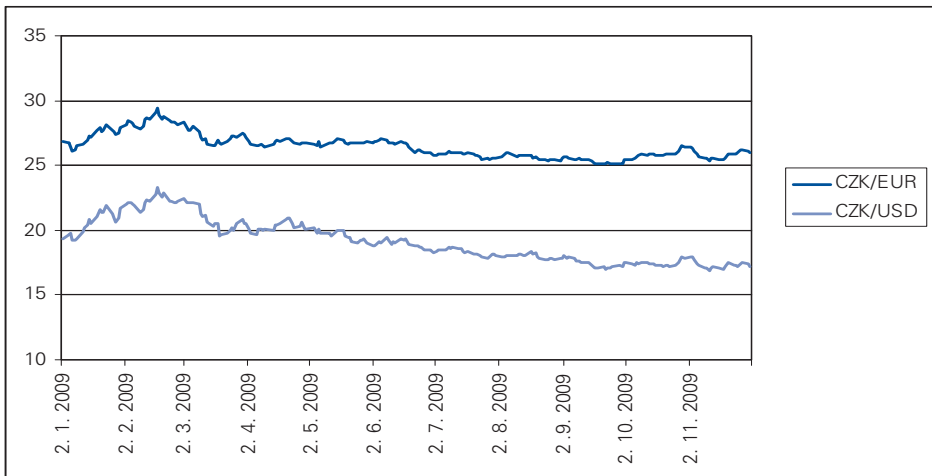
The Act on Foreign Exchange allows:

- a resident without a foreign exchange permit to undertake contractual obligations towards a non-resident and to fulfil the resulting commitments in either Czech or foreign currency;
- a resident to acquire foreign currency or other rights denominated in foreign currency, to acquire property abroad and to export and import Czech and foreign currency; and
- a non-resident to purchase foreign currency or other rights denominated in foreign currency in exchange for Czech currency or vice versa, to acquire real estate (subject to restrictions) and to import and export Czech and foreign currency.

The above general clauses are restricted by certain qualifications. Usually the exchanges are subject to the duty to notify the CNB.

The role of foreign exchange regulation as an important means of preventing or detecting money laundering is constantly growing.

Figure 4: Value of the Czech crown during 2009 (CZK/EUR and CZK/USD)²⁰



²⁰ Source: Czech National Bank

The Czech crown did not fluctuate significantly in comparison to the US dollar and the euro. The volatility of the Czech currency was higher mainly during the first quarter of 2009. In Q2 and Q3 the Czech currency appreciated slightly against the US dollar, the exchange rate against the euro was mainly stable.

Repatriation of capital and profit

The Czech currency is allowed to float freely, and is convertible outside the Czech Republic. Czech companies may freely repatriate both current year profits and retained earnings in whatever currency they desire. However, they should follow the minimum capital requirements imposed by the CNB. Branches of foreign banks do not have such limitations, as the capital is raised and monitored centrally.

The following types of payments from a Czech company to its foreign parent may be transferred abroad freely, subject to the appropriate withholding taxes:

- dividends,
- interest,
- charges for intangible property (e.g. royalties and know-how fees),
- management fees,
- liquidation balance.

Chapter 8

Employment policy

General

The Czech Republic has a skilled and educated labour force, and the literacy rate is above 98 percent.

Employment law is governed by the Labour Code and numerous government decrees. Where an employee from another EU member state is sent by an employer to work in the Czech Republic as part of the transnational provision of services, the Czech Labour Code regulations shall apply to:

- maximum working hours and the minimum length of rest periods;
- the minimum annual leave entitlement;
- the minimum wage and overtime rates;
- occupational safety and health;
- working conditions for pregnant employees;
- working conditions for female employees;
- equal treatment of male and female employees;
- prohibition of discrimination;
- conditions of work with regard to employment agencies.

However, the Czech Labour Code shall not apply if the provisions of the home EU country legislation are more advantageous for the employee.

The maximum working week is 40 hours. The standard working week is Monday to Friday from 8:00 to 16:30, although manufacturing companies may start earlier.

The average retirement age is generally 60 for women, or earlier, depending on the number of children raised, and 62 for men. The minimum retirement age for men and

women will gradually be raised until 2030, when the retirement age will range from 62 to 64 for women, depending on the number of children raised, and 65 for men, childless women and mothers with one child.

Employment contracts

Employers are required to conclude written employment contracts with their employees. Employers must inform employees about their rights and duties, and the salary resulting from the contract. The contract must describe the type of work, the date that the employee will commence work, and where the work will be performed. Trial periods cannot be longer than three months and must be agreed in writing.

Employment contracts are valid for an indefinite period unless explicitly stated in a contract. A fixed-term employment contract may be concluded for up to two years.

These rules do not apply to fixed-term employment contracts concluded between employment agencies and their employees concerning work to be carried out for another employer. Employment contracts with an agency must be concluded in writing. Employees can only be assigned to work for another employer with their written consent, entitling the other employer to organise and inspect the employee's work.

An employee may have more than one employment contract concurrently. The rights and duties ensuing from each are unrelated.

An employment contract concluded for an indefinite period or fixed term may be terminated as follows:

- by agreement,
- by notice,
- by immediate cancellation,
- by cancellation during the trial period.

Cancellation by agreement must be made in writing.

The employer or the employee may cancel a contract by giving written notice. The notice period commences on the first day of the calendar month following the date on which the notice was delivered to the other party. The notice period for the employer

and the employee is at least two months, and the employee can give notice without stating a reason.

When an employer terminates an employment contract, it must be for one of the following reasons:

- a) the employer (or a department of the employer) is being liquidated or is ceasing to carry on business;
- b) the employer (or part of the company or organisation) is relocating;
- c) organisational changes;
- d) the employee is not able to work for long-term health reasons;
- e) the employee is not sufficiently qualified;
- f) serious disciplinary breaches by the employee.

Where an employment contract is terminated for any of the reasons under letters a) to c), the employer is obliged to pay the employee a minimum of three months' severance pay.

Specific termination conditions apply in respect of disabled persons, pregnant women and employees caring for minors. Specific termination conditions, severance pay and other conditions may also be included in a collective agreement if in force.

Compensation for redundancy is legally set at a minimum of three months' salary. In practice, the amount varies depending on the company, whether collective agreements have been concluded, etc.

During the trial period, the employment contract may be cancelled by either side for any reason or without any reason being given. Cancellation must be in writing and delivered at least three days before the termination date.

Mass layoffs

If an employer terminates employment relationships with a certain number of employees as defined in the Labour Code, for the specific reasons set out above under letters a) to c), within a period of 30 calendar days, this is considered a mass layoff. A two-month notice period applies for mass layoffs. However, the employment relationship of an employee who is affected by a mass layoff shall not be terminated

earlier than 30 consecutive days after the day the employer sent a report on the final decision on the layoffs to the local labour office (see below), unless the employee does not insist on extension of the termination period.

At least 30 days before termination notices are issued, the employer must inform a trade union or work council in writing and hold negotiations with either of these bodies to mitigate the scope and effects of the redundancies. If there is no union or work council, the employer must take the same steps in relation to all affected employees. At the same time, the employer must also inform in writing the local labour office of the redundancies.

The employer must submit a report on the final decision of the redundancies to the labour office. It must contain the results of negotiations with the union or work council and the final number and arrangement of the redundancies.

Trade unions

Trade unions engage in collective bargaining at a national level. A Tripartite Council, including representatives from trade unions, employers and the government, meets annually to discuss labour issues.

Employment confirmation

Employers have a duty to provide proof of employment (*potvrzení o zaměstnání*) to all employees, or their new employer, upon termination of an employment contract. It must contain information regarding the duration of employment, social security and health insurance contributions paid, the employee's obligations to the company, and details of the employee's annual salary for the employment period.

Where an employee requests employer to provide him or her with a reference (*pracovní posudek*), the employer is obliged to provide it within a period of 15 days, but not earlier than two months before the end of the employee's employment.

Holidays

An employee is entitled to holiday pay if the employment contract lasts for at least 60 continuous days during a calendar year. Where the contract lasts for less than a year,

one-twelfth of the annual holiday is accrued for each calendar month of continuous employment with the same employer.

The minimum holiday period is four weeks per annum, unless lengthened by a collective bargaining agreement or internal regulations. State employees are entitled to five weeks per annum. Holiday pay is calculated on the basis of an employee's average monthly salary.

Social security and health insurance

There are two major schemes to which both the employee and the employer contribute: social security and health insurance.

Payments from the social security insurance system typically include:

- pensions,
- cash benefits:
 - a) sick leave,
 - b) benefit for a family member's health treatment,
 - c) parental benefits,
 - d) social benefits,
 - e) death benefits,
 - f) maternity benefits.

Chapter 9

Corporate transactions

During the 1990s, corporate transactions became a feature of the Czech legal environment, making it possible for entrepreneurs and business persons to expand or restructure their business activities in the Czech Republic. This was a hugely important development, particularly in relation to its accession to the EU, as a result of which the Czech Republic is obliged to implement the legal regulations of the EU, including those allowing cross-border mergers. The process of mergers and acquisitions itself is primarily regulated by the Commercial Code, the Act on Takeover Bids, the Act on Transformations of Business Companies and Co-operatives, accounting and tax laws, anti-monopoly regulations, and a number of special regulations applicable to specific sectors, such as banking, insurance and other financial services.

Privatisation

A number of enterprises in sectors such as electricity and transport are awaiting privatisation by sale to strategic investors. The privatisation process is initiated by a government decision. All transactions are subsequently carried out by the relevant ministry, generally through a tender.

Ownership of real estate

The five-year transition period agreed by the Czech Republic upon EU accession ended on 1 May 2009. The real estate market was therefore completely liberalised, opening up to individuals and companies from other EU states. Currently, only acquisitions of agricultural land and forests continue to be regulated for the remainder of the seven-year transitional period, with the possibility of a three-year extension.

Foreign individuals who are EU citizens gained the freedom to directly acquire real estate. With a few exceptions, non-EU citizens cannot acquire real estate freely.

The freedom of foreign individuals, including EU citizens, is also restricted in respect of acquiring farmland and forest.

Foreign corporations registered in the EU are entitled to acquire real estate in the Czech Republic, with the exception of agricultural land and forests. Non-EU registered corporations may purchase real estate only if they have a branch incorporated in the Czech Republic. However, the restrictions concerning non-EU citizens and corporations are interpreted by lawyers in different ways.

Acquisition and disposal of Czech legal entities

Foreign private and legal entities are permitted to own a business or hold shares in companies, and they can acquire and sell up to 100 percent of the share capital of a limited liability or joint-stock company. Likewise, they can also participate in companies with other legal forms, but the transfer of an ownership interest in a limited liability company must be recorded in the Commercial Register. The acquisition of shares in a joint-stock company is not restricted, although the shares of certain joint-stock companies are registered with the Central Register of Securities (i.e. shares that do not exist in paper form but whose details and ownership is recorded). The ownership of such shares changes when the acquisition is recorded in the Central Register. In respect of shares traded on the regulated securities market (Prague Stock Exchange and RM System) in the Czech Republic or another EU member state, the acquirer is obliged to notify the company (the issuer) and the Czech National Bank (the supervisory body of the capital market) if its share of the company's voting rights exceeds a certain level. In addition, if a shareholder acquires a minimum of 30 percent of voting rights and actually controls the company, it is obliged to bid for the shares of the remaining shareholders.

Purchase of an enterprise

An acquisition can also be made by purchasing an enterprise or part of it, in which the buyer acquires all rights, assets and liabilities connected with running the business. The sale and purchase agreement associated with the acquisition must be approved by the general meeting or shareholders of the company before the transaction is signed.

Contribution to a company

Another way of securing a share in a business is by making a financial or a non-monetary contribution, where the general meeting of the company must decide on a new share issue. The increase is registered at the commercial court. In the case of a non-monetary contribution, an independent valuation of the investment must be submitted by an independent expert, with some exceptions. If the company statutory body so decides, a valuation can also be submitted by an independent and generally accepted expert.

Transformation of a company (merger, transfer of assets to a shareholder, demerger and change of legal form)

In Czech legislation, mergers come under the category of “transformation of a business”, which also includes the demerger of the company, transfer of assets to a shareholder or any change in the company’s legal form. Transformation of a business is possible even if the company is in liquidation or insolvency proceedings. The transformation can be undertaken as a national or cross-border transaction with legal entities registered in other EU or European Economic Area countries. If a company has the legal form of a European Company (Societas Europea), business transformations can also involve foreign companies.

Probably the most frequent form of transformation is merger by acquisition: one of the companies carries on its activities and the other ceases to exist, and its assets and liabilities are transferred to the successor company. Another option is merger by the formation of a new company: all of the original companies cease to exist, and their assets are transferred to a new successor company.

From a financial point of view, an important issue is the tax losses carried forward in respect of wound up companies. Under the legislation valid prior to 1 May 2004, these losses could not be transferred to the successor company. However, following the Czech Republic’s accession to the EU, tax losses can now be carried forward. The earliest taxation period for which losses can be carried forward is the period when the Accession Treaty between the Czech Republic and the EU came into force (i.e. on 1 May 2004). Losses assessed in previous taxable periods cannot be carried forward.

Mergers are carried out on the basis of merger projects, which must be approved in advance by general meetings. Share exchange ratios and other possible arrangements after the merger are key factors in merger projects. The merger becomes legally effective on the date it is recorded in the Commercial Register. However, from a tax and accounting point of view, the companies are considered a single entity as of the merger date, which precedes all necessary steps and decisions in relation to the merger. In some cases, subject to the agreement of all shareholders or partners, the merger procedure can be significantly simplified. A new option has been created for mergers of joint-stock companies, allowing the voluntary buyout of the other shares if the successor company owns more than 90 percent of the merging company's registered capital. Should the legal status of shareholders of any participating company be worsened as a result of the merger, the successor company has an obligation to buy out these shareholders under certain circumstances.

Companies with a different legal status can also merge, and the merger may involve more than two entities.

A number of special regulations apply to cross-border mergers. An important condition is that the merger procedure must be regulated in the same way as in the legal systems of the countries in which the participating companies are registered. The preparatory phase of the cross-border merger is carried out in accordance with the laws to which each of the participating companies is subject, and the completion process is governed by the laws of the country where the successor company has its registered office.

The transfer of assets to a shareholder is a legal form of company transformation, where the shareholder owning more than 90 percent of the company's registered capital may transfer the company's assets to itself, provided it has obtained the consent of the general meeting; at the same time it has the duty to fairly compensate all other minority shareholders.

A company can be demerged (divided) through: (i) demerger by the formation of new companies; (ii) "demerger by acquisition"; (iii) spin-off connected with the formation of new companies; and (iv) spin-off connected with acquisition, or a combination of the options mentioned in either (i) or (ii), or in (iii) and (iv). Upon demerger of the company by the formation of new companies or by acquisition, the company being demerged

ceases to exist, without liquidation, while it does not cease to exist upon demerger by spin-off.

Czech legislation allows a company to change its legal status, whereby the company does not cease to exist, but only changes its internal legal position and structure.

Public bid for purchase or exchange of participating securities issued by a joint-stock company

If someone (entity or individual) intends to make an offer to more than 100 shareholders or the volume of requested securities exceeds 1 percent of the issue, the offer must be made in the form of a public bid. If the public bid is required by law, the offer must correspond to the value of the participating securities. If the securities are traded on the regulated market, the bidder must submit an offer and provide evidence to the Czech National Bank that the consideration is adequate.

Takeover bids

Voluntary takeover bids

For joint-stock companies traded on the regulated market, an investor can make a public offer to the shareholders if the bid allows it to gain control over the company. The bid is binding for no less than four weeks. If it is binding for more than 10 weeks, the investor shall notify the shareholders two weeks before the period expires. All shareholders must be treated equally; the statutory bodies of the target company shall maintain neutrality and are obliged to inform trade unions or other employee representatives. A new breakthrough rule has been introduced, whereby the restriction regarding the transferability of listed securities may be lifted during the takeover bid period. During the bid's validity period the bidder can increase the consideration or prolong the validity. In addition, another person may make a counter bid during the validity period of the first bid. Takeover bids may be published only with the prior consent of the Czech National Bank.

The Act on Takeover Bids also deals with a situation where the target company is registered in the Czech Republic but its shares are traded on the foreign regulated market, and where a target company has its registered office in a foreign country but its shares are traded on the Czech regulated market.

Obligatory takeover bids

An investor acquiring a minimum of 30 percent of the voting rights in the target company traded on the regulated market and who actually controls the company must offer to buy out other shareholders within 30 days of the acquisition (“obligatory takeover bids”). The consideration can be provided in cash, shares or a combination of both. The minimum consideration must correspond to the highest price for which the investor acquired shares in the target company in the 12 months before the takeover bid obligation arose. If such a price cannot be determined, the minimum consideration must correspond to the weighted average of prices for which the shares were traded on the regulated market during the six months before the obligation arose. An obligatory takeover bid may be published after its approval by the Czech National Bank.

Right to buy out participation securities (squeeze out)

A shareholder with participation securities representing more than a 90 percent share of the registered capital of a joint-stock company (“majority” shareholder) is entitled to ask the board of directors to convene the general meeting to decide on the transfer of all the other participating securities owned by minority shareholders to it (a “squeeze out of minority shareholders”). The general meeting of the company approves the squeeze out by paying them adequate compensation on the basis of an expert valuation, or another reasonable consideration if a valuation is not required. An expert opinion is not required if the target company’s shares are traded on the regulated market. In such a case, the justification of the consideration is subject to approval by the Czech National Bank.

Regulation

With regard to mergers and acquisitions, the interests of minority shareholders are protected because companies are obliged to ensure early notification and, for the majority of transactions, the opinion of an independent expert is required to determine whether the parameters of the transaction – in particular the price – are fair and reasonable. In the Czech Republic, mergers and acquisitions are also regulated by special legal measures. For example, for a transaction to come into effect in the banking and insurance sector, the appropriate authorities (Czech National Bank and the Ministry of Finance) must approve a contract on the merger or acquisition of a bank or insurance company.

Mergers and acquisitions also fall within the jurisdiction of the Office for the Protection of Competition. Its permission is required if:

- the aggregate net turnover of the participants in a transaction in the Czech Republic for the prior accounting period exceeded CZK 1.5 billion and at least two of the merging companies each recorded a net turnover of more than CZK 250 million in the Czech Republic for the same period, or
- one or more of the participants in the transaction had a net turnover in the Czech Republic of at least CZK 1.5 billion in the previous accounting period, and for the same period the worldwide net turnover recorded by the other participant exceeded CZK 1.5 billion.

APPENDIX

Useful addresses

Czech Government Offices

Ministry of Finance of the Czech Republic

Letenská 15
118 10 Prague 1

Tel.: +420 257 041 111
Fax: +420 257 042 788
www.mfcr.cz

The Ministry of Industry and Trade

Na Františku 32
110 15 Prague 1

Tel.: +420 224 851 111
Fax: +420 224 811 089
www.mpo.cz

Ministry for Regional Development of the Czech Republic

Staroměstské náměstí 6
110 15 Prague 1

Tel.: +420 224 861 111
Fax: +420 224 861 333
www.mmr.cz

Czech National Bank

Na Příkopě 28
115 03 Prague 1

Tel.: +420 224 411 111
Fax: +420 224 412 404
www.cnb.cz

CzechInvest (Czech Agency for Foreign Investment)

Štěpánská 15
120 00 Prague 2

Tel.: +420 296 342 500
Fax: +420 296 342 502
www.czechinvest.org

Financial Institutions

LBBW Bank CZ a.s.

Vítězná 1/126
150 21 Prague 5

Tel. : +420 233 233 233
Fax : +420 233 233 299
www.lbbw.cz

Citibank a.s.

Evropská 178
166 40 Prague 6

Tel.: +420 233 061 111
Fax: +420 233 061 617
www.citibank.cz

COMMERZBANK Aktiengesellschaft

Jugoslávská 1
120 21 Prague 2

Tel.: +420 221 193 111
Fax: +420 221 193 699
www.commerzbank.cz

Czech Export Bank, a.s.

Vodičkova 34
111 21 Prague 1

Tel.: +420 222 841 100
Fax: +420 224 226 162
www.ceb.cz

Česká spořitelna, a.s.

Olbrachtova 1929/62
140 00 Prague 4

Tel.: +420 261 071 111
Fax: +420 261 073 032
www.csas.cz

Československá obchodní banka, a.s.

Radlická 333/150
150 57 Prague 5

Tel.: +420 224 111 111
Fax: +420 224 119 560
www.csob.cz

Deutsche Bank Aktiengesellschaft Filiale Prag

Jungmannova 34/750
110 00 Prague 1

Tel.: +420 221 191 111
Fax: +420 221 191 411
www.db.com/czechrepublic

GE Money Bank, a.s.

Vyskočilova 1422/1a
140 28 Prague 4

Tel.: +420 224 441 111
Fax: +420 224 442 901
www.gemoney.cz

HSBC Bank plc

Gestin Premier Centrum
V Celnici 1040/5
110 00 Prague 1

Tel.: +420 225 024 121
www.hsbc.cz

ING Bank N. V.

Nádražní 344/25
150 00 Prague 5

Tel.: +420 257 471 111
Fax: +420 257 473 555
www.ing.cz

J&T BANKA, a.s.

Pobřežní 297/14
186 00 Prague 8

Tel.: +420 221 710 111
Fax: +420 221 710 211
www.jtbank.cz

Komerční banka, a.s.

Na Příkopě 33
114 07 Prague 1

Tel.: +420 800 111 055
www.kb.cz

mBank ČR

Nile House
Karolinská 654/2
186 00 Prague 8

Tel.: +420 844 777 000
www.mbank.cz

Oberbank AG

I. P. Pavlova 5
120 00 Prague 2

Tel.: +420 224 190 100
Fax: +420 224 190 150
www.oberbank.cz

PPF banka a.s.

Evropská 2690/17
160 41 Prague 6

Tel.: +420 224 175 888
Fax: +420 224 175 980
www.ppfbanka.cz

Raiffeisenbank a.s.

Hvězdova 1716/2b
140 78 Prague 4

Tel.: +420 225 541 111
Fax: +420 234 405 633
www.rb.cz

UniCredit Bank Czech Republic, a.s.

Na Příkopě 20
111 21 Prague 1

Tel.: +420 221 112 111
Fax: +420 221 112 132
www.unicreditbank.cz

Volksbank CZ, a.s.

Na Pankráci 129
140 00 Prague 4

Tel.: +420 800 133 444
Fax: +420 221 969 951
www.volksbank.cz

Business Organisations

American Chamber of Commerce in the Czech Republic

Dušní 10
110 00 Prague 1

Tel.: +420 222 329 430
Fax: +420 222 329 433
www.amcham.cz

British Chamber of Commerce Czech Republic

IBC, Pobřežní 3
186 00 Prague 8

Tel.: +420 224 835 161
Fax: +420 224 835 162
www.britcham.cz

Canadian Chamber of Commerce in the Czech Republic

Klimentská 46
110 02 Prague 1

Tel/Fax.: +420 225 000 345
www.gocanada.cz

Czech-German Industrial Chamber of Commerce

Václavské náměstí 40

Tel.: +420 224 221 200

110 00 Prague 1

Fax: +420 224 222 200

www.dtihk.cz

Economic Chamber of the Czech Republic

Freyova 27

Tel.: +420 266 721 300

190 00 Prague 9

Fax: +420 266 721 690

www.komora.cz

Enterprise Ireland Prague

Tržiště 13

Tel.: +420 257 199 621

118 00 Prague 1

Fax: +420 257 532 224

www.enterprise-ireland.com

Japan External Trade Organization, Praha

Pařížská 11/67

Tel.: +420 224 814 971

110 00 Prague 1

Fax: +420 224 813 998

www.jetro.go.jp

Netherlands Chamber of Commerce in Prague

Zlatý Anděl, Nádražní 25

Tel.: +420 257 473 740

150 00 Prague 5

Fax: +420 257 473 744

www.nlchamber.cz

Swiss-Czech Chamber of Commerce

Na Pankráci 1062/58

Tel.: +420 222 516 614

140 00 Prague 4

Fax: +420 222 513 685

www.hst.cz

Taipei Economic and Cultural Office, Prague, Czech Republic

Evropská 33c/2590

Tel.: +420 233 320 720

160 00 Prague 6

Fax: +420 233 322 944

www.roc-taiwan-cz.com

Italian-Czech Chamber of Commerce and Trade in the Czech Republic

Čermákova 7
120 00 Prague 2

Tel.: +420 222 015 300
Fax: +420 222 015 301
www.camic.cz

Joint Czech-Belgium-Luxembourg Chamber of Commerce in the Czech Republic

Thámova 20
186 00 Prague 8

Tel.: +420 221 890 738
Fax: +420 221 890 768
www.cblchamber.cz

CCFT – FČOK French-Czech Chamber of Commerce

IBC, Pobřežní 3
186 00 Prague 8

Tel.: +420 224 833 090
Fax: +420 224 833 093
www.ccft-fcok.cz

International Chamber of Commerce

Thunovská 12
118 00 Prague 1

Tel./Fax: +420 257 217 744
www.icc-cr.cz

The Slovak-Czech Chamber of Commerce

Ovocný trh 572/11
110 00 Prague 1

Tel.: +420 226 002 302
www.scok.cz

Czech-Arabian Chamber of Commerce

Freyova 27/82
190 00 Prague 9

Tel.: +420 773 131 858
www.czaok.cz

Czech-Polish Chamber of Commerce

Janáčkova 10
702 00 Ostrava

Tel.: +420 596 612 230
Fax: +420 596 612 231
www.opolsku.cz

Czech-Israeli Chamber of Commerce

Václavské náměstí 802/56

Tel.: +420 224 032 161

110 00 Prague 1

Fax: +420 224 032 162

www.ciok.cz

Czech-Mongolic Chamber of Commerce

Nad Vršovskou horou 88/4

Tel.: +420 728 730 395

101 00 Prague 10

www.cemok.org

Nordic Chamber of Commerce in the Czech Republic

Václavské náměstí 51

Tel.: +420 774 123 370

110 00 Prague 1

Fax: +420 226 015 885

www.nordicchamber.cz

Czech-Moroccan Chamber of Commerce

Václavské náměstí 802/56

Tel./Fax: +420 224 032 519

110 00 Prague 1

Chamber of the Czech-Portuguese cooperation

Bryksova ul. 720

Tel.: +420 281 917 909

198 00 Praha 9

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