

# Tax & Business News

Tax, accounting, advisory and assurance newsletter

03|2009

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Dear Business Partners,

Welcome to the April edition of Tax & Business News in which we bring you updates and news from the area of tax, accounting and financial advisory. The main theme of this month's edition is change, principally in the area of tax, and we highlight the more important tax changes we believe will impact businesses in the Czech Republic. Most of the changes we refer to aim to help businesses and, at the same time, stimulate the economy. This is a common theme right across Europe at the moment, where many different approaches are being adopted. Of course, it is difficult at this stage to assess the extent to which the efforts being made by Governments to stimulate business activity will be effective but what is certain is that being prepared for the changes we have highlighted is the best way to ensure that your business takes full advantage and avoids any potential pit falls. Undoubtedly, the tax changes highlighted below will provide significant advantages for certain businesses and I hope that in bringing them to your attention you find this edition of Tax & Business News helpful.

Yours sincerely,  
Peter Skelhorn

Partner, Tax and Legal Services, PricewaterhouseCoopers Czech Republic

## Deduction on the social security insurance contributions

A new government draft law on social security insurance contributions was submitted to Parliament. The purpose of this draft law is to establish a deduction on the social security insurance contributions paid by employers.

The employer would be entitled to apply the deduction to social security insurance contributions for each employee whose social security insurance assessment base is lower than 1.15 \* the average wage and whose employment lasts the whole calendar month.

The amount of the deduction on social security insurance contributions for each employee would be calculated as 3.3% of the difference between 1.15 \* the average wage and the actual social security insurance assessment base of an employee, but to a maximum of 25% of the social security insurance assessment base of each employee.

The deduction on social security insurance contributions can only be applied until the due date for social security insurance contributions for the calendar month to which the deduction relates. The deduction cannot be applied retroactively.

According to the draft law, this deduction should be valid until the end of 2011.

### Extraordinary deduction

An extraordinary deduction on social security insurance contributions could be applied by the employer starting the month when the new enactment is effective.

The extraordinary deduction would be calculated as a sum of all the above-mentioned 'regular' deductions from the social security insurance contributions for each calendar month of 2009 before the effective date of the enactment. It would be something like a 'compensative' deduction for the part of 2009 when the employer could not yet apply the 'regular' deduction.

The deduction calculation would only reflect those employees whose employment lasts until the final day of the calendar month, when the enactment becomes effective.

### Discounts when hiring certain employees

In addition to the deduction described above, the Ministry of Labour and Social Affairs also published another amendment to the law and introduced another type of deduction on social security insurance contributions. This type of deduction is intended for employers who would hire, for example, students, people older than 55, people taking care of small children or handicapped people. This deduction would take effect as at 1 January 2010.

According to actually available information, similar deductions on health insurance contributions are not planned.

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## Parliament discusses important amendments of several tax laws

At a meeting started on 17 March 2009, the Chamber of Deputies discussed amendments to the income tax, social security insurance and investment incentives laws, from which we choose the most important news:

### Shortening of depreciation period

As a tool to increase the sale of new machines and devices, the amendment of the income tax act brings an opportunity to shorten the depreciation period for new tangible fixed assets acquired in the period from 1 January 2009 to 30 June 2010:

- Shortening of the depreciation period relates to the fixed assets classed into the first two depreciation groups
- The depreciation will be asserted on a monthly basis
- For property in the first depreciation group, the depreciation period will be shortened from 3 years to 12 months
- For the fixed assets in the second depreciation group, the depreciation period will be shortened from 5 years to 24 months, where in first 12 months will be depreciated 60% of input price and, in the next 12 months, the remaining 40% of input price.
- The technical appreciation of the fixed assets depreciated by the above-mentioned approach will not increase their input price and will be depreciated separately as another tangible property.
- The taxpayers have the opportunity to use current methods of depreciation.
- It will be possible to appropriately shorten the rent period where the fixed assets are acquired through financial leasing.

### Changes in incentive investment regulation

The amendment of the incentive investments act significantly changes the entire incentive investment system, while it revokes some of the current forms of incentives completely:

- Cancelling grants for creating new jobs and for the training and re-training employees
- Cancelling incentives in the form of the transfer of technical equipment and remittance of estates for discounted prices
- The only incentive left is tax relief.
- Launching the new form of expense specification, which can be supported by the incentives (in addition to specified investment expenses, it will be possible to include the value of salary expenses for the berth created by investment, to the extent of an incentive discount)
- Cancelling incentives for the processing industry, from now on the incentives (tax relief) will only be provided to technological centres and the centres of strategic services.

The last term for submitting an incentive investment request for the processing industry is in accordance with the current modification, 29 days after the declaration of the law amendment.

The deadline for the submission of the applications in accordance with the proposed legal adjustment is 30 June 2011 (that means, after this date there will be no new projects which may be granted incentives).

The current tax relief for research and development projects in the income tax act stays the same. The amendment also does not change the conditions for investment projects, which already obtained incentives in accordance with current legal adjustment.

The motion of above-mentioned amendments must be first of all discussed in the Chamber of Deputies, then approved by the Senate and signed by the President.

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## Changes in VAT

### Accelerated repayment of VAT refund

As help for tax payers affected by the economic slowdown, the Czech Ministry of Finance has decided to shorten the period for the repayment of VAT refunds if VAT returns are submitted electronically.

Under the Czech VAT Act, the Tax Authorities refund excess VAT deductions to VAT payers automatically, no later than 30 days after the VAT assessment. If the Tax Authorities have any doubts about the correctness, truthfulness or completeness of the filed VAT return, they can start proceedings. In such cases, the period for repayment of the VAT refund is extended.

If a VAT return is submitted electronically and the Tax Authorities do not start proceedings, according to the new instruction of the Ministry of Finance, the VAT refund should be repaid by the Tax Authorities within 15 days after the tax assessment.

VAT returns can be filed electronically by using [the web pages of the Ministry of Finance](#). You can submit VAT return electronically in two ways:

1. With an advanced electronic signature with qualified certificate (in Czech: Zaručený elektronicky podpis s kvalifikovaným certifikátem)
2. Without any electronic signature

If the VAT return is submitted electronically with an advanced electronic signature with qualified certificate, the VAT return is filed the moment it is submitted. If the VAT return is submitted electronically without any electronic signature, the VAT return is valid only if the Tax Authorities receive a signed E-report in paper form within 3 days after the electronic submission of the VAT return. The E-report is generated automatically after submission of the VAT return on the web pages mentioned above.

The accelerated repayment of VAT refunds can be used to VAT returns submitted electronically for all VAT returns from January 2009.

### Government approved EU agreement on reduction of VAT rates

In order to support the economy and keep employment high in related economic segments the Czech government approved the European Council agreement proposing a permanent reduction of VAT rates for selected labour intensive services.

The initiative relates especially to services such as home care of children, the elderly and handicapped, books on any type of media, home cleaning services, catering in restaurants, small repairs, hairdressing services and the reconstruction and renovation of flats and residential houses.

The proposal needs formal approval by the European Council during its spring session, publication of the amendment to the VAT directive and approval by the parliaments of particular EU member state.

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## Input VAT deduction for passenger cars – approved and signed by the President

A VAT Act amendment that allows claiming an entitlement to input VAT deduction on the purchase of passenger cars used for business activities, regardless of car category, was approved by the Czech Senate on 26 March 2009. The Act was signed by the Czech President the very next day, on 27 March 2009. It is expected the amendment will be published on 1 April 2009 in the Collection of laws and will come into force the same day. This means that the first entitlement to a VAT deduction for passenger cars could be claimed in the April 2009 VAT return, or alternatively in the 2Q VAT return for quarterly VAT payers.

According to the transitional provisions of the amendment, it will be possible to claim an entitlement to a VAT deduction only for passenger cars purchased after the effective date of the amendment.

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## Amendment to the Income Taxes Act

Effective from 1 April 2009, the new thin capitalization rules apply pursuant to of the Income Taxes Act<sup>1</sup> which limits the tax deductibility of the financial costs (i.e. interest and some other related costs) only to the loans and credits received from the related parties (including so-called "back-to-back" loans) in the amount of four times (or six times in case of banks and insurance companies) taxpayer's own equity. Similarly, the new rules also apply to the recharging of tax non-deductible interest which becomes tax deductible pursuant to Income Tax Act<sup>2</sup> (provided the recharging is made in the same tax period), or the income from the recharging is not taxable pursuant to the Income Tax Act<sup>3</sup> (provided the recharging is made in the following tax periods).

These new rules may be applied also backwards for the tax periods beginning in the year 2008 either in the regular tax return (where the deadline for its submission has not expired yet) or through the additional tax return. That means, if the deadline for the tax return expires today, the new rules may already be applied (although they will become effective starting tomorrow).

Even though the temporary provisions to the Amendment state, that beginning by the year 2010 the new thin capitalization rules will apply to all financial costs from all loans and credit, it is obvious that the lawmaker's intention is to limit the restrictions only to the related-party loans and credits.

<sup>1</sup> Income Taxes Act, No. 586/1992 Coll., Section 25(2)(w)

<sup>2</sup> Income Taxes Act, No. 586/1992 Coll., Section 24(2)(zc)

<sup>3</sup> Income Taxes Act, No. 586/1992 Coll., Section 23(4)(e)

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## Zero customs duty on LCD monitors with video connectors

There have been several pieces of positive news recently in connection with customs duty on LCD monitors. The latest concerns the case of the European Court of Justice ("ECJ") according to which it is possible to apply a 0% customs duty on LCD monitors with both video connectors and connectors used in an automatic data-processing ("ADP") machine. Until now, these LCD monitors were classified as video monitors and carried a 14% customs duty.

The ECJ has considered the situation where LCD monitors with video connectors (D-Sub; DVI-D; USB; S-video and composite video) have been classified as video monitors and a 14% customs duty has been applied. However, the ECJ has decided that the fact that an LCD monitor can display signals from other sources as well as from ADP machines does not exclude it from the 0% customs duty. To determine if an LCD monitor is indeed of a kind principally used in an ADP machine (with the 0% customs duty), the authorities must consider all criteria and to not automatically set the 14% customs duty.

All importers who import LCD monitors that are capable of displaying signals from both ADP machines and other sources and which also meet other criteria may argue that the LCD monitors should be liable to the 0% customs duty. Furthermore, these importers can claim a refund for any customs duty paid on such imports for the last three years. We would be pleased to help you determine if the customs duty was applied correctly and to help you with a refund claim.

PricewaterhouseCoopers has a wide network of customs specialists who will be pleased to assist you in any EU Member State with customs duty and with reclaims.

**H** Will the changes affect your company? Can these changes be beneficial to your business? If you are interested in obtaining more information about customs tariffs, please contact:

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## The Government approved an amendment of environmental taxes

One year after the introduction of environmental taxes (i.e., tax on natural gas and some other gases, tax on solid fuels and tax on electricity), the Czech Ministry of Finance has analysed the problems that arose during the introduction thereof and has prepared an amendment to eliminate problems that have been identified. The amendment was passed by the government on 9 March 2009 and should be effective from 1 July 2009.

The most significant changes relate to the exemptions. A positive impact is the extension of exemptions related to boiler houses used for household heating and those related to combined heat and power generation. On the other hand, the amendment will markedly limit exemptions related to the losses of electricity in distribution and transmission networks.

The amendment also classifies some general terms used in the legislation and some administrative obligations on the part of environmental tax payers. The amendment also introduces other important changes related to tax points, correction of tax documents and tax exemptions.

A new specification regarding tax points relates to the illegal taking-off from distribution and transmission networks, to on-sales of energy products made between final consumers and to the delivery of energy products abroad for direct consumption.

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## Most important changes in IFRS for this year

If you are preparing financial statements in accordance with the International Financial Reporting Standards (IFRS), you should apply a number of changes in the IFRS valid from 1 January 2009. You can briefly familiarise yourself with the most important changes and you can read more details in next issues of Tax&Business News.

The International Accounting Standards Board (IASB) revised the [IAS 1 – Presentation of Financial Statements](#). Revised IAS 1 requires that all changes in equity resulting from transactions other than those with the owners be presented in a new Statement of comprehensive income (presented in the Statement of changes in equity before the revision). Net profit is only a subtotal in this statement. An entity has to present a Statement of financial position (a Balance sheet before the revision) as at the beginning of the earliest comparative period when the entity makes a retrospective restatement or reclassifies comparable items or applies an accounting policy retrospectively.

[IAS 23 – Borrowing Costs](#) (revised) eliminates the possibility of recording borrowing costs directly as an expense. Revised IAS 23 allows capitalisation of borrowing costs, i.e. interest and other costs that an entity incurs in connection with the borrowing of funds for the acquisition of qualifying assets.

The IASB also prepared a new standard [IFRS 8 – Operating Segments](#) which set out requirements for the disclosure of information about an entity's operating segments and also about the entity's products and services, the geographical areas in which it operates, and its major customers. IFRS 8 replaces IAS 14 – Segment Reporting and the main objective is to make preparation of operating segments disclosure easier for the reporting entity and, simultaneously, to provide high quality informations as to enable users of its financial statements to make their decisions.

The International Financial Reporting Interpretations Committee (IFRIC) prepared few new interpretations from which we would like to mention IFRIC 13 and IFRIC 15. Interpretation [IFRIC 13 – Customer Loyalty Programmes](#) treats recognition of revenues when granting loyalty awards to customers. Interpretation [IFRIC 15 - Agreements for the Construction of Real Estate](#) should help reporting entities identify transactions that include construction contracts and provide guidance on how to account for revenues from these contracts (whether to apply IAS 11 or IAS 18).

**i** As a result of the annual improvements process a range of minor amendments in 25 IFRS standards became effective as at 1 January 2009. If you are interested in more detailed information about changes in IFRS and their impact for your company, contact:

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## Professional Training

PwC Business Academy is committed to the social and economic development of the Czech Republic. Through building the knowledge, skills and attitudes of Czech business leaders, we aim to support the business and economic growth in the country. Czech business and economy requires highly competent and motivated human capital – PwC Academy helps develop that capital by providing knowledge leadership and training.

We are offering the following seminars for the up-coming months:

### **3 April 2009 IFRS News and Updates**

This seminar is designed for professionals, who are familiar with the IFRS standards and need to obtain the information about the latest changes in the legislation. This course is offered in Czech language only.

### **April – May ACCA Diploma in IFRS**

ACCA Diploma in IFRS (DiplIFR) is an international qualification in IFRS developed by the leading professional accounting organization Association of Chartered Certified Accountants (ACCA). Obtaining this qualification will raise your professionalism in IFRS to the next level. The program starts on 6 April 2009.

### **17 April Capitalization of borrowing costs - are you in line with IFRS?**

From 1 January 2009 there has been a significant change in IAS 23 covering how companies should report their borrowing costs. This seminar is focused on the impact of these key changes and provide practical examples of how these IFRS fundamentals will be applied in practice.

### **26 May 2009 Understanding Financial Instruments**

This programme is aimed at providing a solid understanding of accounting for financial instruments in accordance with IFRS. The course will be led by our Finance IFRS experts, with substantial teaching and consulting experience within the finance and banking services sector.

### **8 June 2009 Hedge Accounting**

This session will provide a practical approach to applying hedge accounting in accordance with IAS 39.

### **16 - 17 June Internal Audit Certified Programme - Modul 1: The practice of Internal Audit**

PricewaterhouseCoopers launches a certified programme which is focused on development of key skills and techniques that internal auditor professionals should have as they progress in their career. The programme is delivered by PwC Internal Audit professionals using proven PwC internal audit methodology.

You may find more details about each of the courses offered at our web-site [www.pwc.cz/academy](http://www.pwc.cz/academy).

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## Quo Vadis employer?

The Czech Republic has already been going through a global crisis for a couple months.

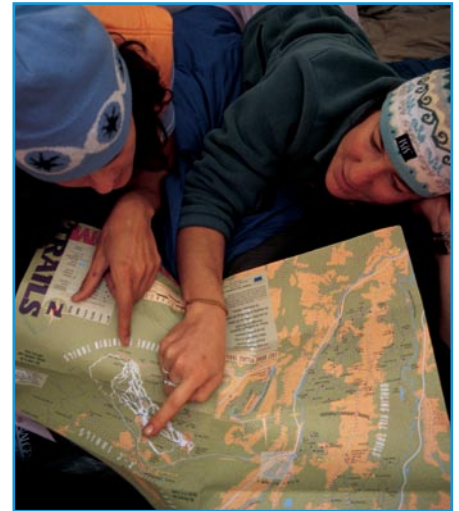
The initial shock from the immediate and deep fall of the economy and the belief in a quick recovery was soon replaced by helter-skelter cost cutting efforts “whatever it takes” – ranging from agency workers lay offs, shortened working hours, forced holidays to restrained business travels and employee benefits.

The very specific current role of human resource management has been significantly underestimated. Labour costs are under the intense scrutiny in situations when companies are trying to decrease their costs and defer investments. This is not surprising taking into consideration the fact that labour costs are high on the list, especially in the manufacturing industry and service-based companies. Extreme situations often call for extreme measures, which is why we see employers deferring or freezing hiring, salary and benefit cuts and, in the worst cases, lay offs. However, the pressure on headcount reduction may jeopardise the business in the time, when the economy and business recover, the management should therefore concentrate on how to keep the core employees – the muscle – but get rid of redundant workers – the fat – and stay in shape for the better times.

At the beginning of 2009, PricewaterhouseCoopers conducted an analysis of the impact of the financial crisis on human resource management and collected responses from 130 major Czech companies across all industries. Over 70% of the companies took precautions in labour-related costs which, in most cases, included also lay offs. Although this step might bring a relatively quick-win in terms of costs, it can incur long-term problems at the time when a business starts to recover. Therefore the key point in human resource management during a time of crisis is to understand well what activities are all the employees occupied in during the work day. What portion of their working hours are they productive and how long does it take them to add value for the company? A complex and detailed analysis of their activities will help companies to better manage human resources, distribute and delegate work accordingly and ensure that knowledge and crucial skills are kept in the company. HR analysis can be further used to benchmark corporate strategy in this area with competitors in the same industry.

In the past 10 years, employers were extremely generous in terms of remuneration and salary increases. The trend of approximately 5% salary increases brought certain anticipation in year-to-year salary adjustments and inflated salary structures in general. What will happen in times of financial crisis? Will Czech companies decrease fixed salaries or bonuses, or will they keep raising salaries to keep employees satisfied, even though the pressure will be to scale down in all areas?

The answer to this question is not straightforward and will largely depend on industry specifics. Some industries are suffering as a consequence of the unfavourable economic conditions, whereas others feel a minor impact or none at all. For example, while the pharmaceutical industry is still expecting the stable salary increases of 5%, there is no, or a maximum 1% salary increase anticipated for the manufacturing sector. How much will the salaries and benefits paid vary across all industries? Current development offers several options like the redistribution of risk between the employer and its employees, indicating that employees will no longer enjoy only the benefits of positive development, e.g. 13th month salary, but will also bear the consequences of unfavourable development.



**PricewaterhouseCoopers' study offers a fresh look at how the crisis may impact human resources management on a sample of 130 leading companies across all industries. If you are interested in the study findings please contact our HR professional:**

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## Investment performance tops insurance risks

According to an Insurance Banana Skins survey, conducted by the CSFI in association with PricewaterhouseCoopers, stable investment returns are the most important element of the business for insurance companies facing an uncertain future in what is proving to be the worst business crisis in decades. This is in sharp contrast to the previous survey in 2007 when the top focus was on operational risks such as too much regulation.

With over 400 responses from 39 countries, the new Insurance Banana Skins survey shows how respondents rank the risks facing the industry. High on the list is the macro-economic outlook and its impact on the insurance industry. Lower business volumes are expected to put strains on profitability and capital in many parts of the world.

The survey also shows that the industry is seen to be less well prepared to handle risk than it was in 2007. Only 4% of respondents thought that insurance companies were well prepared compared with 21% last time.

The survey in full is available at our [website](#). More information can be obtained also at [www.pwc.cz](http://www.pwc.cz) in the press releases section.

## Tax & Business News, Czech Republic, 31 March 2009

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