Meet the heart of Europe

Investment in the Czech Republic

2017
Welcome to the Czech Republic!
In today's highly competitive and dynamic economic environment, few decisions are as critical to success as selecting your business location. Most entrepreneurs at some point consider relocating to create fresh momentum and pursue new growth opportunities.

Compared to its regional peers, the Czech Republic is doing fairly well in terms of GDP per capita and competitiveness. It also clearly stands out as a regional champion in the inflow of foreign direct investment (FDI). Currently, the Czech Republic is experiencing growth across various sectors of the economy, including merger and acquisition activity.

While cost is a factor, it is only one of many considerations that influence the choice of destination: an education system that yields a highly skilled workforce; high living standards and a diverse culture; capacity for innovation; a modern infrastructure combined with a position in the heart of Europe.

The Czech Republic has been a popular destination for foreign capital and has attracted high volumes of FDI since the 1990s. FDI activities in the Czech Republic stand out in a very important feature: profitability.

The Czech Republic is home to many advantageous conditions – from its geographical location combined with a reliable infrastructure, availability of suppliers and specialized inputs needed by foreign investors, to quality of life and social stability, cost competitiveness, financial stability and availability of financing, investment incentives as well as a skilled workforce and a high educational level, all making it an attractive location for all types of investors and companies.

This publication sets out insights and data relevant to planning investments or conducting business in the Czech Republic. As the tax and legal systems in the Czech Republic are still comparatively new, certainty about the legal effects of transactions is sometimes less easy to obtain than in more developed economies. In addition, Czech and EU legislation are frequently amended. Accordingly, the information should be viewed only as a general guide for preliminary planning purposes.

We nevertheless hope it will be a helpful source of background information and a constructive tool in making your investment decisions.

Combining KPMG's insights and expertise in relocation issues, we can help you determine if the Czech Republic is the right base for your business in Europe. If you have any questions, remarks or suggestions, please feel free to contact the respective KPMG experts.

We look forward to assisting you with your investment in the Czech Republic.

KPMG in the Czech Republic
Meet a regional champion

Where the Czechs score the best. The Czech Republic clearly stands out as a regional champion for the inflow of foreign direct investments. Among the new member states of the EU, the Czech Republic is:

- no. 1 in quality of electricity supply
- no. 1 in low wastefulness of government spending
- no. 1 in local availability of specialized training services
- no. 1 in quality of air transport infrastructure

1 Central and Eastern European new member states of the EU; this group consists of 11 post-socialist countries which entered the EU in 2004, 2007 and 2013: Bulgaria, Croatia, Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Romania, the Slovak Republic and Slovenia.
In the overall Global Competitiveness Report 2016-2017, the Czech Republic ranks **31st in the competition of 138 countries** in the world. It has made remarkable progress from 37th to 31st place since 2014-2015. It has been classified as an **innovation-driven economy**.

Meet your business destination in the geographical heart of Europe.

The Czech Republic has an advantageous geographical location. Known as the heart of Europe, it is close to most major European business centres.
<table>
<thead>
<tr>
<th>City</th>
<th>Travel Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amsterdam, the Netherlands</td>
<td>1 h 30 min</td>
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<tr>
<td>Athens, Greece</td>
<td>2 h 40 min</td>
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<td>Barcelona, Spain</td>
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<td>Basel, Switzerland</td>
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<td>Belgrade, Serbia</td>
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<td>Venice, Italy</td>
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<td>Bergen, Norway</td>
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<td>Berlin, Germany</td>
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<td>Bologna, Italy</td>
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<td>Bratislava, Slovakia</td>
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<td>Bristol, Great Britain</td>
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<tr>
<td>Brussels, Belgium</td>
<td>1 h 25 min</td>
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<tr>
<td>Budapest, Hungary</td>
<td>1 h 20 min</td>
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<tr>
<td>Bucharest, Rumania</td>
<td>2 h 5 min</td>
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<tr>
<td>Zurich, Switzerland</td>
<td>1 h 20 min</td>
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<tr>
<td>Dublin, Ireland</td>
<td>2 h 25 min</td>
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<tr>
<td>Düsseldorf, Germany</td>
<td>1 h 20 min</td>
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<tr>
<td>Edinburgh, Great Britain</td>
<td>2 h 15 min</td>
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<tr>
<td>Frankfurt am Main, Germany</td>
<td>1 h 5 min</td>
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<tr>
<td>Hamburg, Germany</td>
<td>1 h 20 min</td>
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<tr>
<td>Helsinki, Finland</td>
<td>2 h 10 min</td>
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<tr>
<td>Copenhagen, Denmark</td>
<td>1 h 25 min</td>
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<tr>
<td>Cologne, Germany</td>
<td>1 h 10 min</td>
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<tr>
<td>Kosice, Slovakia</td>
<td>1 h 20 min</td>
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<tr>
<td>Ukraine</td>
<td>2 h 10 min</td>
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<tr>
<td>Lisbon, Portugal</td>
<td>3 h 25 min</td>
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<tr>
<td>Poland</td>
<td>1 h 0 min</td>
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<tr>
<td>Great Britain</td>
<td>1 h 55 min</td>
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<td>Lublin, Slovenia</td>
<td>1 h 10 min</td>
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<tr>
<td>France</td>
<td>1 h 40 min</td>
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<tr>
<td>Madrid, Spain</td>
<td>2 h 55 min</td>
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<tr>
<td>Manchester, Great Britain</td>
<td>2 h 5 min</td>
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<td>Milan, Italy</td>
<td>1 h 30 min</td>
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<td>Belorussia</td>
<td>1 h 45 min</td>
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<td>Munich, Germany</td>
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<tr>
<td>Russia</td>
<td>2 h 50 min</td>
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<td>Napoli, Italy</td>
<td>1 h 55 min</td>
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<td>Nice, France</td>
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<td>1 h 20 min</td>
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<tr>
<td>Vienna, Austria</td>
<td>55 min</td>
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<tr>
<td>Switzerland</td>
<td>1 h 30 min</td>
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</tbody>
</table>
Meet a popular foreign capital destination

The Czech Republic has been one of the most successful CEE countries in terms of attracting foreign direct investment (FDI) since the 1990s. The primary investing sectors are manufacturing, financial institutions, real estate, transport and communications. Where did most of the FDIs originate?

<table>
<thead>
<tr>
<th>TOP 10 investing countries</th>
</tr>
</thead>
<tbody>
<tr>
<td>1Netherlands</td>
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<tr>
<td>2Germany</td>
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<tr>
<td>3Austria</td>
</tr>
<tr>
<td>4France</td>
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<tr>
<td>5Switzerland</td>
</tr>
<tr>
<td>6United States</td>
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<tr>
<td>7United Kingdom</td>
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<tr>
<td>8South Korea</td>
</tr>
<tr>
<td>9Japan</td>
</tr>
<tr>
<td>10Sweden</td>
</tr>
</tbody>
</table>

Meet the financial support for your investment

Covering up to 25% of costs associated with investment projects. That’s what the Czech Republic offers to both new and existing investors. Aid is provided mainly from the national investment-incentives scheme.

**Job-creation grants** Financial support for creation of new jobs (EUR 3,700 – 11,100 per new job).

**Training grants** Financial support for training and retraining of new employees (up to 50% of eligible training costs).

**Tax incentives** Full corporate tax relief for up to ten years for new companies, partial for existing ones.
Meet your investment opportunities

With **1.3 million vehicles** produced annually, the Czech Republic has maintained its supreme position as the largest passenger-car producer in Central and Eastern Europe.

Prague, the capital of the Czech Republic, is home to the headquarters of the European Global Navigation Satellite Systems Agency.

The Czech Republic is one of the world’s **most attractive location** for shared business support services in financial, accounting, IT and customer support.

The Czech Republic hosts one of the highest concentrations of automotive manufacturing enterprises. By volume alone, it belongs to the 15 largest global passenger car producers. It has a long industrial tradition and is able to compete at a global level. More than half of the world’s top-100 tier one suppliers are located in the Czech Republic.

**Current successful investors:** Hyundai, Johnson Controls, Volkswagen, Robert Bosch, Toyota/PSA, Faurecia, Continental, Valeo

A strong engineering background, excellent research and development (R & D) facilities, an outstanding product reputation and high product reliability ensure safe investment opportunities. The Czech Republic is an active member of the European Space Agency.

**Current successful investors:** Honeywell Aerospace, GE Aviation, Latecoere, Textron, UGMK

What makes the Czech Republic one of the world’s **most attractive locations for business**? The answer is simple: its location, infrastructure and a skilled workforce with foreign language skills.

**Current successful investors:** DHL, Accenture, IBM, SAP, Infosys
The Czech Republic offers abundant opportunities for investors in the design, manufacture and delivery of new technologies for environmental protection and energy savings.

When investing in the Czech Republic, you can count on top technical competence, manufacturing excellence and cost effectiveness.

Current successful investors: Doosan, Vyncce, Solar Turbines, Bilfinger, Mavel

Current successful investors: Ingersol Rand, Siemens, Edwards, Daikin, Bombardier

Current successful investors: Microsoft, NetSuite, Tieto, RedHat, SolarWinds

Current successful investors: Sanofi, Teva Pharmaceutical Industries, Lonza, Otsuka Pharmaceutical, Nanotherapeutics

Current successful investors: AGC, Saint-Gobain, FEI Company, Fibertex Nonwovens A/S, Toray Industries

The sector’s main exports are turbines, transportation solutions, air-conditioning equipment, construction machinery and machine tools.

With the Czech Republic's strong inflow of high value-added projects, tradition of excellence in technical fields and heritage of thorough technical and mathematical education, the Czech origins of global ICT companies like AVG Technologies, AVAST and Y Soft are not surprising.

The country offers a growing network of research clusters, state-of-the-art research facilities, attractive locations for manufacturing and contract R&D operations plus effective patent protection. The government’s policy goals include the continuation of R&D support. GMP, GLP and GCP standards have been adopted.

CEITEC, the Regional Centre of Advanced Technologies and Materials, the Technical University of Liberec are undisputedly world-class centres of nanotechnology research. They are supported by a state-of-the-art research infrastructure and by the Czech Nanotechnology Cluster and Nanotechnology for Society funding programme.

The Czech Republic is home to world-class mechanical engineers. From 80 to 90 % of the sector’s output is exported.

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The current macroeconomic forecast

The Czech Republic is a country with relatively low external and internal macroeconomic imbalances and manageable levels of public debt and deficits. A stable and healthy banking sector with excess liquidity is able to meet the financing needs of both domestic and foreign investors with a minimal risk of losses due to financial crises and related instabilities.

Main macroeconomic indicators (November 2016 estimates, Ministry of Finance of the Czech Republic) 2017

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross domestic product</td>
<td>CZK 4 864 bil.</td>
</tr>
<tr>
<td>Average inflation rate</td>
<td>1,2%</td>
</tr>
<tr>
<td>Unemployment rate (LFS)</td>
<td>3,9% (average)</td>
</tr>
<tr>
<td>Current account balance</td>
<td>1,8% of GDP</td>
</tr>
<tr>
<td>Exchange rate CZK/EUR</td>
<td>26,9</td>
</tr>
<tr>
<td>Long-term interest rates</td>
<td>0,6% p.a.</td>
</tr>
</tbody>
</table>

According to the European Economic Forecast, the Czech Republic has experienced a strong economic rebound over the last two years. The recovery has given rise to significant improvements in the labour market, while poverty and social exclusion remain among the lowest in the EU. Higher GDP growth is leading to a resumption of the economic convergence process vis-à-vis the EU. The Czech Republic is highly integrated into global value chains and evidence points to recent competitiveness gains.

European Economic Forecast for the Czech Republic
(Autumn 2016 estimates)

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth (% yoy)</td>
<td>2.6</td>
<td>2.7</td>
</tr>
<tr>
<td>Inflation (% yoy)</td>
<td>1.2</td>
<td>1.6</td>
</tr>
<tr>
<td>Unemployment (%)</td>
<td>4.1</td>
<td>4.0</td>
</tr>
<tr>
<td>Public budget balance (% of GDP)</td>
<td>-0.2</td>
<td>-0.1</td>
</tr>
<tr>
<td>Gross public debt (% of GDP)</td>
<td>39.1</td>
<td>38.5</td>
</tr>
<tr>
<td>Current account balance (% of GDP)</td>
<td>-0.7</td>
<td>-0.7</td>
</tr>
</tbody>
</table>

3 http://ec.europa.eu/economy_finance/eu/countries/czech_republic_en.htm
The Czech Republic in numbers

The Czech Republic is an advanced democracy with a free-market economy. It is well known for its skilled workforce, reliable infrastructure, cost competitiveness and high educational level. Favourable labour costs are also among the main attractions of the Czech economy.

Since 1989, a parliamentary republic with a multi-party democratic political system

Three distinct regions: Bohemia, Moravia and Silesia

1348 One of the oldest continuously existing universities in the world (Charles University) was founded.

A working population of about 5.3 million

Since 2004, a member of the EU; since 1999, a member of NATO,
since 2007, a member of Schengen.

Population of capital city Prague 1.3 million

Overall population 10.6 million
The Czech Republic is rated very positively by all three major rating agencies: Moody's, Standard and Poor's and Fitch.

Moody's A1

Fitch A+

Standard and Poor's AA-
Living in the Czech Republic

Foreign nationals coming to the Czech Republic are subject to the so-called Foreigners Act, which establishes two categories of foreigners: citizens of the EU, the EEA and Switzerland and nationals of third countries.

Residency and visas

To stay in the Czech Republic for more than three months, citizens of non-EU countries require a long-term visa or a long-term or permanent residence permit. Natural persons with permanent residence outside the Czech Republic or legal entities with a registered office outside the Czech Republic may run a business in the Czech Republic under the same conditions and under the same limitations as a Czech person/entity.

Cost of living in Prague

Wage levels are 20.3, compared to New York’s 100.

Average prices of goods and services (including rent) are 36.4, compared to the New York benchmark of 100.

Goods and services comparison is based on the cost of a basket of 122 goods and services weighted according to European consumption habits. Wage levels are calculated as effective hourly wages for 15 professions, weighted by distribution; net after tax and social security deductions. UBS, Prices and Earnings (Edition 2015); at: https://www.ubs.com/microsites/prices-earnings/edition-2015.html
After the Velvet Revolution in 1989, the Czech Republic became a highly popular destination for foreigners. Today, tens of thousands of them benefit from the combination of a high standard and low cost of living.

The Czech Republic is home to numerous international educational institutions, offering a growing choice of foreign-language educational programmes ranging from preschools to MBA degrees.

Although in most respects, life in the Czech Republic is rapidly approaching Western standards of living, the cost of living remains substantially lower than in Western Europe.

A number of foreign cultural centres ranging from the British Council to the Goethe-Institut offer a wide array of cultural events and services.
The Czech Republic’s current attitude towards incoming investors is the most positive in its history.
Business meetings

Czechs always come to business meetings on time; arriving late is considered impolite. The dress code should convey respect to a business partner. You can take off your jacket only after the business partner with the highest rank does.
Attracting new investment

Over the past few years, the Czech Republic has significantly increased its focus on both green field investments and the expansion of existing investments. It currently has the most positive attitude to incoming investors in its history.

Investors can obtain the following financial benefits:
- investment incentives – tax holiday + cash grants
- subsidies from EU funds – cash grants
- R&D tax allowances
- education tax allowances

All benefits are provided according to the law and transparency rules, which are in compliance with EU regulations. In this respect, some measures have been redesigned further to a change of EU rules in 2014. EU regulations have generally become stricter and to a certain extent limit the granting of incentives by individual member states. The Czech government responded to the new rules with an amendment to the Czech Act on Investment Incentives, effective since May 2015. The aim of the last amendment is to increase the attractiveness of investment incentives for investors and to reduce the impact of the new EU rules on them. The information below is based on the new legislation. No substantial change in legislation is expected for 2017 and 2018.

Investment incentives

Forms of support
Incentives are provided in the following forms:
- corporate income tax relief for up to 10 years (tax holiday)
- employment subsidies in the form of cash grants for job creation and training (only available in regions with high unemployment rates)
- cash grants for strategic projects
- availability of land at discounted prices
- exemptions from real estate tax in selected industrial zones.

Main conditions
The main conditions for granting investment incentives differ depending on the supported activity.

Manufacturing industry:
- establishment of a new manufacturing plant, or expansion of an existing plant, including its modernization and diversification of product portfolio
- minimum investment in tangible and intangible assets of CZK 100 million (approx. EUR 3.6 million or USD 4 million), in selected regions this has been reduced to CZK 50 million. Machinery must be new
- creation of at least 20 new jobs.
Technology centres:
- establishment of a new technology centre, or expansion of an existing technology centre
- minimum investment in tangible and intangible assets of CZK 10 million (approx. EUR 360,000 or USD 400,000), of which at least CZK 5 million must be invested in machinery. Machinery must be new
- creation of at least 20 new jobs.

Business support services centres:
- establishment or expansion of:
  - shared services centre
  - software development centre
  - high-tech repair centre
  - customer support centre
  - data centre;
- creation of at least 20 new jobs for software development centres, 500 new jobs for customer support centre or 70 new jobs for other business support services centres.

The following conditions apply for all types of investments:
- The acquisition of assets for the project, including construction work, cannot start before the application for incentives is submitted.
- The investment must be maintained (in the minimum amount and structure) for at least five years from its finalization.

Strategic investment (large projects)
- Large projects can qualify for strategic investment status.
- The main benefit of this status is the possibility to obtain a higher portion of incentives in cash instead of tax relief.
- Cash grants can reach up to 10% and can be further increased to 12.5% in case of projects combining manufacturing sites and technology centres.
- For strategic investments in the manufacturing industry, the minimum amount to be invested in fixed assets is CZK 500 million, of which CZK 250 million must be invested in new machinery. At least 500 jobs must be created.
- For strategic investments into technology centres, the minimum amount to be invested in fixed assets is CZK 200 million, of which CZK 100 million must be invested in new machinery. At least 100 jobs must be created.

Income tax relief
Calculation
The tax treatment of a new company (plant) differs from that of an expanded facility only in the calculation of tax relief that can be claimed.
For new companies, taxpayers are entitled to full tax relief, excluding tax on net interest income.
For the expansion of an existing plant, the amount eligible for tax
relief is the difference between the tax relief that would be available for a new company and the average of the tax liabilities in the three years immediately preceding the first year in which tax relief can be claimed. The latter figure is adjusted with reference to industrial inflation and the current tax rate. This formula represents a rough attempt to limit the amount eligible for tax relief to any additional profits resulting from the expansion.

Permissible level of state aid and subsidy amounts
The total value of incentives must not exceed the maximum permissible level of state aid. The maximum amount of state aid is based on the rules set by the EU and comes to 25 percent of eligible costs (investment in land, buildings, machinery and equipment and selected intangible assets) except for Prague, where no incentives can be provided.
For technology centres and business support services centres, eligible costs may alternatively comprise the wage costs of employees in newly created jobs within 24 months of the month in which a particular position was filled.

Job creation
Cash grants will be provided to employers creating new jobs in regions with unemployment at more than 25 percent above the national average or in special economic zones. Cash grants may amount to CZK 100,000 – 300,000 per new job.

Training and retraining of employees
Cash grants for the training and retraining of employees will be provided to employers in the form of partial reimbursements of the costs incurred. Subsidies may cover 25 percent of the eligible costs of employee training and retraining.

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

How can KPMG help investors in the area of incentives?
KPMG in the Czech Republic is a leading advisor on investment incentives and can help investors with:
• initial assessments of whether projects qualify for investment incentives
• calculation of estimated benefits
• preparation of applications for investment incentives
• full support during the approval process
• full support during the implementation phase
• negotiations with the government on extraordinary incentives
• site selection analysis.
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. EU funds are available mostly in form of **investment cash grants**. A wide selection of grants is available. The grants below are the most relevant to new investors:

- **Programme Innovation** – support for innovations in production
- **Programme ICT** – shared service centres
- **Programme Potential** – support for R & D centre expansion/establishment
- **Programme Energy Savings**
- **Program Applications** – support for operational costs of R & D projects.

To obtain more detailed information, please contact Jan Linhart at jlinhart@kpmg.cz.

R & D tax allowance

Companies performing R & D activities may apply a special tax deduction. The R & D deduction in fact allows companies to claim internal R & D costs twice: first, within the income statement, second, as a special tax deduction. Effectively, savings can thus be up to 19 percent of R & D costs. The deduction can be claimed every year and there is no limit on the maximum amount to be claimed.

KPMG in the Czech Republic is an authorised advisor in the area of R & D tax deductions and provides a wide range of related services. It can help clients with:

- eligible activity **definition**
- calculation of the deduction
- preparation of required documentation
- obtaining a ruling from the tax authority
- issuance of a certified court expert opinion.
Education tax deduction

The education tax deduction was introduced as a new tool in 2014. Companies may obtain a special tax deduction for certain costs relating to vocational or professional education activities.

The deduction covers various activities relating to the education of secondary school or university students on the premises of companies. Companies can also receive a deduction for assets acquired for the purposes of such education.
Establishing a company in the Czech Republic is neither financially demanding nor very time-consuming – e.g. for a limited liability company (s. r. o.), minimum registered capital of CZK 1 is sufficient and the company can be established within one month.
Visiting

If you are invited to a Czech household, you are expected to take off your shoes in the entrance hall. Your hosts will probably provide you with slippers. Progressive households may find this outdated and will most likely tell you to keep your shoes on.
The basic provisions governing business obligations and other specific aspects of doing business in the Czech Republic are set out in the Civil Code and the Act on Business Corporations, both effective as of 1 January 2014. The Act on Business Corporations addresses the main aspects of Czech corporate law. It also regulates the relationship between companies and their statutory representatives, their rights, obligations and liabilities for breaches of due care. Further, it sets out the rules for holding companies and the liability for damage caused by their controlling entities.

The Act on Business Corporations recognises the following types of business entities:
- limited liability companies
- joint-stock companies
- general partnerships
- limited partnerships
- co-operatives
- Societas Europaea (SE, European Companies)
- European Economic Interest Groupings (EEIG).

Foreign legal persons may also establish a branch in the Czech Republic. A branch is not considered a legal entity, but must nevertheless be registered in the Commercial Register. The Act on Business Corporations regulates the status and activities of entrepreneurs and applies to both legal entities and individuals. A Czech legal person is an entity that has its registered office in the Czech Republic. Foreign persons are defined as persons (individuals or legal entities) 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 it is recorded in the Commercial Register.
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 sole shareholder.

The main characteristics of the various legal entities are described below.

Limited liability company (společnost s ručením omezeným – spol. s r.o. or s. r. o.)

- The company must have at least CZK 1 of registered capital.
- The list of shareholders, the amount of each shareholder’s contribution and the names of the members of the supervisory board (if one is established) must be recorded in the Commercial Register.
- The law allows the creation of different kinds of shares. Shares to which the same rights and obligations are attached form one kind of share. Shareholders may own more than one share and also different kinds of shares.
- The shares of a shareholder may be represented by a common share certificate (kmenový list). However, such a certificate cannot be in the form of a registered certificate and may not be publicly offered or admitted to trading on the regulated market.
- A supervisory board is not required. Upon their discretion, shareholders may decide on its establishment.
- The general meeting appoints an executive (jednatel) or executives, who are legally responsible for the management of the company and whose details, including information on their authorisation to act on behalf of the entity, must be recorded in the Commercial Register.
- Companies may also appoint legal entities as executives.
- A limited liability company’s financial statements do not have
to be audited unless two or more of the following criteria have been met for two consecutive years:
• Net turnover exceeds CZK 80 million per annum.
• Total assets exceed CZK 40 million.
• The average number of employees exceeds 50.
• Establishment will occur around one month after having provided all necessary documents and information.

Joint-stock company (akciová společnost – a. s.)
• Registered capital has to be at least CZK 2 million or EUR 80,000.
• Non-cash contributions to registered capital must be valued by an independent expert proposed by the founders or the already existing company in case of a registered capital increase. The valuation is binding for the company.
• Financial statements of a joint-stock company do not have to be audited unless any of the following criteria has been met for two consecutive years:
  Net turnover exceeds CZK 80 million per annum.
  Total assets exceed CZK 40 million.
  The average number of employees exceeds 50.
• Annual financial statements must be published.
• The company may decide between two internal structures: either a supervisory board and a board of directors (dualistic organisation of corporate bodies), or an executive director and a managing board (monistic organisation of corporate bodies). The chairman of the managing board may be the same person as the executive director (i.e. one person can secure the entire operation of a joint stock company). A legal entity may also be appointed as member of a joint stock company board of directors. The executive director has to be a natural person.

General partnership (veřejná obchodní společnost – veř. obch. spol. or v. o. s.)
• A general partnership is formed by two or more persons (individuals or legal entities).
• The partners in a general partnership are liable for the debts of the company.
• The names and addresses or the registered offices of the partners must be registered in the Commercial Register.
• All partners are entitled to act on behalf of the partnership and are jointly and severally liable for the partnership’s obligations to the extent of their entire property.
• Requirements for financial statement audits 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 (individuals or legal entities). At least one of the partners must be a general partner, with unlimited liability for the debts of the partnership. At least one partner must be a limited partner, 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.
• Requirements for financial statements audit are the same as for a limited liability company.

Co-operative (družstvo)
• Co--operatives are formed by at least three members, either legal entities or individuals, to undertake business activities for the economic or social benefit of their members.
• Members are not liable for the obligations of the co-operative; however, the co-operative may demand contributions from its members to cover losses.
• Requirements for a financial statements audit 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 registered in the Commercial Register.
• The entry in the Commercial Register must include details about the activities of the foreign business and its office in the Czech Republic, the scope of its business activities and the name and the address of its director (general manager).
• A branch must obtain a trade licence from the regional Trade Licensing Office.
• The liability of a founder of a branch is not limited since a branch is not an independent entity.
• Requirements for financial statement audits are the same as for a limited liability company.

Company formation procedure:

1. memorandum of association
2. obtaining a trade license
3. contribution payment
4. registration in Commercial Register.

A company is formed after a founder’s deed or a memorandum of association has been completed and signed. Limited liability companies and joint-stock companies must obtain these documents in the form of a notarial deed.

After the founder’s deed or memorandum of association has been signed and filed, the future executives of the company must register their trade licences at the Trade Licensing Office and obtain the documents necessary to register the address of the company. The company founders also need to appoint a contributions’ administrator responsible for proving to the Commercial Register that the contributions to the registered capital have been paid up by the shareholders.

After the future executives have collected all necessary documents, they may file an application for the registration of the company in the Commercial Register. Once the court administering the Commercial Register issues a decision on the company registration and this decisions enters into force, the process of the company’s formation is complete. The whole process may take up to two months.
The Commercial Register

A company that is not a branch has an independent legal personality and is entitled to commence business activity in the Czech Republic only after registration in the Commercial Register. Courts have to register a new company in the Commercial Register within five business days after the delivery of a defect-free application. Fees amount to CZK 6,000 for a limited liability company and CZK 12,000 for a joint-stock company (approx. EUR 220 and 440).

Entries in the Commercial Register include the name of the entity and the address of its registered office, the identification number of the entity, the scope of its business activities, the type of entity and the names and addresses of the executives or directors, together with details of their authorisation to act on behalf of the entity.

Access to the Commercial Register is freely available on the internet (www.justice.cz; www.mfcr.cz).
Employment policy

The Czech Republic has a skilled and educated labour force.
Gifts

It is considered polite to bring some small gift when visiting; this may be a bottle of wine or flowers. Please note! Flowers should be in odd numbers since even numbers may evoke funeral arrangements. Czechs usually unwrap their presents immediately after receiving them.
Employment policy

The Czech Republic has a skilled and educated labour force and its literacy rate is above 98 percent. **Czech labour law is not considered excessively rigid and is relatively flexible within the EU context.** Employment law is governed by the Labour Code. 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, Czech Labour Code regulations will apply to the basic conditions of employment, such as maximum working hours, minimum length of rest periods, minimum annual leave entitlement, minimum wage and overtime rates, occupational health and safety, etc. **The maximum working week is 40 hours.** The standard working week is **Monday to Friday.**

The maximum amount of **overtime** that may be assigned by the employer is **150 hours per year.** The maximum amount of overtime worked with the employee’s consent may not exceed **416 hours annually.** Overtime must be distributed evenly. The **retirement age** for individuals ranges from **60 to 65** based on gender, date of birth and the number of children raised (applicable to women only).

Employment contracts

Employers are required to conclude **written employment contracts** with their employees. The contract must at least describe the **type of work, the date** the employee will commence working, and **where** the work will be performed. **Trial periods** may generally not be longer than **three months,** except for managerial positions, where they may extend to up to **six months.** A fixed-term employment contract may be concluded for up to **three years,** and may only be **renewed twice.** An employment contract concluded for an indefinite period or a fixed term may be terminated:

- **by agreement**
- **by notice**
- **by immediate termination**
- **anytime during the trial period.**

A fixed-term employment contract also terminates upon the expiry of the agreed period. If employment is terminated with notice, a notice period of at least **two months** applies.
The employee can give notice without stating a reason. However, if the notice is given by the employer, it must specify one of the reasons stated in the Labour Code, such as:

- The employer is being liquidated or is ceasing to carry on business.
- The employer’s operations are relocating.
- The employee has become redundant following the employer’s organisational change.
- The employee has committed a serious breach of obligations.
- The employee is no longer healthy enough to perform work.
- The employee has failed to fulfil the prerequisites for the performance of the job.

Where an employment contract is terminated for any of the reasons under points 1 to 3, the employer is obliged to pay the employee up to three months’ severance pay depending on the duration of the employment relationship. If the reason for termination is the employee’s health incapacity resulting from an occupational disease or accident at work, the severance pay equals twelve times the employee’s monthly salary.

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

Employment terminations during the trial period may be submitted by either party for any reason, or without any reason being given.
Employment policy

#### Employment agencies

An alternative to employment contracts is agency employment. An employment agency provides its clients with human resources, without the clients having to conclude employment contracts directly with the employees. Even though this option is more expensive, it provides greater flexibility in the allocation of human resources.

#### Trade unions

Unions can be formed freely and neither the state nor any other subject can restrict their formation. 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. The role of trade unions in the Czech Republic is to formulate and assure the labour, economic and social interests of employees. The aim of collective bargaining is to facilitate employee agreements with employers.

#### Mass layoffs

If an employer terminates the employment relationships of a certain number of employees as defined in the Labour Code, for the specific reasons set out above under points 1 to 3, within a period of 30 calendar days, this is considered a mass layoff and special conditions, such as a notification obligation to the Labour Office and unions, apply.
Holidays

The minimum holiday period is four weeks per annum, unless increased by a collective bargaining agreement, employment contract or internal regulations. For employment relationships shorter than a year, employees accrue one-twelfth of the annual holiday for each calendar month of continuous employment with the same employer.

Holiday pay is calculated from employee's average monthly earnings.

Social security and health insurance

Both the employee and the employer must contribute to two major schemes: social security and health insurance.

Payments from the social security insurance system typically include:
• pensions
• cash benefits such as sick leave, maternity benefits, social benefits, etc.

Social security treaties have been concluded with certain countries and relieve seconded employees of the burden of having to pay social security contributions in more than one country.

Concurrence of a function as a member of a corporation’s statutory body and employment

Current legislation does not allow the concurrence of membership in a statutory body (executive officership) and employment at a managerial position.
The Czech financial sector: a safe harbour for foreign investments (continuing profitability, sufficient liquidity, as well as capital adequacy)
Going for a beer

Czechs like to go out for a beer with friends. They order beers and prepare coasters on which waiters then place their beers. Once the drinks are on the table, Czechs toast each other by raising their glasses, meeting each other’s eyes, clinking glasses and saying “Na zdraví” (cheers)!
Regulation and supervision

The Czech National Bank (CNB) is the central bank of the Czech Republic. It determines the country’s monetary policy, carries out and coordinates the supervision of the Czech financial market, issues banknotes and coins, and manages the circulation of currency as well as the payment and settlement systems between banks. More details can be found at: www.cnb.cz.

The responsibility for preparing primary legislation for the financial sector mainly lies with the Ministry of Finance; the CNB assists in this process. As the Czech Republic is an EU member, in the area of supervision the CNB cooperates with European institutions (the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority) on unifying supervisory procedures and creating conditions for close cooperation between home and host supervisors. The CNB also closely cooperates with the European Central Bank in its role of banking supervisor within the Single Supervisory Mechanism.

Prudential rules for banks, credit unions and investment firms are primarily regulated by the Capital Requirements Regulation (CRR) directly applicable in EU member states and a decree issued in 2014, driven by measures agreed on at the EU level and implementing the requirements of Basel III/CRD IV into Czech legislation.

Solvency II, a new, harmonised EU-wide insurance regulatory regime, became fully applicable on 1 January 2016 in all EU member states, including the Czech Republic.

Licences

The licensing of banks and other financial institutions and matters connected with mergers and acquisitions and other market entries are fully within the responsibilities of the CNB.

A foreign financial institution can enter the Czech market in the following four ways:
• as a new company, with up to a 100 percent foreign ownership
• by acquiring an equity stake in an existing entity
• by establishing a branch of the parent institution with a separate licence
• by establishing a financial institution of the parent based on the licence of the parent institution (applicable to all banks and insurance companies with a registered office in the EU under the “single licence principle”).

Deposit insurance

In 2010, the deposit limit for 100-percent protection was raised to EUR 100,000. The deposit claims of banks, 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 their parent country) are obliged to participate in the scheme and to contribute to the deposit insurance fund in compliance with the Act on Banking.
Banking sector

The Czech banking sector is primarily represented by banking institutions with international ownership. It is dominated by big foreign banking groups such as Erste, KBC, Societe Generale, UniCredit or Raiffeisen. Although the banking sector is significantly concentrated, small and medium banks have been able to strengthen their position on the Czech market in recent years. Typical activities include commercial lending to corporate and retail clients, customer accounts and deposits administration, credit card operations, international lending and loan syndications, mutual funds management and administration, bank treasury operations and back office activities.

As at 31 December 2016, 45 banks (including foreign branches) offered banking services to clients in the Czech Republic; 37 of them were controlled by foreign investors and eight by local stakeholders. The group of the four largest banks (banks with total assets greater than CZK 200 billion) continues to play a predominant role in the banking sector in the Czech Republic. As at 30 September 2016, their share of total banking assets equalled approximately 60 percent.

Despite a low interest rate environment, the Czech banking sector showed very good profitability in 2016. Net profits for the first nine months of 2016 exceeded CZK 60 billion (for the whole year of 2015 it was CZK 66 billion) with the level of non-performing loans at approximately 5 percent.
Insurance sector

The Czech insurance sector is dominated by the Generali and VIG insurance groups. The remainder of the TOP 10 insurance companies is made up by composite insurance companies, while the rest is represented by bank-assurance and specialised insurance companies.

As at 30 September 2016, 54 insurers (including foreign branches) and one reinsurance company offered insurance services to clients in the Czech Republic. Local shareholders controlled 14 insurance companies, whereas the rest had mostly foreign owners. The two largest groups reached CZK 73.9 billion of gross written premium (measured by annual premium equivalent). Overall market profitability is approximately a 10% return on equity (three-year average/2013 - 2015) and the market manages approximately CZK 484 billion of assets.

Typical products include both life and non-life insurance. The non-life insurance business is dominated by car insurance (compulsory motor third party liability insurance and casualty and collision (automobile insurance)) and commercial insurance.

Supervision of the insurance market is performed by the CNB.

Investment management and funds

As at 31 December 2016, according to CNB statistics, the Czech market was represented by 310 investment funds domiciled in the Czech Republic. In addition, 1,447 foreign investment funds are registered for public offer in the Czech Republic.

According to an act adopted in 2013 and extending options for establishing new investment funds in line with European regulations, investment funds may take the following legal forms:

- mutual fund
- trust fund
- joint-stock company
- investment company with variable capital (société d'investissement à capital variable)
- limited partnership
- limited liability company
- European company

Generally, minimum fund capital of EUR 1.25 million is required. The Czech National Bank has to approve the foundation of funds fulfilling EU requirements. A notification duty to the CNB only applies to special investment funds not fulfilling these requirements. However, every fund’s asset manager must have CNB approval.

Supervision of the investment fund market is handled by the CNB.
The stock exchange

The Prague Stock Exchange (PSE) began trading in April 1993. Trading on the PSE is conducted via licensed securities dealers, who are also PSE members. These are primarily major banks and brokers. If a common investor decides to invest in the exchange, they need to contact one of the PSE members or become a member themselves.

It is currently possible to conclude trades either directly through the regulated market (administered by the PSE) or the non-regulated market, primarily intended for OTC (over-the-counter) trades (administered by the Central Depository). Since 2012, trades on the regulated market are traded via the stock international exchange platform – Xetra. The basic criteria for trading and listing on either market can be found at: www.pse.cz.

Foreign exchange

Regulation
The Act on Foreign Exchange fully implements the obligations that the Czech Republic accepted under international agreements in relation to the free movement of capital and the system of payments. The Czech Republic has concluded many agreements with other countries on the promotion and reciprocal protection of investments.
Market development
The exchange rate of the Czech crown (CZK) to the euro (EUR) as well as to other main currencies was affected by the intervention of the CNB, which started in November 2013 (see Figure 11). The CNB announced its intention to keep the Czech currency below the level of 27 CZK/EUR. The intervention was primarily driven by the fact that inflation had been well below the inflation target for a prolonged period, potentially threatening deflation. The CNB subsequently announced that it will not discontinue using foreign exchange market intervention as a monetary policy instrument sooner than in the second quarter of 2017.
As is shown in the graph below, during 2016, the CZK stayed around the threshold of 27 CZK/EUR set up by the CNB. The Czech crown slightly depreciated against the US dollar in 4Q. As at 31 December 2016, the foreign exchange rate of CZK to EUR was 27.02; the exchange rate of CZK to USD was 25.639.

Repatriation of capital and profit
The Czech currency 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 – if applicable – imposed by the CNB.
Branches of foreign banks do not have such limitations, as the capital is managed and monitored centrally.
The following types of payments from a Czech company to its foreign parent may be transferred abroad freely, subject to appropriate withholding taxes:
• dividends
• interest
• charges for intangible property (e.g. royalties and know-how fees
• management fees
• liquidation balances.
The Czech Republic is party to a large number of double taxation treaties and has implemented the relevant EU directives.
Public transport

When travelling by public transport, Czechs first yield to those getting off and only then start getting on. With respect to seating, younger people let older people sit; it is also common to vacate seats for pregnant women and mothers with small children. It is considered impolite for a man not to yield his seat to a woman.
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 also legal entities, the profits of a general partnership (v. o. s.) are not subject to corporate tax; instead, the partners’ shares of profits are taxed in their own 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. In addition, trusts are subject to corporate tax even though they are not legal entities.

A foreign company’s branch or permanent establishment is generally subject to tax on the same basis as a company. They may also be taxed on a deemed profit basis, which is usually a percentage of the 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 they realise are included in the calculation of their business profits (see below). Special rules apply to entities not established to make profits, as these enjoy certain restricted tax privileges.

In 2017, the corporate income tax rate is 19 percent. A reduced rate of five percent applies to the income of qualifying investment funds and a reduced rate of zero percent applies to qualifying pension funds. Full or partial tax relief from corporate tax may be claimed for certain qualifying investments (see chapter – Investment incentives and state aid).

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 are 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, Iceland or Liechtenstein, and at least 10 percent of the shares have been held for 12 months.

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

Dividends received by Czech resident companies from non-residents 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 have been held for 12 months.

The exemption also applies if all 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 legal form similar to 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.

Exemptions for capital gains and dividends do not apply if the parent company or the subsidiary are either:
• exempt from corporate income tax (or similar tax);
• able to claim a corporate income tax exemption or corporate income tax relief;
• subject to corporate income tax at a rate of zero percent, or if the recipient is not the beneficial owner of the income.

Following an amendment expected to be implemented in 2017, earnings under hybrid loan arrangements (i.e. payments that are treated as deductible expenses in the source state and as tax-exempt dividends in the recipient state) will not be tax exempt at the level of the recipient company.

Mergers and divisions of companies can generally be carried out on a tax neutral basis. The EU Mergers Directive and the EU Cross-Border Merger Directive 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 same economic activity that generated the tax loss.

Taxation of business income

The starting point for computing taxable profit is the profit before tax in the Czech statutory financial statements. This is then subject to adjustments under the Income Taxes 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 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, if it is the last day of a calendar month. If the financial year-end changes, provisions in the Income Taxes Act deal 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 Taxes Act attempts to define deductible and non-deductible expenses in some detail. The general rule is that expenses incurred for the purpose of generating, assuring or maintaining taxable income are tax deductible. A special deduction equal to deductible expenditures on research and development (R & D) can be claimed and effectively means that the expenditure can be deducted twice. If not used in the period in which it arises, this deduction may be carried forward to the next three tax periods.
The Act on Provisions allows restricted deductions for bad debt provisions. It also allows taxpayers to create tax-deductible provisions for future repairs, subject to the existence of supporting evidence in the form of project plans, as long as the funds are transferred to a separate bank account by the due date of the annual tax return.

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

Tax depreciation can be claimed on fixed assets. For this purpose, fixed assets are divided into several categories broadly reflecting their expected useful life. Depreciation on most assets may be claimed on either a straight-line or an accelerated basis.

**Tax losses may be carried forward for five years.** Losses may not be carried forward following a substantial change in the direct ownership of a company, unless it can be shown that at least 80 percent of the company’s revenues derive from the same activities as those carried out in the period when the loss arose. A substantial change is the change of at least 25 percent in the ownership of registered capital or voting rights, or a change resulting in a person obtaining a controlling influence in the company. Restrictions also apply in the case of certain corporate restructuring. A ruling may be obtained from the tax authority to confirm whether a loss may be utilized after a substantial change or restructuring.

As has been the case in other OECD countries, the review of transfer pricing policies has become **one of the biggest priorities of the Czech tax authorities.** The focus is not only driven by global BEPS (Base Erosion and Profit Shifting) initiatives, but also by the state administration’s general focus on increasing the compliance of companies with valid regulations and arm’s length principles.

Czech legislation is relatively simple in this area. 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 base should be adjusted.** It is possible to request a unilateral or bilateral advance pricing agreement from the tax authorities on the appropriate transfer pricing methodology. No retroactive agreements are possible.

In addition to the provisions of the Income Taxes Act, the Ministry of Finance has issued guidelines providing more detailed information, especially on transfer pricing documentation (e.g. Decrees D-332, D-333, D-334 and D-10). These are not legally binding, but given that the tax authorities usually follow them, they represent useful guidance for taxpayers.

Companies are also required to disclose various types of related party transactions, including the volumes realized with each
related party, in an appendix to the corporate income tax return. This disclosure obligation falls upon Czech taxpayers who meet one of the three below-listed criteria:
- assets totalling more than CZK 40 million
- a net turnover of more than CZK 80 million
- a recalculated headcount exceeding 50 employees.

The obligation is further limited to companies meeting the above criteria and that have either:
- performed transactions with related parties abroad
- incurred tax losses
- are recipients of investment incentives.

There is currently no legal obligation to prepare transfer-pricing documentation. However, during tax inspections, the tax authorities regularly require transfer pricing documentation to be provided, usually giving taxpayers a deadline of 15-30 days.

Thin capitalisation provisions act to restrict the deductibility of interest and other loan expenses where the borrower has insufficient equity. The rules can be summarised as follows:
- Financial expenses (including interest) arising from loans and credits received from related parties in excess of four times the borrower’s equity (six times for banks and insurance companies) 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 principle, 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 interest or other revenue is derived from the borrower’s profit, all financial expenses on the loans or credits received are non-deductible.

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.

Further restrictions on interest deductibility are laid down by the EU Anti-Tax Avoidance Directive, which introduces an earn-
Direct taxes

ings-stripping rule whereby in principle no deduction will be permitted for net interest expenses exceeding 30% of EBITDA (or EUR 3 million if higher). The rules allow for flexibility and exemptions upon transposition and include de minimis thresholds, escape clauses and a grandfathering provision. Member states have until 31 December 2018 to implement the main provisions of the directive in their national legislation, which would then apply as from 1 January 2019. **To date it is not clear precisely how the rules will be implemented in the Czech Republic.**

**Taxation of individuals**

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

**Czech tax residence is defined as either:**
- having a permanent home in the Czech Republic;
- 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 in the above categories.

There are numerous exemptions, the most important of which are the exemptions from tax on gains from the sale of shares and securities.
- Gains on the sale of securities acquired before 31 December 2013 are exempt if the securities were held for more than six
months and do not represent more than five percent of registered capital and voting rights for 24 months preceding the sale.

• Gains on the sale of securities acquired before 31 December 2013 representing more than five percent of registered capital and voting rights for 24 months preceding the sale.

• Gains on the sale of securities acquired before 31 December 2013 representing more than five percent of registered capital and voting rights and any securities acquired on or after 1 January 2014 are exempt if they were held for three years.

• Generally, no tax is payable if the income from the sale of securities does not exceed CZK 100,000 in a tax year.

• Gains on the sale of shares in a limited liability company are exempt if the shares were held for five years.

• Gains from the sale of non-business real estate are exempt if the property was 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. If it was used for less than two years, the exemption applies if the gains are to be used for the taxpayer’s housing in the future.

From 2015, exempt income exceeding CZK 5 million in a given tax year must be declared to the tax authorities.

The income of individuals is subject to a flat tax rate of 15 percent. An additional seven percent (a “solidarity tax”) is applied on income (the sum of gross salary and the self-employment tax base) exceeding the maximum annual assessment base for social security contributions (CZK 1,355,136 in 2017). The 15% percent flat tax on employment income is calculated based on the super-gross salary, which is the gross salary increased by social security and health insurance contributions payable by the employer. Employment income taxable in the Czech Republic and paid to individuals not subject to Czech social security is increased by an employer’s deemed contributions regardless of the social security and health insurance contributions actually paid. Thus, the effective tax rate is not 15 percent (or 22 percent for persons subject to the solidarity tax) but a higher rate, depending on the income level.

Dividends and certain types of other Czech source income are taxed separately and are subject to a 15 percent withholding tax at their source.

Foreign source investment income should be included in the tax base and is subject to a flat tax rate of 15 percent. Business income or other self-employed income may be reduced by actual expenses or by an optional lump-sum deduction ranging from 30 to 80 percent of gross income. The annual lump-sum deduction is limited to a maximum of CZK 1,600,000 for income from agricultural business, CZK 1,200,000 for business income based on a trade license, CZK 600,000 for rental income and CZK 800,000 for other business income. An amendment to the Income Tax Act proposes to reduce the lump sum deductions by 50%. If approved, the new rules will apply from 1 January 2018. 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 available for both business and 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. **Employer contributions to defined private pension schemes up to CZK 50,000 per year (CZK 30,000 prior to 1 January 2017) are tax-free for the employee.**

The Czech pension system comprises two pillars – a **mandatory pay-as-you-go pension system** run by the government (the first pillar) and a **voluntary additional pension system** administered by commercial insurance companies (the third pillar).

There are no special provisions dealing with employee share option schemes, and gains realised on exercising an option are regarded as taxable income. It is generally accepted, however, that no gain arises on the granting of an option.

The salaries of employees are usually subject to the deduction of wage tax withheld by their employer on a monthly basis, with possible annual reconciliations. It is 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 cases, no liability to withhold tax arises. Instead, the employees themselves are liable to file tax returns and pay tax, normally in quarterly instalments.

**Employees of foreign companies may fall under a further possible tax treatment, the “deemed employer” rule, which is essentially an anti-avoidance provision.**

The rule may apply if employees of a foreign employer work in the Czech Republic under the control of a Czech person who pays a fee to the foreign employer for their services. Here, 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. Further special treatment applies to licensed labour agencies.

**Resident and non-resident individuals may claim a basic personal tax allowance of CZK 24,840 per year.** Various other cred-
Direct taxes

Its are granted to residents, such as a tax credit of CZK 24,840 per year for a spouse living in the taxpayer’s household if the spouse’s annual income does not exceed CZK 68,000, and tax allowances for children (a tax allowance of CZK 13,404 for the first-born, CZK 17,004 for the second-born and CZK 20,604 for the third-born and any subsequent child). Tax allowances up to the amount of the minimal wage announced for a given tax year (CZK 11,000 for 2017) can be claimed for fees paid to childcare facilities.

Limitations apply to individuals earning business or rental income and who claim flat rate expense deductions, but under a proposed law amendment, these limitations should be abolished in 2018.

Allowances are also granted to residents of the EU or EEA if at least 90 percent of their income is derived from sources in the Czech Republic. The amount of income from foreign sources should be confirmed by the foreign tax authorities in the state of residence.

Social security contributions, where payable, amount to 45 percent of an employee’s salary (for income up to an annual cap for social security – see below). This consists of an employee contribution of 11 percent and an employer contribution of 34 percent, made up as you can see in the chart.

The maximum annual assessment base for social security premiums in 2017 is CZK 1,355,136. There is no cap on health insurance premiums. Social security and health insurance contributions must be paid on a monthly basis. Social security contributions must be paid until the aggregate of the monthly assessment base exceeds the maximum annual assessment base. Upon achieving this limit, the employer should stop paying social security contributions. The assessment base is very similar to the tax base.

Foreign persons under local employment contracts are subject to Czech social security. With a social security treaty between the Czech Republic and the country of the employer in place, foreign persons employed by a non-Czech employer are subject to Czech social security unless, under the terms of the treaty, they can remain in the social security system of the home state. The authorities take the view that expatriate employees of EU employers are subject to Czech social security based on EU social security rules. In practice, this means that expatriates are liable to Czech contributions unless they remain in their home state system under EU rules.
Tax on the acquisition of immovable property

Tax liability arises upon the registry of the transfer of ownership in the land register. The tax is payable by the acquirer. The tax rate is four percent of the tax base. The tax base is the higher of the agreed price (including VAT if applicable) and of a reference value. The reference value is calculated by tax authorities based on prices for similar transactions. If the tax authorities cannot calculate a reference value, the tax base will be the higher of the agreed price and 75 percent of the value assessed by an expert. If real estate is transferred as part of an enterprise, the tax base will be based on an expert valuation. The taxpayer must submit a tax return by the end of the third month following the month in which the transfer was registered. The tax is due by the same deadline. Tax declared in the return is in some cases considered a prepayment and is subject to review by the tax authorities.

Taxation of income from inheritance and gifts

From 1 January 2014, gift and inheritance taxes have been abolished and the taxation of such income is now governed by the Income Taxes Act. Gifts are taxable unless the donor is a qualifying spouse or close relation and are subject to a flat rate of 15 percent for individuals and 19 percent for companies. No tax is payable on inherited property.
Tax on immovable property

Tax on immovable property is payable by owners of immovable property situated in the Czech Republic. This tax is generally small compared with other developed countries. Different rates apply to land and buildings. The property tax on buildings used for business purposes is based on the area of the buildings, using the rates below. An additional charge of CZK 0.75 per square metre is levied for each storey (above the ground floor) of a building used for business purposes if the area of the storey exceeds one third of the area of the ground floor.

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 2 per square metre for building plots, CZK 5 per square metre for improved land surface used for business purposes and CZK 0.20 per square metre in other cases.

For some types of property, the rates are multiplied by a coefficient ranging from 1 to 5 depending on the location of the property. In addition, the tax can be increased by another coefficient, varying from 2 to 5, based on the decision of the relevant municipality.

<table>
<thead>
<tr>
<th>Classification</th>
<th>Rate (CZK/m²)</th>
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<tbody>
<tr>
<td>Residential and agricultural</td>
<td>2</td>
</tr>
<tr>
<td>Industrial</td>
<td>10</td>
</tr>
<tr>
<td>Other business</td>
<td>10</td>
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</table>

International tax issues

A company’s registered office is the place where the effective management of the company is located. Companies with their registered office in the Czech Republic are subject to Czech tax on their worldwide income and are referred to as Czech residents. Other companies (non-residents) are subject to tax only 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 their taxable profit. Dividends from foreign companies are a separate-source of income taxable at a special rate of currently 15 percent, unless the participation exemption 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 available only if a double taxation treaty exists 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 a dependent activity (employment) performed in the Czech Republic
• income from services provided in the Czech Republic
• income from the sale or use of real estate situated in the Czech Republic
• royalties, dividends and other profit distributions, interest, and lease rentals
• income from the transfer of shares in Czech resident companies not tax exempt under domestic legislation
• income from the sale of a business as a going concern located in the Czech Republic.

These tax liabilities are to some extent mitigated by tax treaties, where applicable. **In particular, if there is a treaty in place, then:**
• 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 Czech permanent establishment of a foreign company, or if they spend more than 183 days in the Czech Republic.

**Income liable to tax is generally subject to withholding taxes at a rate of 15 percent.** The rate is increased to 35 percent if the income is paid to residents of countries that have not signed a double taxation treaty with the Czech Republic, and when no arrangement is in place for the exchange of information on tax matters.

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 some 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; hence, dividends paid by a Czech subsidiary to a parent company that is a 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, Icelandic and Liechtensteiner corporate shareholders.

The EU Interest and Royalties Directive has also been implemented in the Czech Republic. As a result, interest and royalties paid to some associated companies resident in the EU, Switzerland, Norway, Iceland and Liechtenstein are generally exempt
Beneficial ownership concept

A number of double taxation treaties concluded by the Czech Republic expressly limit their benefits to the 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 Taxes Act and double taxation treaties.

The income paid from Czech investments will normally be treated as the income of the ultimate beneficial owner of the investment via the transparent entity.

from withholding tax (subject to advance clearance procedures). Other types of income paid to non-EU or EEA residents, notably from permanent establishments, real estate and sales of securities, etc., are subject to withholding tax that is not the final tax, but a prepayment in respect of the ultimate tax liability. **This tax is generally levied at the rate of 10 percent** (one 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 administration of tax is mainly governed by the Tax Code 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 partnership profits.

All individuals with an annual taxable income exceeding CZK 15,000 must file tax returns unless the income is tax exempt or subject to withholding tax. A return must also be filed by any individual who is liable to the solidarity tax. This means that, in general, low-paid employees of Czech companies or branches of foreign entities are not required to file returns unless they have other taxable income higher than CZK 6,000.

Anyone claiming a tax loss must also file a return.

The deadline for the 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 1 April. This deadline is extended by a further three months if:

- the taxpayer is subject to a statutory audit;
- 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 to establish or examine the tax base or any 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 deadline for filing the ordinary tax return. However, the deadline for the assessment of additional tax may be extended to a maximum of 10 years under certain circumstances, such as the filing of an additional tax return or the occurrence of a tax audit. In the event of some tax-related crimes, additional tax may be assessed regardless of the lapse of the period for tax assessment.

For taxpayer declaring a loss, the period in which a tax audit 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, if extended deadlines apply, an audit can be carried out up to 15 years after the tax return became due.

If an appeal is lodged against an assessment, the payment of any additional tax is deferred until the payment order becomes legally effective, but interest continues to be calculated on the outstanding amount.
Interest on overdue tax is assessed at the Czech National Bank repo rate plus 14 percent, starting on the fifth working day following the due date. Where additional tax is assessed, a penalty of 20 percent of the additional tax is levied. If the tax authorities reduce a VAT refund, they will levy a penalty of 20 percent of the reduction. If a tax loss is reduced, one percent of the reduction becomes payable as a penalty. If the taxpayer corrects the tax base in an additional tax return, only interest on the overdue tax is payable.
Indirect taxes

The Czech VAT system is based on the harmonised principles of EU Directive 2006/112.
Restaurants

Men always enter restaurants first. This custom stems from the time when restaurants were considered not safe and men created a sort of shield for women. Czechs do not usually call for service but instead try to establish eye contact. The person who initiated the meeting always pays the bill. In Czech restaurants, a 10% tip is usually paid to waitstaff.
Value added tax (VAT)

The Czech Value Added Tax Act is based on the general principles of EC Directive 2006/112 and as such is very similar to the tax acts of other EU countries. VAT is generally due on supplies of goods or services, intra-community acquisitions of goods and imports of goods with the place of supply in the Czech Republic.

VAT rates

The standard VAT rate is 21 percent (effective from 1 January 2013). The Czech Republic also applies two reduced rates. The first reduced rate of 15 percent applies to e.g. food products, public transportation services, social housing construction, and transfers of social housing, unless these are tax-exempt. The second reduced rate of 10 percent (effective since 1 January 2015) applies to essential baby nutrition, pharmaceuticals for human and veterinary purposes, books (and newspapers, effective as of 1 March 2017), mill products and their mixtures for the production of foods for gluten-intolerant individuals. Exports and intra-community supplies of goods, as well as the international transport of goods relating to exports or imports of goods, are zero-rated.

Certain supplies of goods and services are exempt from VAT, for example:

- insurance and financial services
- postal services
- education
- health and welfare services
- transfer and financial leasing of immovable property under certain conditions
- renting of immovable property (apart from short-term leases, leases of parking spaces and leases of safe deposit boxes).
VAT registration

VAT registration is obligatory for taxable persons established in the Czech Republic whose turnover for the preceding 12 consecutive months exceeded CZK 1 million. Other situations may also lead to obligatory VAT registration (e.g. the purchase of a going concern from a VAT payer, the transfer of the assets of a dissolved or spun-off VAT payer entity to a taxable person).

A taxable person not established in the Czech Republic becomes a Czech VAT payer if they make a specific transaction with the place of supply in the Czech Republic, such as a zero-rated supply of goods to another EU member state or a Czech local taxable supply (supply of goods, provision of services) on which they have to account for VAT (i.e. the reverse-charge regime is not applicable). No registration threshold applies.

Taxable persons (both established and not established in the Czech Republic) may voluntarily register for VAT.

A group of related parties established or having a VAT establishment in the Czech Republic may register as a single VAT payer (group registration).

Persons identified for VAT

A taxable person who is not a VAT payer can become a person identified for VAT if they purchase a specific type of supply where the place of supply is in the Czech Republic, e.g. they acquire goods from another EU member state, or they supply services where the place of supply is determined in another EU member state under the general rule. The person identified for VAT is obliged to account for VAT on the received supply; however, they are not entitled to claim related input VAT.
Reporting requirements

VAT returns
In general, VAT returns have to be submitted electronically on a monthly basis. Under certain circumstances, VAT payers can opt for a quarterly reporting period. However, for VAT groups and taxable persons whose turnover exceeded CZK 10,000,000 in the previous calendar year, a quarterly reporting period is not possible.

VAT returns must be submitted by the 25th day of the month following the relevant tax period. VAT payers who are not established in the Czech Republic and who do not have a VAT establishment in the Czech Republic and persons identified for VAT are only required to submit VAT returns for VAT periods in which they performed taxable or zero-rated transactions.

VAT must be paid by the VAT return’s due date. If excess input VAT is reported, VAT credit should be paid to the VAT payer within 30 days of the deadline for submitting the VAT return. The VAT returns must be submitted electronically via a special-purpose application.

A penalty applies for non-submission/delays in the submission of a VAT return (max. CZK 300,000) and penalty interest applies for late payment of VAT (14.05 percent p.a.).

EC Sales Lists
An EC Sales List must be completed if a VAT payer or person identified for VAT (where applicable) either:
• supplies goods from the Czech Republic to another EU member state to a person registered for VAT in another EU member state
• moves their own goods from the Czech Republic to another EU member state
• acts as the intermediary in a triangular transaction between VAT registered traders in other EU member states
• provides a service to a customer established in another EU member state, where the place of taxable supply is determined in that EU member state under the general rule.

The EC Sales List should be submitted electronically on a monthly basis, within 25 days of the end of the month in which the supply takes place. Quarterly VAT payers who only provide services as described in point 4 above, may submit EC Sales Lists on a quarterly basis.

VAT Ledger Statement
Since 1 January 2016, Czech VAT payers are obliged to file a VAT Ledger Statement which is considered an effective tool to detect and prevent tax evasion and fraud. The VAT ledger statement is filed electronically on a monthly or quarterly basis (depending on
Indirect taxes

the status of the VAT payer) within 25 days after the end of a VAT period. VAT payers are obliged to report particular data about:
• local supplies;
• local purchases;
• acquisition of goods from another EU member state and supplies acquired from persons not established in the Czech Republic;
• supplies (both received and provided) under the local reverse charge regime.

The VAT Ledger Statement does not substitute for the VAT return or the EC Sales List.

Intrastat declarations
Businesses dispatching goods to or receiving goods from other EU member states and exceeding relevant annual thresholds (CZK 8 million for dispatches or CZK 8 million for goods received) must complete and file Intrastat declarations. Intrastat declarations are submitted on a monthly basis, by the 12th working day of the month following the month for which the declaration is being filed. Intrastat declarations must be submitted electronically. A penalty of up to CZK 1 million may be imposed for failing to submit an Intrastat declaration.

Recovery of input VAT

In general, a Czech VAT payer is entitled to deduct input VAT in respect of received supplies used for the VAT payer’s own business activity. Input VAT can be claimed within three years after the end of the tax period in which the taxable supply was made. A VAT payer must have a VAT invoice to exercise the right to deduct input VAT (a VAT document). A VAT payer is generally not entitled to deduct input VAT on taxable supplies used for VAT exempt supplies, representation (entertainment) or non-business purposes. A partial VAT deduction may be claimed in respect of taxable inputs related to both types of supplies, i.e. those qualifying for deduction of input VAT and those not qualifying for deduction (e.g. exempt supplies or non-business use). The Czech Republic has implemented the general provisions of EU directives in respect of VAT refunds for entities registered for VAT purposes in other EU member states or non-EU businesses. VAT incurred in the Czech Republic is recoverable under the same conditions that apply to Czech VAT payers. The application for a VAT refund should be filed electronically in the state where the taxable person 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. Non-EU businesses can claim refunds of Czech VAT by submitting a written application to the tax authority for Prague 1. Refunds are only made on the basis of reciprocity (currently applicable only for Switzerland, Norway and Macedonia).
Other notes

Local reverse charge for selected transactions
The reverse charge mechanism applies to supplies of gold, scrap materials and waste, construction and assembly works and emission rights effected between Czech VAT payers.

The reverse-charge regime has been extended to include:
• cereal and technical crops, metals, mobile phones, integrated circuits, tablets, laptops, and videogame consoles as of 1 April 2015
• sugar beets as of 1 September 2015
• as of 1 January 2016, supplies of immovable property, unless they are exempt
• supplies of gas and electricity to dealers and supplies of electricity certificates as of 1 February 2016
• selected telecommunication services for entities operating on a wholesale basis as of 1 October 2016
• provision of labour for construction and assembly work or various forms of forced delivery of property (should be effective as of 1 March 2017).

The mechanism shall be applied when the commodities under a) and b) are supplied between two domestic VAT payers and if the total tax base for all of the selected goods supplied exceeds CZK 100,000. The reverse-charge regime could be applied also to supplies below CZK 100,000, if the contracting parties agree on this treatment in writing.

Local supplies of goods effected by a person not established in the Czech Republic
From 29 July 2016, the reverse charge mechanism also applies to local supplies of goods effected by a person not established in the Czech Republic to a Czech VAT payer unless the supplier is already registered as a Czech VAT payer.

Bad debt relief
A VAT payer is allowed to claim a VAT refund for uncollectible receivables (bad debts). Where debtors are under bankruptcy proceedings, VAT refunds should be possible for certain receivables after maturity.

Liability for payment of VAT
As the recipient of a taxable supply, a Czech VAT payer can be liable for VAT from the received supply if it has not been paid by the supplier. The tax authority may demand VAT payment if:
• a supplier intentionally failed to pay VAT and the customer knew or should have known of this fact
• the price for the received taxable supply is clearly and unjustifiably different from the arm’s length price
• consideration for a taxable supply has been remitted to a foreign account
• the supplier has been identified by the tax authority as an unreliable VAT payer or newly as an unreliable entity (the new concept should apply as of 1 April 2017)
• the payment has been made to a bank account not published in the tax authority’s register (liability is only applied if the payment exceeds CZK 540,000, including VAT)
• fuel is supplied by a fuel distributor not published as a registered distributor of fuel at the moment of the taxable supply
• consideration for a taxable supply is provided in a virtual currency such as Bitcoin, Litecoin or CzechCrownCoin (this should apply as of 1 April 2017).

As the Czech Republic is an EU member state, customs matters are governed by EU law. Customs duties are payable on goods imported from outside the EU. Customs rates depend on the type of goods.

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.
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 Czech Act on Excise Duty implements 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. The regime of the suspension exemption can be applied if excise goods are transported to another EU member state or exported.

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. The rules for energy taxes are harmonised within the EU. The rates of energy taxes are fixed at a set amount per unit for each group of products. An exemption from energy tax may be claimed under certain conditions, e.g. if the energy is used in metallurgical or mineralogical processes, the electricity is generated from renewable sources or natural gas and other gases are used for the production of heat for households and heating facilities.
Financial reporting and audit

The disclosure scope of Czech accounting legislation is considerably less demanding than that of IFRS. Under specific conditions, IFRS can/must be used.
Weekend houses

On Friday evenings, many Czechs living in large cities go to their weekend houses in the country. Hence, do not try to arrange business meetings for Friday afternoons, especially during summer. At their weekend houses, Czechs often have barbeques or go mushroom picking.
Financial reporting

Main features of financial reporting
Czech accounting rules are similar to International Financial Reporting Standards (IFRS), but with some significant differences. In particular, Czech accounting rules are much less detailed than IFRS rules.

The Act on Accounting serves as the main framework, and detailed guidance is provided in the Decree on Double-Entry Accounting and the Czech Accounting Standards. Different decrees and standards specify the rules and standards for different types of corporations (accounting units), e.g. companies, sole entrepreneurs, banks, insurance companies and non-profit organisations, as well as municipalities and institutions financed by the state.

All corporations listed in the Commercial Register are obliged to use double-entry bookkeeping. Some specific accounting units not registered in the Commercial Register are permitted to keep simplified accounting records (tax evidence).

All corporations recorded in the Commercial Register are obliged to publish their annual statutory financial statements, annual reports and consolidated financial statements in the Commercial Register; all financial data about all Czech corporations is thus publicly accessible.

The Act on Accounting defines public interests entities in line with EU legislation; i.e. accounting units whose transferable securities are admitted to trading on a regulated market, credit institutions and insurance companies.

All accounting units and groups are categorised depending on the following criteria: net turnover, balance sheet total and average number of employees. In total, there are four accounting unit categories (micro, small, medium and large) and three group categories (small, medium and large).

All accounting records must be in Czech.
All accounting records must be kept and financial statements presented in Czech crowns (CZK).
It is possible to specify a business year-end other than 31 December.
An annual physical count of inventory and fixed assets is required.
The general structure of accounts must be in accordance with the standard chart of accounts.
Statutory financial statements consist of a balance sheet, an income statement (minimally classified by nature), a cash flow statement, a statement of changes in equity and notes.

Different categories of accounting units disclose different information in their financial statements (e.g. the cash flow statement and the statement of changes in equity are mandatory for medium and large entities only; different requirements exist for disclosures in the notes, etc.).
The exact layout, structure and headings of the balance sheet,
the income statement and the cash-flow statement are set in prescribed templates, and minimum disclosures in the notes are prescribed in the decrees. The disclosure scope of Czech accounting legislation is considerably less demanding than that of IFRS. A separate annual report must be prepared by all accounting units that are subject to a mandatory statutory audit. A separate report on payments to governments must be prepared by large entities and public interest entities that are active in extractive industries or in the logging of primary forests. All accounting units with shares or bonds publicly listed in the EU must maintain books and prepare their financial statements in accordance with IFRS, as adopted by the EU. All other accounting units may choose to maintain books and prepare their financial statements in accordance with IFRS if they are consolidated by a parent or an ultimate parent company in accordance with IFRS, or if they have to consolidate, and if they prepare both standalone and consolidated financial statements in accordance with IFRS. The Act on Accounting requires that consolidated financial statements be prepared for an accounting unit that is a controlling entity. Subsidiaries and accounting units over which significant influence is exercised are deemed consolidated accounting units. The obligation to consolidate applies to medium and large groups. Small groups must consolidate only if they include a public interest entity. Consolidation is not obligatory where the consolidating entity is part of another consolidating entity that is governed by the law of an EU member state, and where specific prescribed conditions have been met. However, this rule does not exempt from the obligation to publish consolidated financial statements as mentioned above. A Czech corporation opting not to consolidate has to translate and publish the consolidated financials of its parent or ultimate parent. The above exemption from the duty to prepare consolidated financial statements does not apply to banks, insurers and reinsurers, and publicly listed share or bond issuers. The Act on Accounting also requires that all corporations for which an audit is compulsory (see below) are obliged to prepare an annual report in addition to financial statements. The Act on Accounting as well as some other acts specify the disclosure requirements of the annual report. The financial statements also form an integral part of the annual report. The Act on Corporations requires that all corporations that are part of a group prepare a report on relations between related parties. Where relevant, this report constitutes an integral part of the annual report.
Auditing requirements

Audits are compulsory for:
• large accounting units
• medium accounting units
• small accounting units that are joint-stock companies and that, in both the current and previous accounting period, have met at least one of the following criteria:
  • net turnover exceeds CZK 80 million per annum
  • total assets exceed CZK 40 million
  • the average number of employees exceeds 50
• all other small accounting units that meet at least two of the above criteria in both the current and previous accounting period
• foundations and certain other non-profit organisations.

Audit requirements also apply to annual reports:
• The auditor expresses an opinion on whether the annual report is consistent with the financial statements for the same financial year and whether it was prepared in accordance with legal requirements; or
• the auditor issues only one report which comprises opinions on both the financial statements and the annual report.

The Act on Auditors defines the responsibility of the Chamber of Auditors, which authorises auditors and sets 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 relevant guidance (aplikační doložky) of the Chamber of Auditors of the Czech Republic. Auditors must be appointed by a corporation’s general meeting and its supervisory board is responsible for audit quality supervision. Public interest entities are also defined in the Act on Auditors, which stipulates responsibilities for both public interest entities and their auditors, e.g. audit committees, lead partner rotation, and transparency reports.

The latest amendments to the Act on Auditors implemented EU regulations requiring mandatory firm rotation for public interest entities and imposing limitations on audit/non-audit services provided to public interest entities.
Corporate transactions have become an important feature of the Czech legal environment, making it possible for entrepreneurs to expand or restructure their business activities in the Czech Republic.
Shaking hands

Czechs shake hands both at the beginning and at the end of meetings. A firm handshake and eye contact are vital. A limp handshake or averted eyes are considered impolite. Persons with a higher social status always extend their hand first. Men always stand when shaking hands.
Corporate transactions have become an important feature of the Czech legal environment, making it possible for entrepreneurs to expand or restructure their business activities in the Czech Republic. Mergers and acquisitions are primarily regulated by the Civil Code, the Act on Business Corporations, 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

Although currently not a hot topic, a number of enterprises in sectors such as electricity and transport may still be subject to potential privatisations through sales to strategic investors. The privatisation process is usually initiated by a government decision. All transactions are subsequently carried out by the relevant ministry, generally through a tender.

Ownership of real estate

The Czech Republic does not place any restrictions on real estate ownership.
Acquisition and disposal of Czech legal entities

For foreign individuals and legal entities, no restrictions apply to owning a business or holding shares in Czech companies. Foreign persons may acquire and sell up to 100 percent of the share capital of a limited liability or joint-stock company (most commonly used legal entities). Other legal forms are also available (European Companies, general partnerships, limited partnerships, cooperatives).

The transfer of an ownership interest in a limited liability company must be recorded in the Commercial Register. The shares of certain joint-stock companies are registered with the Central Securities Depository Prague or deposited in escrow at the Central Securities Depository Prague, a bank or other entity entitled to maintain records of investment instruments. In the case of shares traded on the regulated securities market in the Czech Republic or another EU member state, the acquirer is obliged to notify the company (the issuer) and the Czech National Bank if their share of the company’s voting rights exceeds a certain level. In addition, if a shareholder acquires 30 percent or more voting rights, thereby gaining factual control over the company, the shareholder is obliged to bid for the shares of the remaining shareholders.

Purchases of enterprises

An acquisition can also be made by purchasing an enterprise or its parts, with the buyer acquiring the rights, assets and liabilities connected with a running business. The sale and purchase agreement associated with the acquisition of enterprise must be approved by the general meeting or the shareholders of the company.
Contributions to companies

Another way of acquiring a share in a business is by making a financial or non-monetary contribution in the company registered capital. For this purpose, the general meeting of the company must decide on a new share issue. The increase in registered capital is then registered with the Commercial Register court. With some exceptions, non-monetary contributions have to be evaluated by an independent expert listed in a special register.

Transformations of companies (merger, transfer of assets to a shareholder, demerger, change of legal form and cross-border relocation)

If several entities are controlled by one person, it is possible to consolidate or restructure them.

In Czech legislation, mergers fall within the category of transformations of businesses, which also include demergers of companies, transfers of assets to shareholders, any changes in a company’s legal form and cross-border relocations. Transformations of businesses are possible even if the companies are in liquidation or insolvency proceedings. Transformations can be undertaken as national or cross-border transactions with legal entities registered in other EU or EEA countries, including European Companies (Societas Europaea).

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

From a financial point of view, carrying forward the tax losses of wound up companies is generally allowed.

- Mergers are carried out on the basis of merger projects, subject to approval by the general meetings.
- The merger date can be determined either retrospectively or prospectively.
• In some cases, the merger procedure can be significantly simplified.
• In the case of mergers of joint-stock companies, it is possible to allow the voluntary buyout of new shares representing a minority share in the merging company if the successor company owns more than 90 percent of the merging company’s voting rights.

Companies with different legal forms can also merge, and mergers may involve more than two entities. Cross-border mergers are possible; however, a number of special regulations apply. The transfer of assets to a shareholder is a legal form of company transformation in which a company’s assets are transferred to a shareholder owning more than 90 percent of the company’s registered capital and also representing more than 90 percent of the company’s voting rights.

A company can be demerged (divided) through:
1. demerger by formation of new companies
2. demerger by acquisition
3. spin-off connected with new company formation
4. spin-off connected with acquisition
5. a combination of the options mentioned under either 1 or 2 or 3 and 4.

Upon the demerger of a company by formation of new companies or by acquisition, the company being demerged ceases to exist without liquidation, while in a demerger by spin-off, its existence continues. Czech legislation allows a company to change its legal form solely by changing its internal legal structure without having to cease to exist.

Under certain conditions stipulated by Czech legislation, a foreign company with its registered office in another EU or EEA country can relocate to the Czech Republic while a Czech company can relocate to another EU or EEA country.
Public bid for purchase or exchange of participating securities issued by a joint-stock company

If an entity or individual intends to make an offer to more than 100 shareholders or if the volume of requested securities exceeds one percent of the issue of the regulated market, the offer must be made in the form of a public bid. If a 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 CNB that consideration offered for the trade is adequate.

Takeover bids

Voluntary takeover bids
For joint-stock companies traded on the regulated market, investors can make a public offer to the shareholders if the bid allows them to gain control over the company.

Obligatory takeover bids
An investor acquiring 30 percent or more voting rights in a target company traded on the European regulated market thereby gaining factual control over the company, must offer to buy out the other shareholders within 30 days of the acquisition by submitting an obligatory takeover bid.

An obligatory takeover bid may be published only after it has been approved by the CNB.

Obligatory takeover bids are also required if a company decides to remove its shares from trading on the European or other foreign regulated market, or changes the nature of its shares or their transferability.
Right to buy out participation securities (squeeze-out)

A shareholder owning securities representing more than a 90-percent share of the voting rights of a joint-stock company (a major shareholder) is entitled to ask the board of directors to convene a general meeting to decide on the transfer of all the other participating securities owned by minority shareholders, resulting in a squeeze-out of minority shareholders. The general meeting of the company decides on the squeeze-out. An expert valuation has to determine adequate compensation for the minority shareholders. Should the shares be traded on the European regulated market, a document justifying the compensation and prior consent of the CNB are required. Conversely, minority shareholders have the right to request the majority shareholder as defined above buy-out their shares.

Regulations

With regard to mergers and acquisitions, the interests of minority shareholders are protected as companies are obliged to ensure early notification and, for the majority of transactions, the opinion of an independent expert 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, in the banking and insurance sector, for a transaction to come into effect the competent authorities (the CNB and the Ministry of Finance) must give their prior consent.

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 the worldwide net turnover recorded by the other participant exceeded CZK 1.5 billion for the same period.
How KPMG can help

KPMG in the Czech Republic is the advisor of choice for many businesses who have selected the Czech Republic as an investment location.
Being on first name terms versus being on formal terms

Similarly as in French, which distinguishes tu and vous, The Czech language makes a difference between being on a first-name basis (tykání in Czech) and being on formal terms (vykání in Czech). Vykání shows higher respect. The woman or the higher-ranked or older person should be the first to offer the use of first names.
We understand the challenges and pressures faced by those looking to set up business in a new jurisdiction. We can work with you to help you focus on what matters, to avoid pitfalls and unnecessary costs and to ensure your investment projects will start to deliver a measurable return in the shortest possible time frame. We work with both leading names as well as start-up companies in every sector. As a result, KPMG in the Czech Republic has become the advisor of choice to many who have selected the Czech Republic as an investment location, providing all the support required to ensure continued business success. Thanks to the KPMG global network of professional firms, we can also work with you in your home country to maximize the potential of your investment in the Czech Republic.

We can assist in the following areas:

- **Initial assessment and start-up** – a timely, pragmatic and cost effective assessment of the key issues, including the most beneficial corporate and tax structures available, any potential for maximising group taxation benefits on a global basis and available grant assistance. We can also advise on employee benefit issues, e.g. those relating to foreign and Czech state option schemes. We also provide practical business-focused advice and support in dealing with areas such as incorporations and grant application and assessment.

- **Ongoing business** – we offer a broad range of audit, tax, advisory and legal services designed to ensure that investors in the Czech Republic continue to receive timely, proactive and relevant advice and support.
Our services

Audit

• Audits of Czech financial statements
• Audits of financial statements (IFRS, US GAAP, HGB, etc.)
• Audits of financial reports and information
• Audits of prospective financial information
• Review reports
• Reporting on internal control systems
• Sustainability reporting

Tax Services

• Corporate tax
• Indirect tax
• International executive services
• International tax
• Investment incentives and subsidies
• Mergers and acquisitions
• Transfer pricing
• Tax inspections and tax disputes
• Tax services for the financial sector
• Tax outsourcing

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Management Consulting

• Corporate strategy
• Enterprise architecture
• Finance, capital and profit management
• Programme and project management
• People and change
• EU funds advisory
• Marketing advisory
• IT advisory
• Export advisory
• Customers and sales
• Business intelligence (BI) and data management
• Sports and gaming advisory
• Operations management
• Data and analytics

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Risk Consulting

• Accounting advisory services
• Financial risk management
• Internal audit, risk consulting services
• Regional and local authorities and organisations

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How KPMG can help
Deal Advisory

- Corporate finance
- Restructuring
- Transaction services
- Forensic

Accounting Services and Payroll

- Management reporting
- Financial accounting
- Payroll outsourcing
- Administrative support

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Legal Services

- Corporate law
- Transactions and restructuring
- Labour law
- Regulatory issues

Our priority sectors:

- Automotive
- Banking
- Building, Construction and Real Estate
- Consumer Markets
- Energy
- Food and Drink
- Government and Public Sector
- Healthcare
- Industrial Manufacturing
- Insurance
- Middle Markets
- Retail
- Sports and Gaming
- Telecommunications
- Transportation
- Travel, Leisure and Tourism

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Our foreign desks:

- Chinese Desk
- German Desk
- Japanese Desk
- Korean Desk
- Russian Desk
KPMG in the Czech Republic

- Prague
- Brno
- Ostrava
- České Budějovice

KPMG has been active in the Czech Republic since 1990, when the first office in Prague was opened. Currently, KPMG Czech Republic has over 900 employees and offices in Prague, Brno, České Budějovice and Ostrava. KPMG Czech Republic provides Audit, Tax, Advisory and Legal services. As a member of a global network of professional firms, KPMG Czech Republic can draw on the knowledge and experience of more than 174,000 experts working in 155 countries. The independent member firms of the KPMG network are affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. Each KPMG firm is a legally distinct and separate entity and describes itself as such.
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