

Doing Business in the Czech Republic

2012



BAKER & MCKENZIE

Preface

Baker & McKenzie is one of the world's largest law firms with its presence in 70 locations in 42 countries. We have been active in the Czech Republic since 1993 and our work includes a full range of legal and tax services directed primarily to foreign investors doing business in the Czech Republic, but also, increasingly, to large, domestic Czech companies, especially as they seek to expand into new markets.

Over the past 10 years, the Czech Republic has adopted new laws in virtually every area of regulation in the Czech legal system consistent with European standards as it prepared for accession to the European Union. The Czech Republic formally joined the European Union on May 1, 2004 and its legal system continues to develop in line with European norms.

Doing Business in the Czech Republic has been prepared by the Prague office of Baker & McKenzie as a general guide for those companies or persons who wish to engage in business activities or invest in the Czech Republic.

The information contained in this publication is general in nature and is intended only to provide an introduction to the Czech legal system and investment climate. This publication may not be relied upon in relation to any transaction or investment decision and it should not be viewed as a substitute for specific legal and tax advice. In addition, readers should be aware that the law and its interpretation are constantly changing in the Czech Republic; as such, the information contained in this publication may quickly become outdated.

We would be pleased to provide you with updates on the material contained in this guide, or to provide you with further information regarding a specific industry or area of Czech law in which you have a particular interest.

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1. The Czech Republic

1.1 Key Facts

Area	78,866 km ²
Population	10.5 million (approx.)
Labor force	4.929 million (approx.)
Capital	Prague
Language	Czech
Currency	Czech Crown (CZK)

The Czech Republic is located in the heart of Europe, neighboring Germany (to the west), Poland (to the north), Slovakia (to the east), and Austria (to the south). The country is comprised of three historically defined regions: Bohemia, Moravia and Silesia. It has a population of approximately 10.5 million, which is comparable to other medium-sized European nations (e.g. Hungary, Austria). Approximately one-fourth of the population lives in the five largest cities: Prague, Brno, Ostrava, Plzen and Olomouc. The capital city, Prague, has approximately 1.2 million inhabitants. Prague has historically been regarded as the “geographic center” of Europe. Its cobblestone streets form a maze of cozy restaurants, shops, galleries and bars. Prague has excellent conference facilities, hotels with the latest business services and an economy that makes doing business here advantageous.

The Czech Republic is a parliamentary republic. The National Legislature consists of two houses: the lower house, the Chamber of Deputies, which has 200 members and the upper house, the Senate, having 81 members. The electoral system declares universal direct suffrage for party proportional representation, subject to a 5% threshold. The Czech Republic is divided into 14 regions (Higher Territorial Self-governing Units – Vyssi uzemne-spravni celky - VUSC in Czech), which came into effect on January 1, 2000. The regions are newly further subdivided into 206 Districts of the Municipalities with Extended Authority (Obvody obci s rozsirenou pravomoci in Czech). Selected competencies are being transferred from the central government to self-governing regional councils.

Czech history has always been interwoven with the history of Europe. Prior to World War I it was an integral part of the Hapsburg Empire. In 1918, after the defeat of the Austrian-Hungarian Empire, several centuries of Hapsburg rule came to an end with the birth of independent Czechoslovakia, uniting the Czechs and Slovaks into a one nation-state. During the inter-war years, the First Republic (as it is referred to) was a rapidly developing industrial society, with a stable democratic system of governance and a vibrant cultural and intellectual life. However, the Munich Agreement, signed in October 1938, essentially sealed Czechoslovakia’s fate and led to its occupation by Nazi Germany in March 1939. At the end of the war, Czechoslovakia fell into the *de facto* sphere of Soviet influence. From 1948, the Communist Party took full control of the state and Soviet dominance extended for the next 40 years. In 1989, the Soviet empire in Europe began to crumble, and on November 17, communism in the Czech lands gave way to the popular and peaceful demonstrations known as the Velvet Revolution. In 1993, Czechoslovakia underwent a “velvet divorce” and peacefully dissolved into the Czech and Slovak Republics.

Although not without setbacks, the Czech Republic has made great progress in its transition to a pluralistic, democratic and market-oriented society. The country boasts a highly skilled and educated workforce and foreign direct investment has increased each year, especially since the introduction of large-scale investment incentives by the Czech government in 1998, enacted into law by Act No. 72/2000 Coll. The Czech Republic became a member of the European Union on May 1, 2004 and currently has one of the lowest unemployment rates in Europe.

1.1.1 Political and Economic Stability

The Czech Republic is a fully-fledged parliamentary democracy with one of the most advanced transition economies. Economic policy is consistent and predictable. A strong and independent Central Bank (Czech National Bank) has maintained an extraordinary degree of currency stability since 1991. The Czech Republic was the first CEE country to be admitted into the OECD. The country is a member of NATO and is fully integrated into other international organizations such as the WTO, IMF and EBRD.

EU legislation was adopted in preparation for EU accession; commercial, accounting and bankruptcy laws are compatible with Western standards.

The Czech koruna is fully convertible. All international transfers (e.g. profits and royalties) related to an investment can be carried out freely and without delay.

1.1.2 Non-Discrimination

Under Czech law, foreign and domestic entities are treated identically in all areas; from protection of property rights to investment incentives. The government does not screen any foreign investment projects, with the exception of those in the defense and banking sectors.

As an OECD member, the Czech Republic is committed to non-discrimination against foreign investors in privatization sales, with the same aforementioned exceptions.

1.1.3 Investment Protection

The Czech Republic is a member of the Multilateral Investment Guarantee Agency (MIGA), an international organization for the protection of investment, belonging to the World Bank-IMF group. The country has signed a number of bilateral international treaties which support and protect foreign investments, for example, with the United States, Germany, UK, France, Austria, Switzerland, Italy, Belgium, Luxembourg, The Netherlands, Finland, Norway and Denmark.

These treaties provide that each party shall permit and treat investments, and associated activities of the other party's residents, on a non-discriminatory basis and guarantee full protection and security by law. The full text of each respective treaty is available in Czech and the official language of the other country only. The Czech version can be obtained from the Collection of Laws of the Czech Republic. The other language version is available from the authorities of the other involved country, such as their embassy.

The Czech Republic has also concluded agreements for the avoidance of double taxation – see the section on Repatriation of Profits below.

1.1.4 Protection of Property Rights

The Czech Republic is a signatory to the Bern, Paris, and Universal Copyright Conventions. Existing legislation guarantees the protection of all forms of property, including patents, copyrights, trademarks and semiconductor chip layout design. Trademark law and copyright law are compatible with EU directives.

The only case where the property of a foreign person or entity could be expropriated in the Czech Republic would be on public interest grounds that could not be satisfied by any other means, which would then have to be through an Act of Parliament and with full compensation at market value. No expropriation of the property of a foreign investor has taken place since the Velvet Revolution in 1989.

1.1.5 Repatriation of Profits

No limitations exist concerning the distribution and expatriation of profits by Czech subsidiaries to their foreign parent companies other than the obligation of joint stock and limited liability companies to generate a mandatory reserve fund and pay withholding taxes.

The Czech Republic has treaties to prevent double taxation with many countries, including all EU countries, Switzerland, the USA, Canada, Japan and Australia. A full list of countries is available from the Ministry of Finance.

Double taxation treaties cover taxes on dividends, interests and royalties. Actual rates of withholding tax are determined by the treaty and range from 0 to 15 per cent. The exact method of double taxation prevention must be determined by reference to the actual treaty between the Czech Republic and the other concerned country.

1.1.6 Investment Risk

An open investment climate has been a key element of the Czech Republic's economic transition. The country's investment grade ratings, from international credit rating agencies, and its early membership in the OECD, testify to its positive economic fundamentals.

2. Corporate Registration and Compliance

2.1 Forms of Business Vehicles

The Czech Commercial Code recognizes a variety of legal entities and forms of business vehicles (some of which, such as the branch office, are not legal entities) under which it is possible to do business in the Czech Republic.

The legally recognized entities or registered forms of business vehicles that are typically utilized and encountered by foreign investors are:

- (i) Limited liability company (commonly referred to as “s.r.o.” or a “spol. s r.o.”) (společnost s ručením omezeným);
- (ii) Joint stock company (commonly referred to as “a.s.” or an “akc. spol.”) (akciová společnost);
- (iii) Limited commercial partnership (commonly referred to as “k.s.” or a “kom. spol.”) (komanditní společnost);
- (iv) General commercial partnership (commonly referred to as “v.o.s.” or a “veř. obch. spol.”) (veřejná obchodní společnost);
- (v) Branch office (organizační složka);
- (vi) Cooperative (družstvo);
- (vii) European company (evropská společnost);
- (viii) European cooperative company (evropská družstevní společnost); and
- (ix) Sole entrepreneur (fyzická osoba - podnikatel).

All of the above vehicles need to be registered in the Commercial Register.

In addition, Czech law provides for the possibility of establishing associations of legal entities (sdružení). Such associations, however, are not legal entities and do not need to be registered.

2.1.1 Limited Liability Company

The principal features of a limited liability company are:

- (i) No shares are issued to the participants; rather, the participants acquire a participation interest (also referred to as a quota or ownership interest) in the limited liability company, which can then be transferred by notarized agreement (subject to any transfer restrictions or pre-emption rights contained in the limited liability company’s constituent document or the Czech Commercial Code); a participation interest may only be divided in connection with its transfer (such division is to be recorded by a notarial deed);
- (ii) A limited liability company has no board of directors; instead, the company is represented by one or more executives. There is no need to establish a supervisory board;
- (iii) Minimum capitalization is 200,000 Czech crowns (“CZK”). If there is one participant, the initial capital must be fully paid by the time of submission of the petition for incorporation into the Commercial Register. If there are two or more participants, at least CZK 100,000 of

the registered capital and 30% of each participant's initial capital must be paid by the time of submission of the petition for incorporation (the remainder of the initial capital must be paid within 5 years of registration of the s.r.o. in the Commercial Register). The minimum contribution of each participant is CZK 20,000;

- (iv) If the limited liability company is to have one participant only, the company can be formed on the basis of a simple notarial deed, with no need to prepare a detailed and lengthy constituent document; if there is to be more than one participant, a memorandum of association must be prepared in the form of a notarial deed;
- (v) There must be a minimum of one, and a maximum of fifty, participants;
- (vi) Liability of the participants in a limited liability company is limited (up to the total of the unpaid contributions to the registered capital of the s.r.o. as registered in the Commercial Register);
- (vii) A limited liability company is not a flow-through entity for Czech tax purposes;
- (viii) Czech law prohibits the "chaining" of limited liability companies, i.e. a structure when a limited liability company with a sole participant is a sole participant in another limited liability company;
- (ix) One participant, being a natural person, may be the sole participant of a maximum of three limited liability companies; and
- (x) A participation interest in a limited liability company can be pledged.

2.1.2 Joint Stock Company

The principal features of a joint stock company are:

- (i) Capital stock is divided into shares which may be issued in the form of a bearer or registered share ("Shares"). Bearer shares are transferable by physical delivery and their transferability cannot be restricted. Limitation of transferability of registered shares is possible; such limitation must be included in the Statutes of the joint stock company. The Shares can be issued as certified shares or can be maintained in the form of book-entry (computer entry) securities in a special account at the Central Securities Depository, which is maintained by the joint stock company Centrální depozitář cenných papírů, a.s. The identity of the shareholder is not stated on the certified bearer shares. However, the identity of shareholders holding shares exceeding 10% of the registered capital has to be known by the company in order to take part in public procurement procedures, as the rules on public procurement require the submission of a list of such shareholders. The shares in the joint stock company may be pledged;
- (ii) A joint stock company has a board of directors consisting of at least three members. Should the joint stock company be established by a single shareholder, the board of directors may consist of less than three members. The term of office of individual members of board of directors is to be stated in the Articles of Association and may not exceed five years. Ex-members can be reappointed;
- (iii) A joint stock company has a supervisory board consisting of at least three members (the number of members of the supervisory board must always be divisible by three). The term of office of individual members of a supervisory board is to be stated in the Articles of Association and may not exceed five years. Ex-members can be reappointed;

- (iv) The minimum capitalization of a joint stock company (formed without public offering) is CZK 2,000,000. The minimum capitalization of a joint stock company formed by public offering is CZK 20,000,000;
- (v) It is possible for a single shareholder (being a legal entity and, commencing January 1, 2012, also being an individual) to establish a joint stock company. There is no maximum limit as to the number of shareholders;
- (vi) The nominal value of preference Shares must not exceed 50% of the registered capital of a joint stock company. Preference Shares may be voting or non-voting;
- (vii) Convertible bonds and preference bonds may be issued up to an amount equal to 50% of the registered capital;
- (viii) It is not possible to issue same classes of ordinary Shares with different rights attached to them;
- (ix) Shareholders are not liable for the company's obligations (the company is liable by its assets);
- (x) A joint stock company is not a flow-through entity for Czech tax purposes; and
- (xi) At least one third of the members of the supervisory board must be elected by employees, if a joint stock company has over fifty employees working for a period exceeding half a working week (i.e. more than 20 hours per week), as of the 1st day of the accounting period in which the general meeting electing the members to the supervisory board takes place.

2.1.3 Limited Commercial Partnership

The principal features of a limited commercial partnership are:

- (i) At least one limited partner and one general partner must found the partnership. The minimum contribution for a limited partner is CZK 5,000. The limited partner(s) is/are liable up to the amount of his/her/their unpaid contribution(s) to the registered capital registered with the Commercial Register; general partner(s) face/s unlimited liability regarding the obligations of the partnership;
- (ii) Only general partner(s) is/are authorized to carry out commercial management of the partnership; and
- (iii) A limited commercial partnership is a flow-through entity, with regard to the general partner, for Czech tax purposes.

2.1.4 General Commercial Partnership

The principal features of a general commercial partnership are:

- (i) At least two partners are required to establish a general partnership and each partner is jointly and severally liable for all of the obligations of the partnership;
- (ii) Profits are shared equally among the partners; and
- (iii) The partnership is a flow-through entity for Czech tax purposes.

2.1.5 Branch Office

The principal features of a branch office are:

- (i) A branch is not a separate legal entity, i.e. it does not have a legal capacity under Czech law (except labor law area) and its capability to make any legal acts and perform any steps is derived from the legal capacity of its founder;
- (ii) Activity of the branch is dependent on directions and instructions of its founder. The business activities carried out in the Czech Republic by the branch must not exceed the scope of business activities which may be carried out by the founder;
- (iii) The branch may not be sold or merged with another branch unless the founders are sold or merged at the same time. It is possible to sell the enterprise or the assets of the branch;
- (iv) The branch is founded by a simple resolution of the founder of the branch. The formal requirements for such resolution (if any) are prescribed by the law of incorporation of the founder;
- (v) There are no capitalization requirements for a branch;
- (vi) Subject to the provisions of any applicable tax treaty, a branch would be subject to Czech taxation on all income attributed to the activities of the branch;
- (vii) A branch is required to maintain its books according to Czech accounting standards and on an accrual basis; and
- (viii) The head of the branch, registered in the Commercial Registry, is authorized to perform on behalf of the founder all legal acts regarding the branch.

2.1.6 Choice of Entity or Vehicle

Most foreign investors utilize a limited liability company, joint stock company, or branch as the vehicle for carrying out their business activities in the Czech Republic.

The principal advantage of a branch office is that there are no capitalization requirements. The disadvantage of a branch is that it is not a separate legal entity, thus exposing the offshore “parent company” to direct liability for actions by the branch.

The choice between an s.r.o. and an a.s. often depends on the following factors:

	s.r.o.	a.s.
Minimum Capital	CZK 200,000	CZK 2,000,000 (or CZK 20,000,000 in case of public offering)
Minimum No. of Appointments Required	1 (executive)	6 (3 members of the board of directors and 3 members of the supervisory board) (in the case of an a.s. with single shareholder, only 1 member of the board of directors is sufficient)
Supervisory Board	Optional	Mandatory
Listed on a recognized Czech Stock Exchange	No	Optional

	s.r.o.	a.s.
Registered at the Central Securities Depository	No	Depending on the form of shares

2.2 Corporate Governance

The Commercial Code stipulates a six month period after termination of the relevant accounting period for the General Meeting to approve the ordinary financial statements for the relevant accounting period.

In the case of a **limited liability company**, the General Meeting of participants adopts resolutions by a simple majority of votes of the participants present, *unless* either: (i) a provision of law, or (ii) the s.r.o.'s memorandum of association, requires a higher number of votes. A quorum is constituted if participants having at least half of the votes are present at the meeting (unless the memorandum of association requires a higher quorum).

In the case of a **joint stock company**, the General Meeting of shareholders also adopts resolutions by a majority of votes of the shareholders present, *unless* the Commercial Code requires a different (i.e. not necessarily higher) majority. The articles of association of an a.s. may require a higher number of votes in order to adopt a resolution than is required by law. A quorum is constituted if the shareholders who are present hold shares with a total nominal value exceeding 30% of the registered capital of the a.s., if the articles of association of the a.s. do not require a higher quorum.

The execution of any contract pursuant to which a limited liability company or joint stock company will, during the course of one accounting period, sell or acquire assets whose value exceeds one third of such entity's own equity would require the approval of the entity's supervisory board.

The Commercial Code further regulates loan/credit agreements to be concluded between a limited liability company or a joint stock company and its executive(s), member(s) of the board of directors, member(s) of the supervisory board, procurist or other person authorized to execute such agreement or other related person(s); an agreement can only be concluded upon the prior consent of the General Meeting of the relevant company. The same applies for agreements according to which a company's asset is transferred free of charge in favor of such persons.

The Commercial Code also contains regulations on the transfer of assets between a controlling and a controlled entity, its founder, its shareholder, persons acting in concert or other persons described in the previous paragraph. Should the amount of such asset exceed one tenth of the subscribed registered capital, the value of such asset must be evaluated by virtue of an expert elected by the court. Such transfer must also be approved by the General Meeting of the relevant company should the transfer take place within 3 years after its incorporation.

The following business entities are required to be statutory audited:

- (i) joint stock companies if, in the year subject to audit and in the previous year, at least one of the three below stated criteria have been met;
- (ii) other business entities (including branches and limited liability companies) and individual entrepreneurs if, in the year subject to audit and in the previous year, at least two of the three following criteria have been met:
 - balance sheet total amount exceeding CZK 40,000,000;
 - net turnover exceeding CZK 80,000,000;

- adjusted number of employees exceeding 50.

Data mailboxes, accessible through the internet and operated in Czech language only, serve as electronic deposits of documents originating with state administrative bodies, on one side, and as a platform for sending documents to state administrative bodies on the other. Data mailboxes are established automatically and free of charge for legal entities registered in the Czech Commercial Register and subsidiaries of an enterprise of a foreign legal entity registered in the Commercial Register. Generally, a document is deemed to have been delivered at the moment of log-in of the individual entitled to access the data mailbox; or if log-in does not occur within 10 days from delivery of the document into the data mailbox, the document is deemed to have been delivered on the last day of this 10 day period - save for certain cases when such substitute delivery is excluded by statute.

Commercial Documents. Each entrepreneur is required to state its business name, seat or place of business and identification number on all orders, invoices, business correspondence and, additionally, in agreements as well as in the scope of information made available to the public by means of remote access (web pages). In case the entrepreneur is registered in the Commercial Register, it should also give details of such entry, including the relevant file number. Information about the amount of registered capital may only be stated in commercial documents and on web pages if the registered capital has been fully paid up.

A **related parties report** must be prepared by the company's statutory body and should be dated no later than 3 months after the end of the accounting period of the company. This report should state what agreements were concluded between related parties during the last accounting period, what other legal transactions were made in the interests of these parties, and all other measures which were adopted or came into effect in the interest, or at the initiative, of the controlled entity. If some performance was supplied by the controlled entity, the report should also mention what consideration was effected and the advantages and disadvantages of the measures taken, and whether any detriment arose to the controlled entity from said agreements or measures, and whether such detriment was settled in the accounting period or whether an agreement on its settlement was concluded. Finally, this report should also state the relationships between the controlled entity and other entities controlled by the same controlling entity.

Filing. The annual General Meeting approves the financial statements. The financial statements and the related parties report must then be filed with the Collection of Documents of the relevant company maintained by the Commercial Register. If the company's financial statements must be audited, the auditor's report, as well as the annual report of the company, must also be filed with the Collection of Documents. Such filing has to be done within 30 days following approval of the auditor (if appropriate) and the annual General Meeting. In any event, i.e. even if the auditor and/or the General Meeting fail to approve the financial statements and the annual report, the company must file these documents with the Collection of Documents in the Commercial Register by the end of the next accounting period (year).

2.3 Requirements for Members of Statutory and Supervisory Bodies

An executive of a limited liability company, a member of board of directors of a joint stock company, or a supervisory board member, may only be an individual (a natural person) who has attained the age of 18, is fully legally competent, is of unimpeachable character (in the meaning of the Trades Licensing Act) and if there is no impediment to his/her carrying on a trade within the meaning of the Trades Licensing Act. Such conditions are proved by an extract from the Criminal Register of the relevant country (depending on his/her citizenship).

Non-Czech citizens may be appointed as executives or members of a board of directors or supervisory board. A residency permit or visa is not required for purposes of their registration in the Commercial Register.

The authorized representative of a branch office, if non-Czech, also does not need to possess a long-term residence visa or permanent residence permit for the Czech Republic for his/her registration with the Commercial Register.

2.4 Trade Licenses

Most business activities (whether carried out by a branch, an a.s., or an s.r.o.) require issuance of a trade license by either the business license department of the district or the municipal office in the district or municipality in which the registered office of the branch or legal entity is located (the “Office”). The type of trade license required depends on the scope of business of the branch or legal entity. Certain activities, such as banking, insurance and broadcasting, require special licenses issued directly by the relevant state authority.

A so-called “responsible person” is required for certain trade licenses. The trade license responsible person:

- (i) does not need to be in an employment relationship with the company (trade license holder) - any kind of contractual relationship with the company is acceptable; however, a trade license responsible representative cannot be a member of the supervisory board of the company (trade license holder);
- (ii) does not have to be a resident of the Czech Republic (does not need a permanent residency address); and
- (iii) does not need to prove his/her knowledge of the Czech or Slovak languages (trade license holders selling goods or providing services to consumers in an establishment/shop must have a Czech or Slovak speaking person present in their place of business).

Please note that there are two categories of trades: “notifiable” trades, which might be carried out by virtue of a notification to the relevant Office and “concession” trades, which might be carried out by virtue of a concession granted by the relevant Office. To engage in business activities that fall within the scope of “notifiable” trades, the applicant needs only to notify the relevant Office (in the prescribed form) that it intends to engage in such activities. Notification alone is sufficient to allow the company (applicant) to commence such activities. On the other hand, business activities that fall within the scope of “concession” trades may be undertaken only after permission (concession) is granted by the relevant Office. In the case of a newly incorporated entity, authorization to carry out business activity originates, at the earliest, as of the day of registration of the new entity in the Commercial Register.

The following types of business activities are classified as “notifiable trades”:

- (i) unregulated trades (e.g. the purchase and sale of goods, consulting services);
- (ii) crafts (e.g. woodwork, metalworking, printing, leatherworking); and
- (iii) regulated trades (including professional qualifications) (e.g. engineering, production of electrical equipment).

For craft, regulated trades and concession trades, the responsible person must possess certain educational and practice requirements. For unregulated trades, no special requirements are required;

thus, the acquisition of trade license(s) for these trade(s) is subject to minimal requirements and is the “simplest” trade license to obtain.

2.5 Foreign Exchange

Under the current regulations, every direct investment in the Czech Republic by a non-resident must be notified to the Czech National Bank. As of January 1, 2004, such notification is no longer required if the value of the direct investment is less than CZK 1,000,000.

Under the Foreign Exchange Act, a direct investment is defined as the use of funds or other ownership rights to which a monetary value can be attributed, as well as other assets to establish, acquire or increase the long-term economic interests of a non-resident (or non-residents acting in concert) in a business in the Czech Republic; particularly in one of the following forms:

- (i) establishment or acquisition of a majority shareholding (controlling interest) in a business, including any expansion of a business;
- (ii) participation in a new or existing business where the investor owns or acquires 10% or more of the registered capital of a trading company or co-operative, or 10% or more of the equity capital of a company, or 10% or more of the voting rights, or any other share in excess of 10% in the business of a company;
- (iii) any other provision or acceptance of funds or other assets or ownership rights to which a monetary value can be attributed as part of long-term economic interests established by direct investment;
- (iv) a financial credit associated with a profit distribution agreement or with the exercise of a significant influence over the management of business; and
- (v) the use of profits from an existing direct investment in the same investment (re-investment of earnings).



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3. Taxation

3.1 General Overview

3.1.1 Applicable Taxes

The following taxes apply in the Czech Republic:

- (i) Income Tax, which is divided into (a) Personal Income Tax and (b) Corporate Income Tax;
- (ii) Value Added Tax;
- (iii) Excise Duties (on hydrocarbon fuels, spirits, tobacco, beer and wine);
- (iv) Road Tax (on road vehicles used for business purposes);
- (v) Environmental Taxes;
- (vi) Inheritance Tax;
- (vii) Gift Tax;
- (viii) Real Estate Transfer Tax; and
- (ix) Real Estate Tax.

No stamp/registration duties or capital increase/contribution duties currently apply in the Czech Republic. Environmental Taxes (excise duties on some other fuels (coal, gas, electricity) were introduced as of January 1, 2008.

3.1.2 Tax Authorities and Tax Ruling

Taxation is administered by district “Financial Offices” which report to regional “Financial Directorates.” The General Financial Directorate acts as the supreme tax authority. Decisions of tax authorities may be reviewed by administrative courts. A decision from regional administrative courts may be reviewed by the Supreme Administrative Court.

Czech tax authorities do not issue any individual legally binding tax rulings (with minor exceptions). Furthermore, legally binding guidelines are not issued regarding individual bodies of tax law. The General Financial Directorate issues general guidelines interpreting some provisions of tax law. These guidelines should be binding for tax administrators, though not for taxpayers, but are also practically followed by taxpayers.

3.1.3 Tax Audits

Tax authorities may perform a tax audit and reassess tax for up to three years following the date on which the tax return was due. This time period is automatically extended for a new three-year period as a result of a tax audit. The time period is also automatically extended by an additional 1 year if, in the last 12 months, the taxpayer filed additional tax return, the decision of the tax authorities or appeal decision was delivered to the taxpayer, or certain other circumstances occurred; nonetheless, tax cannot be re-assessed when a period of 10 years expires following the year when the tax return was due. A special time period applies for taxpayers in a tax loss position.

3.1.4 Tax Penalties

- Penalty of 0.05% of actual tax liability for each day (up to 5% of actual tax liability, maximally up to CZK 300,000) when a tax return is filed after the statutory deadline.
- Compensation for non-fulfillment of registration duty for VAT at 10% of the taxpayer's turnover for taxable supplies rendered during the period when the taxpayer failed to register for VAT purposes.
- Penalty of 20% when a taxpayer's tax liability is increased or its tax deduction is reduced by the tax authorities during a tax audit.
- Penalty of 1% if the tax authorities reduce the amount of a taxpayer's tax losses.
- Interest for late payment of tax of the repo rate of the Czech National Bank (currently approximately 0.75% per annum), increased by 14 percentage points. Interest on late payments may be assessed for a maximum of five years.
- For tax liabilities which have arisen by the end of 2006, the above tax penalties do not apply and a tax penalty of interest for 0.1% per each day for late payment of properly reported tax applies instead; decreased to 0.05% per each day for tax paid under a supplementary tax return; increased to 0.2% per each day for tax paid under a tax assessment resulting from a tax audit of the Financial Office. These rates apply for the first 500 days, following which a penalty rate of 140% of the discount rate of the Czech National Bank applies until the due tax is settled.

3.2 Corporate Income Tax

3.2.1 Scope of Taxation

For Czech legal entities, as well as foreign entities whose place of management is in the Czech Republic ("Czech tax residents"), income subject to taxation is generally gross worldwide income (excluding tax exempt income), less tax deductible expenses, less non-taxable revenue and allowable deductions.

3.2.2 Partnerships

A special tax regime applies to general partnerships and limited partnerships, which are partly or entirely "transparent" companies for Czech tax purposes. Income of general partners is taxed at the partner's level, whereas income of limited partners is taxed at the company's level, with a potential withholding tax on distributed dividends in certain cases.

3.2.3 Permanent Establishment

Branches of foreign entities are generally regarded as permanent establishments of foreign enterprises for Czech tax purposes. Tax authorities may deem the profit of a branch to be that of a similar sized entity if it is not possible to ascertain the actual profit attributable to activities of the branch in the Czech Republic. A special method of taxation could be granted to "non-trading" branches by tax authorities.

The concept of a permanent establishment is broadly defined in the Czech Income Taxes Act, as well as in the double tax treaties concluded by the Czech Republic. Nonetheless, besides the fixed place of business through which the business of a foreign enterprise is carried out, a permanent establishment is also deemed to exist in a case of provision of services on the territory of the Czech Republic for a

period exceeding six months in any twelve month period (this period is modified by some double tax treaties).

3.2.4 Tax Rates

Income generated by legal entities is subject to a corporate tax rate of 19% for tax periods beginning in 2011 or later. A special tax rate of 5% applies for income of investment, mutual and pension funds. Capital gains of legal entities are treated as ordinary income and taxed at the standard rate of 19%, but participation exemption is also available in certain cases.

3.2.5 Source of Income

Czech tax residents are subject to Czech income tax on their worldwide income. Czech tax non-residents are subject to Czech income tax only on their Czech sourced income, which is deemed to be as follows, regardless of who pays such income (with the exception of point (e)):

- (a) Income derived from activities carried out by a permanent establishment;
- (b) Income derived from services (with the exception of construction assembly projects), including income from commercial, technical or other consultancy services, managerial or intermediary services and similar kinds of services provided in the Czech Republic;
- (c) Income generated from the sale of real estate situated in the Czech Republic and rights related thereto;
- (d) Income generated from use of real estate (or its parts), including flats (or their parts) situated in the Czech Republic;
- (e) Income derived from Czech tax residents and from Czech permanent establishments of Czech tax non-residents, which are:
 - (i) Payments for the right to use, or for using, someone else's intangible industrial (intellectual) rights, software, production and technological know-how and other economically exploitable know-how;
 - (ii) Payments for the right to use, or for using, copyrights, or rights similar to copyrights;
 - (iii) Shares in profits, settlement shares, liquidation shares in business entities, including co-operatives, other income derived from capital and a proportion of after-tax profits paid to a silent partner. Shares in profits shall also mean an income of unjustified differences between an agreed price and the usual arm's length price in transactions between related persons, as well as interest expense to be considered as tax non-deductible as a result of the thin capitalization rules;
 - (iv) Interest and other yields on credits and loans, deposits and securities;
 - (v) Income derived from the use of a movable asset, or its part, in the Czech Republic;
 - (vi) Income derived from the sale of movable assets being included in the business property of a permanent establishment, securities issued by taxpayers whose registered office is in the Czech Republic, property rights registered in the Czech Republic and an ownership interest or share in a business entity having its registered seat in the Czech Republic;

- (vii) Income of the shareholder of a business entity derived in relation to a decrease of registered capital;
 - (viii) Income from settlement of a receivable acquired through assignment; and
 - (ix) Contractual penalties;
- (f) Income from the sale of participation in a Czech resident entity.

The aforementioned regulations of Czech sourced income subject to Czech income tax could be modified by a relevant double tax treaty.

3.2.6 Tax Base

Tax base is based on economic result, calculated based on Czech statutory accounting standards and adjusted by non tax-deductible expenses and non-taxable incomes. A tax base may also be deducted by certain tax base allowances (e.g. charity donations). Tax liability calculated from a final tax base may be reduced by certain tax allowances (e.g. allowances for handicapped employees).

3.2.7 Tax Deductible Expenses

Generally, any expense can be deducted for tax purposes provided that it has been incurred to generate, maintain and secure taxable income and that the tax payer is able to prove that occurrence. This general definition is accompanied by a non-exhaustive list of expenses, which are expressly stated as tax deductible. Deductible expenses include, for example:

- Tax depreciation of tangible assets and tax amortization of fixed intangible assets (for intangible fixed assets various statutory provisions apply based on the year of acquisition of the asset);
- Tax net book value of tangible and intangible assets upon their disposal by way of sale or liquidation;
- Mandatory health and social security payments made by employers (provided that they have been paid no later than one month after the statutory deadline);
- Rental paid for lease of business premises (subject to certain restrictions when a leased asset is purchased by the tenant);
- Financial leasing installments (subject to certain regulated limits) and ordinary leasing installments;
- Certain taxes paid (including real estate and real estate transfer taxes, but excluding inheritance taxes, gift taxes and income taxes);
- Bank and other professional fees (e.g. brokerage fees for securities trades, organization of employers), but excluding company associations fees (e.g. chambers of commerce participation fees);
- Business trip expenses (e.g. expenditure on accommodation, travel expenses and meal allowances up to certain statutory limits); and
- Employee benefits (e.g. severance payment payable upon termination of employment caused from the employer's side) which arise out of any internal company regulation, a collective

bargaining agreement with any applicable union or employment or other agreement, unless tax law stipulates otherwise for some kind of benefits; employee benefits are provided under employment agreements only when provided for work performed.

3.2.8 Tax Non-Deductible Expenses

Some tax non-deductible expenses are also expressly defined. This non-exhaustive list of tax non-deductible expenses include, *inter alia*:

- Loss from sale of a receivable decreased by created statutory bad debt provisions;
- Expenses on the holding of a share in a subsidiary, including interest expenses;
- Benefits of members of a company's statutory body (this applies only to the statutory bodies of joint stock companies); and
- Taxes paid on behalf of another taxpayer.

3.2.9 Tax Depreciation

Tangible fixed assets with a price exceeding CZK 40,000 and with an operational life of more than one year are depreciated annually (with minor exceptions). The minimum tax depreciation period varies according to the depreciation group into which that particular tangible asset is classified. Currently, Czech tax law divides tangible fixed assets into seven categories, with depreciation periods ranging from 3 to 50 years. Tangible fixed assets are generally depreciated up to the acquisition value.

Two tax depreciation methods are generally available: a straight-line method and an accelerated method. The choice of method must be made on an asset-by-asset basis and, once made, cannot be changed. Certain assets may not be depreciated (e.g. natural resources, plots of land).

Similarly, intangible fixed assets with a price exceeding CZK 60,000 and with an operational life of more than one year are depreciated on a monthly basis (with minor exceptions). The depreciation periods range from 18 to 72 months.

Expenditures for technical improvements to fixed assets exceeding a certain threshold increase the acquisition/residual value of the asset and must be depreciated together with the improved asset; a special regime applies to improvements of leased assets financed by the lessee and when the improvement could be depreciated by the lessee as a separate fixed asset.

3.2.10 Tax Loss Utilization

Tax base may be reduced by tax losses from previous years and may be carried forward for a period of up to five years. Tax losses cannot be carried back. Furthermore, the possibility to utilize a tax loss carried forward from previous tax periods is generally restricted, provided that the company was subject to a change in ownership or participated in a legal transformation and that the scope of business of the company materially changed in comparison with the tax period when the tax loss was incurred. A legally binding ruling could be obtained from the Czech tax authorities on whether the tax loss could be utilized in a particular case.

3.2.11 Capital Gains and Losses

Capital gains from sale of fixed and financial assets are taxable at the general corporate income tax rate of 19% (5% for mutual, investment and pension funds). Capital gains realized by Czech tax non-residents from the sale of shares/ownership interest in a Czech company to a Czech tax resident (or to

a Czech permanent establishment of a Czech tax non-resident) represent Czech sourced income subject to Czech income tax. Nonetheless, this tax on capital is normally eliminated by the applicable double tax treaties (with certain exceptions).

Capital losses from disposal of tangible and intangible assets are generally recognized as tax deductible (with exceptions for loss from sale of land). Losses on securities, shares not valued at market value (shares in subsidiaries), promissory notes and other items (e.g. receivables, ownership interests in limited liability companies), are non-deductible and cannot be carried forward.

3.2.12 Participation Exemption

Based on the new tax legislation effective as of January 1, 2008, dividends and capital gains of parent companies realized on sale of shares and participations in their subsidiaries qualify for corporate income tax exemption if certain conditions are met.

Generally, the conditions can be divided into two sections, i.e. those that are applicable to all subsidiaries and those that deviate depending on the location of the subsidiary. Both categories are briefly summarized below:

Overall conditions for corporate income tax exemption:

- (a) Capital gain is realized by a parent company established or effectively managed in the Czech Republic or a tax resident of another European Union country, Norway or Iceland;
- (b) The parent company has the legal form of a limited liability company, a joint stock company or a co-operation under the Czech commercial law or legal form mentioned in the Annex to the Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States;
- (c) The parent company is the beneficial owner of the capital gain;
- (d) The parent company keeps at least 10% of the registered capital of the subsidiary for a period of at least 12 months;
- (e) The subsidiary is not in the process of liquidation; and
- (f) Shares or participation that are subject to the sale were not acquired within a transfer of business or its part.

Specific conditions for corporate income tax exemption

- (a) A subsidiary – a Czech entity
 - (i) The subsidiary is established or effectively managed in the Czech Republic;
 - (ii) The subsidiary has the legal form of a Czech limited liability company, joint stock company or co-operation under Czech commercial law.
- (b) A subsidiary – a foreign entity located in the European Union, Norway and Iceland
 - (i) The subsidiary is a tax resident of a Member State of the European Union, Norway or Iceland;

- (ii) The subsidiary has the legal form mentioned in the Annex to the Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States;
 - (iii) The subsidiary is subject to tax mentioned in the Annex to the Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States;
 - (iv) The subsidiary is not exempt from corporate income tax and does not have an option for exemption.
- (c) A subsidiary – a foreign entity located outside the European Union, Norway and Iceland
- (i) The subsidiary is a tax resident of a country which concluded a Double Tax Treaty with the Czech Republic;
 - (ii) The subsidiary has the legal form similar to a Czech limited liability company, joint stock company or co-operation;
 - (iii) The subsidiary is subject to tax similar to Czech corporate income tax at least in the tax rate of 12%. This criterion must be met, at the very least, in the taxable period of transfer and in one previous taxable period.

In order to benefit from the corporate income tax exemption all the conditions mentioned above need to be met. If any one or more conditions are not fulfilled, capital gain from the transfer of share is subject to corporate income tax of 19%. The original purchase price and certain other costs related to the transferred share may be used, with some exceptions, as tax deductible items.

Due to the planned reduction of the corporate income tax rate, the tax burden related to even non-exempt capital gains will be decreased in the future as well.

3.2.13 Transfer Pricing

Transfer prices agreed between persons related either by capital or by another manner should be based on an arm's length principle; otherwise, the tax authorities are authorized to adjust the taxpayer's tax base by an ascertained difference.

The tax authorities have been instructed to follow the OECD Transfer Pricing Guidelines when determining the arm's length price between taxpayers when one of them is from a country that concluded a tax treaty with the Czech Republic.

Persons related by capital are generally those whose direct or indirect participation in the capital of, or voting rights in, one company by another company is greater than 25%. Persons related by another manner are those who have relationships between persons directly or indirectly participating in management or control, or have entered into a legal relation for the purpose of decreasing the tax base or increasing the tax loss.

3.2.14 Tax Grouping and Tax Consolidation

Tax grouping has not been introduced; therefore, each taxpayer must file its own tax return and any intra-group transaction cannot be consolidated for Czech income tax purposes. Furthermore, the fiscal unity concept has not been introduced and it is not possible to offset intra-group losses and profits (with certain exceptions for partnerships).

3.2.15 Tax Period

An accounting and tax period is either a calendar year or an economic year. An economic year is the 12 month period beginning in the first of day of a month other than January. Any change of an accounting and tax period from a calendar year to an economic year, and *vice versa*, must be notified to the competent Tax Office at least three months prior to the planned change.

3.2.16 Income Tax Returns and Payments

A tax return must be filed, at the latest, three months following expiry of the annual tax period. By that same time the due tax declared in the tax return must be settled.

The date for submission is extended by another three months if the taxpayer appoints a tax advisor or attorney to submit the tax return under a power of attorney; such extension is automatic for taxpayers who are required by law to have their financial statements audited.

3.2.17 Withholding Taxes

A withholding tax of 15% applies on dividends modified by applicable double tax treaties and, in certain cases, by Czech tax law. The rate of 15% applies on interest paid abroad by a Czech debtor - modified by applicable tax treaties. A rate of 15% also applies on royalties paid abroad by a Czech licensee - modified by an applicable tax treaty.

Where Czech sourced income is paid abroad, but not subject to withholding tax, a Czech payer could be required to withhold tax securing from 1 to 10% (not applicable in certain cases, e.g. when the receiver of income is a tax resident in the European Union or in the other state of the European Economic Area).

3.2.18 EU Parent Subsidiary Directive

This was implemented into Czech tax law for dividend distributions approved after 1 May 2004; distributed dividends are exempt from tax under the following conditions:

- (a) The dividend is received by a parent company established or effectively managed in the Czech Republic or a tax resident of another European Union country, Norway, Iceland or Switzerland;
- (b) The parent company has the legal form of a limited liability company, a joint stock company or a co-operation under Czech commercial law or legal form mentioned in the Annex to Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States;
- (c) The parent company is the beneficial owner of the dividends;
- (d) The parent company keeps at least 10% of the registered capital of the subsidiary for a period of at least 12 months, either prospectively or retrospectively;
- (e) A Czech subsidiary has a legal form of either a limited liability company, a stock exchange company or a co-operative; and
- (f) The Czech subsidiary is not in the process of liquidation.

3.2.19 EU Merger Directive

Mergers (as well as de-mergers, capital contributions and share exchanges) are generally treated as a tax neutral operation with no tax on non-realized incomes arising from the mergers. Tax-effective step-up is not available in the course of a merger.

Tax-effective reserves, provisions and losses (assessed for the tax period started in 2004 at the earliest) of the liquidated company may be utilized by the surviving company under certain conditions; nonetheless, a tax loss cannot be carried forward if the merger is tax driven, i.e. the scope of business of the surviving company must be retained to a certain extent by the surviving company in order to utilize the tax loss.

3.2.20 EU Interest and Royalty Directive

Interest payments from a Czech company to its related company, established in another EU member state, are exempt from Czech withholding tax. The same tax exemption for royalties applies from January 1, 2011. A receiver must obtain a special decision of the Czech tax authorities on application of the tax exemption.

3.2.21 EU Private Savings Directive

Tax exemption for interest on private savings for individuals seated in other EU member states has been implemented. These provisions became effective once the Directive came into force (June 1, 2005).

3.3 Personal Income Tax

3.3.1 Taxable Income and Tax Rates

Individuals with a permanent address in the Czech Republic, or physically present in the Czech Republic for more than 183 days during a particular calendar year, are deemed to be Czech tax residents and are taxed on their worldwide income in the Czech Republic (with possible tax relief under the double tax treaties by tax credit or exemption). The tax status/domicile of an individual may be affected by tie-breaker provisions of an applicable tax treaty.

Other individuals who do not have Czech tax residency are taxable only on their Czech sourced income. This especially includes income from dependent activity performed on the territory of the Czech Republic. Provisions of relevant double tax treaties may provide relief from Czech tax, both for Czech tax residents and non-residents.

The current tax rate for individuals is 15%.

3.3.2 Income from Dependent Activities

This includes salaries, wages, bonuses and other compensations, irrespective of their nature and title, for activities where a person must follow instructions of his/her employer. This income also includes fees paid to directors, members of statutory bodies of companies, and executives and partners of limited liability companies for work performed, even if they are not obligated to follow orders given by another person.

The tax base for calculation of personal income tax from dependent activities includes: (i) gross income of the employee, including mandatory social and health insurance contributions paid by the employee and (ii) mandatory social and health insurance charges paid by the employer.

Tax allowances (e.g., interest on housing saving loans and mortgage loans) may be claimed in the actual amount after the end of the relevant taxable period. Documented tax credits (e.g., annual

personal tax credit, tax credit for a disabled spouse, etc.) can be claimed on a monthly basis, in the amount of 1/12 of the annual relief.

Under provisions dealing with payroll administration from January 1, 2008, employers are obligated to withhold tax advances in the amount of 15% from the monthly tax base adjusted by the tax relief specified above.

Fees paid to non-Czech members of a Czech legal entity's statutory bodies are subject to a 15% final withholding tax at the source.

3.3.3 Income from Business Activities

An individual's tax base from business activities and professional services includes:

- Income from business trades and other independent business activities;
- Income of general partners of general partnerships and limited partnerships; and
- Income from copyrights and industrial property royalties.

The taxpayer may choose the method of tax base calculation. The following method may be used for this purpose:

- Economic result based on accounting;
- Difference between income and expenses based on tax evidence; and
- Difference between income and a lump-sum deduction of 40 to 80% of income.

If economic result is used for tax base calculation, the income may be deducted by tax deductible expenses, which is the same for legal entities.

3.3.4 Capital Income

An individual's income from capital includes, especially:

- Interest income;
- Dividends income;
- Income from silent partnership; and
- Income from bank deposits.

Dividends and interest income from bank private savings are subject to a final withholding tax of 15%. Other income is subject to regular income tax rates representing part of the individual's tax base.

3.3.5 Other Income

This category includes any other income which increases the taxpayer's property and which is not specified in other income categories; for example, income from a sale of certain shares held less than 6 months, income from the sale of participation interests in a limited liability company held less than 5 years and income from the sale of real estate held less than 5 years or used for less than 2 years as the individual's permanent residence.

3.3.6 Tax Allowances

The sum of partial tax bases may be reduced by the following tax allowances:

- Interest on housing saving loans and mortgage loans used for individual's housing needs up to CZK 300,000 annually and on all loans in the same household;
- Life insurance contributions for a qualified life insurance of up to CZK 12,000 per tax period;
- Pension fund contributions exceeding CZK 6,000 of up to CZK 12,000 per tax period;
- Contributions to trade unions up to 1.5% of individual's employment tax base (but not more than CZK 3,000); and
- Charity contribution of up to 10% of the individual's tax base.

3.3.7 Tax Credits

Tax liability may be further reduced by the following tax credits:

- Annual personal tax credit of CZK 24,840 (CZK 23,640 for 2011);
- Annual tax credit per each child of CZK 11,604.

3.3.8 Tax Return

An individual who receives taxable income must file his/her annual tax return, with exception for (i) income from employment subject to Czech payroll tax, (ii) income subject to final withholding tax, and (iii) non-taxable income and tax exempt income. The tax return must be filed by 1 April of the next year; an extension may be granted on an individual basis for another three months. Due tax must be settled in the same tax period.

3.3.9 Mandatory Social and Health Insurance Contributions

Income from dependent activities, as well as from performance of independent business activities, is subject to mandatory social and health insurance contribution, provided that the individual participates (obligatory or voluntarily) in the Czech social system.

Individuals working in the Czech Republic, must generally participate in the Czech social security system (comprising of pension insurance, sickness insurance, unemployment insurance and health insurance) and pay related contributions; it is irrelevant whether the employment contract is governed by Czech or foreign law. Nonetheless, EU social security legislation has been applicable in the Czech Republic since May 1, 2004 and modifies application of the Czech social security system to certain migrating individuals.

The following social security and health insurance rates apply for 2012:

	Employer	Employee	Total
Social Security	25%	6.5%	31.5%
Health Insurance	9%	4.5%	13.5%
Total	34%	11.0%	45.0%

The annual basis for calculation of social and health insurance contributions is capped at the amount of 72 times average monthly salary per employee for health insurance and 48 times average monthly

salary per employee for social insurance. The calculation of average monthly salary is subject to special rules. For the year 2012, the annual cap for health insurance amounts to CZK 1,809,864, for social insurance amounts to CZK 1,206,576.

The employee's contribution must be withheld by the employer from the employee's remuneration and, together with the employer's contribution, must be transferred to the social security and health insurance authorities.

The tax base for calculation of personal income tax from dependent activities includes: (i) gross income of the employee, including mandatory social and health insurance contributions paid by the employee and (ii) mandatory social and health insurance charges paid by the employer.

3.4 Value Added Tax ("VAT")

3.4.1 General

Czech VAT law is harmonized with EU VAT law. Czech VAT is levied upon the following transactions performed within the Czech Republic:

- Supply of goods, including transfer of certain real estate, and provision of services, including transfer of rights;
- Acquisition of goods (intra-community acquisition) from other EU countries and acquisition of services (reverse-charge) from other EU countries and from third countries; and
- Import of goods from third countries.

A distinction must be made between:

- VAT non-taxable supplies, such as, for example, the sale or capital contribution of a business unit/enterprise or assignment of an owned receivable, where no output VAT is payable, but input VAT is deductible;
- VAT taxable supplies, where output VAT is payable, but input VAT may be deducted on received supplies;
- VAT tax-exempt supplies with a right for an input VAT deduction, such as the export of goods to non-EU countries or intra-community supply of goods to VAT payers seated in other EU member states, or international transportation services related to the import/export of goods, where no output VAT is payable, but input VAT is deductible; and
- VAT tax-exempt supplies without a right for an input VAT deduction, such as broadcasting, financial, social and educational services, transfer of ownership in certain buildings or parts of buildings or lease of real estate, where no output VAT is payable, but input VAT is not deductible.

3.4.2 VAT Payers

Persons or entities having a seat, place of business and establishment in the Czech Republic, who carry on economic activities and whose turnover exceeds CZK 1,000,000 for a maximum of the past twelve successive months, are liable to register for VAT purposes. Should a person not achieve the registration threshold, voluntary registration is possible if the person is able to demonstrate that he carries out economic activities. A foreign entity is obligated to register for Czech VAT purposes once it starts to perform taxable supplies in the Czech Republic (if this entity is obliged to assess and pay

VAT) or establishes a VAT permanent establishment; there is no registration threshold stipulated for these entities.

Special VAT registration thresholds apply in certain cases:

- Acquisition of goods from another EU country with worth exceeding CZK 326,000 in the relevant calendar year; and
- Sale of goods by a taxable person from another EU Member State to Czech non-commercial persons through distance selling with a worth exceeding CZK 1,140,000 in the relevant calendar year.

3.4.3 VAT Rates

A standard rate of 20% is levied on most goods and services. A reduced rate of 14% is levied on certain goods such as food or books and certain services such as certain residential construction services, cultural events and social care services (provided that they are not VAT exempt). Beginning January 1, 2008 only residential dwellings classified as social due to their limited flooring are subject to the reduced VAT rate of 14%. The reduced VAT rate valid before 1 January 2012 amounted to 10%.

3.4.4 VAT Period, Returns and Payment

The tax period for submission of VAT returns and payment is dependent upon turnover (for non-Czech taxpayers only a quarter tax period applies):

Turnover for Previous Calendar Year	VAT Period
>= CZK 10,000,000	Calendar month
< CZK 10,000,000	Calendar quarter (optional monthly for turnover above CZK 2,000,000)

VAT returns must be submitted within 25 days following the end of the applicable VAT period. Payment of VAT is due at the same time that the VAT return is due.

3.4.5 Input VAT Deduction

The VAT payer is entitled to exercise, through his VAT return, the right to deduct input VAT with respect to taxable supplies received (including imported goods) and used for his own economic activities, if he has a valid VAT invoice.

If the amount of input VAT recoverable in the relevant VAT period exceeds output VAT payable in that period, VAT in excess is refundable to the VAT payer within 30 days following the deadline for submission of a VAT return for the relevant VAT period.

Input VAT is not recoverable for supplies received regarding provision of VAT exempt supplies without the right for an input VAT deduction. If a VAT payer performs taxable and exempt supplies, it is entitled to claim partial recovery of the input VAT related to the inputs used for both types of supplies. This is calculated by multiplying the aggregate input VAT for the relevant tax period with the pro rata coefficient. The following taxable supplies are VAT exempt without a right for input VAT deduction:

- Postal services;
- Sound and TV broadcasting;

- Financial services;
- Insurance services;
- Transfer and lease of certain land, certain buildings, apartments and non-residential premises;
- Education and training services;
- Medical services and goods;
- Social services;
- Lotteries and similar games and their operations; and
- Supply of goods used for VAT exempt supplies where input VAT was not deductible upon their acquisition.

3.4.6 Input VAT Refunding

Non-Czech business entities may require refunding of input VAT paid as part of the purchase price for supplies subject to Czech VAT and used for their taxable activities. Rules for VAT refund are, in principle, based on the EU refund directives.

Refunds are made upon request of the foreign entity. In case of EU entities, the request is filed with the relevant authority in a Member State of its establishment. Non-EU entities file the refund applications on a prescribed form with the Financial Office for Prague 1.

3.4.7 INTRASTAT Reporting

The INTRASTAT reporting system has applied in the Czech Republic since 1 May 2004. Under this system, a Czech VAT payer performing intra-community transactions regarding supply/acquisition of goods must report these transactions to Czech customs authorities using special forms.

Data required should be reported, in writing or electronically, for the period of a calendar month. Entities with minimum intra-community transactions are exempt from the INTRASTAT reporting duty.

3.5 Other Taxes

3.5.1 Real Estate Transfer Tax

Any transfer of real estate for a consideration is subject to a 3% real estate transfer tax, payable by the transferor. The transferee is a guarantor for the unpaid tax. The tax base is either the agreed transfer price or the value of the transferred asset under the statutory valuator's report, whichever is higher. Special real estate transfer tax exemptions apply for an in-kind contribution of real estate into registered capital and for the transfer of real estate during the course of mergers and acquisitions.

3.5.2 Real Estate Tax

Real estate tax is imposed on buildings and plots of land registered in the Real Estate Cadastre, depending on their size and location. Real estate tax is generally paid by the owner; the tax period is a calendar year and tax is assessed based on the situation as of 1 January; any transfer of real estate is irrelevant. The tax return must be filed by 31 January of the actual tax period. The due date for settlement of the tax depends on the amount of tax assessed and the type of real estate.

3.5.3 Gift Tax

Gift tax is payable for transfer of property without any monetary or in-kind consideration. The tax rate varies from 1 to 40%, depending on the gift's market value and status of the recipient of the gift. Tax is normally payable by the receiver of the gift (with certain exceptions for donations abroad).

3.5.4 Road Tax

Road tax is payable for all vehicles registered in the Czech Republic and used for business purposes, regardless of whether the vehicles are owned by business entities; employees' cars used for employers' business trips are also subject to road tax. The tax period is a calendar year. The tax return must be filed by 31 January of the following year. The tax base calculation is specific for each kind of vehicle.

3.5.5 Customs Duties

As a member of the EU, the Czech Republic follows EU Customs' legislation, including unified EU Customs Nomenclature and Tariff. Goods imported into the Czech Republic from third countries outside of the EU are subject to import customs duties and import VAT (unless those goods are specifically exempted from customs duty and import VAT). Customs duty may also be fully or partially reduced based on either a bilateral (based upon agreements on customs preferences concluded by the EU) or unilateral basis (based on the EU customs preferences addressed to developing countries).

Imported and exported goods can also be subject to other non-tariff measurements restricting import/export, such as import/export licenses and quotas and veterinary inspections.

3.6 Accounting, Auditing and Publication Requirements

3.6.1 Accounting Standards

All Czech business entities, as well as any Czech branches of foreign entities, individuals registered in the Commercial Register and individuals with an annual turnover exceeding CZK 25 million, are required to keep accounting records in accordance with Czech accounting statutory provisions. Furthermore, when an individual enters into an association with an individual or a legal entity which keeps accounting, then such new associated person(s) must also keep accounting records.

Special accounting regulations apply for banks, insurance companies and other financial institutions as well as for municipalities and other non-entrepreneurs. Small entrepreneurs/individuals are required to keep only records for tax purposes.

Accounts, as well as financial statements, must be principally kept in Czech local currency and in Czech language. Assets and liabilities denominated in foreign currencies must also be recorded in those foreign currencies.

Czech companies issuing securities admitted for trading on regulated market in the EU are also required to keep their books according to International Financial Reporting Standards (IFRS). Czech accounting standards currently differ from the IFRS in a number of aspects, including:

- Spare parts are treated as stock; they are not depreciated and the reduction in value is reflected in provisions on reduced value;
- Capitalization of interest relating to investments in assets is not obligatory (interest incurred until the asset is put into use may be treated as an operation expense);

- All leases are treated as operating leases and are recognized on the balance sheet; and
- Effect of change in accounting policy must be reflected in the accounting period when the change occurred and not as a prior year adjustment.

3.6.2 Financial Statements, Annual Report and Report of Control

Czech financial statements comprise the balance sheet, profit and loss account, explanatory notes, cash-flow statement and statement on changes in equity. Explanatory notes must include the following information, relevant for the particular accounting period:

- Information regarding assets, liabilities, financial position and economic results;
- Accounting policies, valuation methods and depreciation rates; and
- Explanation of changes in accounting policies and estimation methods, reasons for changes and effect of the financial position.

Individuals and legal entities subject to a statutory audit of financial statements also need to prepare their annual report. The annual report must include the following:

- Financial statements;
- Consolidated financial statements (if applicable);
- Auditor's report; and
- Commentary on the post balance sheet date events, on the projected future performance, on research and development activities, on employment and environmental matters and on foreign branches.

If a control agreement is not concluded between controlling and controlled entities, the controlled company must prepare a report on relationships between the controlling and controlled entities and on relationships between the controlled entity and other entities controlled by the same controlling entity. This report must be attached to the company's annual report.

3.6.3 Consolidated Accounts

Consolidated financial statements must be prepared by the controlling company or a company exercising substantial influence on the control or operation of another controlled company. Consolidated companies must adopt uniform and consistent accounting policies for the purpose of consolidation.

Consolidated financial statements must be prepared under IFRS, if the controlling company issued securities admitted for trading on a regulated market in the European Union. Other entities may opt to use IFRS as a basis for preparation of the consolidated financial statements.

Since the consolidated tax base has not been introduced, consolidated financial statements are used only for accounting purposes and not for tax purposes or for calculation of distributable profit.

3.6.4 Publication and Archiving of Records

An annual report must be published through a submission to the Collection of Records within 30 days of its authentication by the auditor and approval by the statutory body, but no later than the end of the

following accounting period; if the annual report has not been audited by the end of the following accounting period, it must be noted in the filed annual report.

Certain other company documents must be filed with the Collection of Records, including:

- Company’s Deed of Associations, Articles of Association and Statutes, including all changes and amendments;
- Valuator’s reports on in-kind capital contributions;
- Resolutions concerning changes to the company’s statutory bodies;
- Documents concerning merger, acquisitions, winding up, division, transfer, change of legal form or transfer of property of shareholders;
- Agreements on the transfer of pledge of ownership interest/share in the company, agreements on the transfer or lease of whole or part of the enterprise, control agreement and agreements on the transfer of profit; and
- Decisions of the company’s general meeting or any resolution of a sole shareholder in the capacity of the general meeting.

Accounting documents must be archived for the following minimum periods:

Type of Record	Period
Payroll Data for Pensions and Sick Payments	30 years
Financial Statements and Annual Reports	10 years
Payroll Registers	10 years
Tax documents for VAT purposes	10 years
Other	5 years

Nonetheless, since accounting documents are also normally relevant for tax purposes, the period for which documents are retained must also reflect whether a tax audit could be performed.

3.6.5 Audit Requirements

A statutory audit of financial statements and annual report is required for companies and individuals keeping accounting where at least two of the following conditions are met for both the current and previous accounting period (for joint stock companies one of the following conditions must be met):

- Turnover exceeding CZK 80 million;
- Total gross value of assets exceeding CZK 40 million; and
- Average number of employees exceeding 50 persons.



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4. Labor/Employment Issues

In particular, the following considerations should be kept in mind when employing personnel in the Czech Republic:

4.1 Legal Framework

The Czech Labor Code, Act No. 262/2006 Coll. (“Code”) effective as of 1 January 2007, is the principal legislative act governing employment relations in the Czech Republic. The Code has been adopted after extensive preparation and discussion between experts and parties involved in employment-related matters in the Czech Republic and reflects the achieved level of social and economic relationships in the Czech Republic and corresponds to international trends of employment law developments, including various concepts existing under EU labor law related Directives. Other relevant legislative acts include, in particular, the Act on Employment (Act No. 435/2004 Coll. as amended), Act on Collective Bargaining (Act No. 2/1991 Coll. as amended) and a number of Decrees relating to the Code.

Most of the provisions in the labor legislation are of a mandatory nature and safeguard the observance by employers of the most important principles, such as, *inter alia*, the principle of equal treatment and prohibition of discrimination. On the other hand, the Code respects the principle of contractual freedom of the parties and thus employment relations may be varied by the provisions of the relevant employment agreement, provided that the above principles, as well as basic rights and working conditions of the employees set forth in the Code, must be observed. For example, termination provisions which differ from those as specified in the Code and which are less favorable to the employee would generally not be enforceable.

4.2 Basic Relationships

The Code defines the subject of labor relationships as “fulfillment of dependent (subordinated) work,” provided that the Code safeguards protection of rights and observance of principles mentioned above only to employees fulfilling their work in such subordinated relationship. Under the Code, such employment relationships generally arise between employees and employers in the private sector on the basis of:

- employment agreements (in Czech “pracovní smlouva”); or
- labor relationships outside employment based on (i) agreements for performance of a specific work assignment (in Czech “dohoda o provedení práce”) or (ii) agreements on work activity (in Czech “dohoda o pracovní činnosti”).

A labor relationship may only be created with the consent of an individual and an employer.

4.3 Key Employment Conditions in Employment Relationship

Written form - An employment agreement must be in writing.

Probationary period - The employment agreement may include a probationary period of up to three consecutive months following the date of commencement of the employment relationship or, in case of managing employees, up to six consecutive months following the date of commencement of the employment relationship. The probationary period may not be more than one half of the length of the employment relationship, if agreed for a definite period of time.

Working hours - The length of normal weekly working hours may not exceed 40 hours per week. However, the length of normal weekly working hours of:

- (a) Employees who work underground on extraction of coal, ores or non-metallic raw materials, or on construction of mine-works or who are engaged in geological prospecting on mining sites, may not exceed 37.5 hours per week;
- (b) Employees, who are on a three-shift or continuous work schedule, may not exceed 37.5 hours per week;
- (c) Employees, who are on a two-shift work schedule, may not exceed 38.75 hours per week;
- (d) Employees, who are under the age of 18 years, may not exceed 8 hours per shift and in total from all employment relationships 40 hours per week.

Vacation - The basic vacation period is at least 4 (four) weeks per calendar year. During the vacation period, the employee is entitled to receive compensation in the amount of his/her average earnings.

4.4 Employment of Czech Nationals

Czech law and, in particular, the Code, shall apply to employment relationships between Czech legal entities and their employees in the Czech Republic. An employment relationship between a Czech branch office of a foreign legal entity and its Czech employees in the Czech Republic may be governed by other than Czech law, if so agreed between the employer and the employee. There are, however, some provisions of labor as well as public laws that are always applied by Czech courts or other authorities, regardless of the choice of law clause, to protect public order and good morale, e.g. prohibition of discrimination, safety and protection of health at work, safety regulations, etc. Provisions of the Code are generally less flexible and more protective of the employee than is commonly the case outside EU countries (e.g. the United States).

For example, under the Code an employer is very limited as to its ability to terminate employment relationships of its employees without cause. An employment relationship of an employee may be terminated for cause with immediate effect, if the employee intentionally commits a certain crime or materially breaches his obligations related to his/her employment relationship (e.g. intoxicated on the job, stealing company property, etc.). An employment relationship of an employee may be terminated for cause with a two-month notice period, for example if:

- the employee, after an official written warning, fails within a certain period of time to satisfactorily carry out his/her work obligations or assignments, or fulfill other employment obligations; or
- the employee loses qualifications which are necessary for carrying out his/her work;
- the employee's health condition does not permit him/her to carry out his/her work; or
- the employee breaches regime of sick employee.

Employment relationship may also be terminated by the employer:

- for redundancy reasons,
- due to relocation or cancellation of the employer or its part, or
- during probationary period without stating a reason.

The employee's trade union or works council, if any has been established, would have to be consulted about the termination of an employee by termination notice or immediate cancellation of employment (not in case of agreement, with some exceptions) or requested for approval of the termination by notice or immediate cancellation of employment, depending on the specific case and termination reason.

Severance payment is applicable in case of terminating the employment relationship due to redundancy, relocation or cancellation of the employer or its part equal to at least:

- 1 multiple of employee's average monthly earnings, if the employment relationship with the employer lasted less than 1 year;
- 2 multiples of employee's average monthly earnings, if the employment relationship with the employer lasted at least 1 year, but less than 2 years;
- 3 multiples of employee's average monthly earnings, if the employment relationship with the employer lasted 2 or more years,

unless a higher severance payment has been agreed upon in the collective agreement, or if so stipulated in the internal regulations of the employer, or otherwise agreed between the parties.

Substantially higher severance payment is applicable in case of terminating the employment relationship due to work related injury or sickness or threat of work related sickness equal to at least 12 multiples of employee's average monthly earnings.

4.4.1 Employee Representatives

Employees have the right to information and consultation. The employer is required to discuss with an employee (or the employee representatives if established) certain specified topics and to provide the employee with certain types of information. Special consultation and information duties are stipulated by the Code.

There are three types of employee representatives:

- (a) Trade unions,
- (b) Work council, and
- (c) Representative of employees for safety and protection of health at work.

4.4.2 Collective Agreements

The process of collective bargaining is governed by the Act on Collective Bargaining. Collective agreements regulate the relationship between the employer and trade unions and rights of employees; in particular, wages and other labor entitlements. Rights which individual employees acquire through collective agreements are treated the same as other employee rights arising out of the employee's employment relationship. The trade union shall also conclude a collective agreement on behalf of employees who are not trade union members.

There are four types of collective agreements and all must be entered into in writing to be enforceable but are not mandatory:

- agreements between a trade union or trade unions and the employer;

- agreements of a higher degree concluded for a larger number of employers between a relevant higher trade union body or trade union bodies and organization/organizations of employers (field unionization);
- agreements of a higher degree concluded between a relevant higher trade union and an employer – state; and
- agreements of a higher degree concluded for employers who are bound by specific laws (public functions, government employees, etc.).

A collective agreement cannot provide less to employees than a collective agreement of a higher degree.

4.5 Expatriate Personnel Working in the Czech Republic

4.5.1 Work Permits and Residence Visas

(a) Foreign Employee - a Citizen of any EU Member State

A work permit is not required; however, a notification duty applies for the employer or the recipient person. Any employer, who employs a foreign employee (a citizen of any EU member state) within the territory of the Czech Republic, or any person (recipient) who accepts assignment of a foreign employee (a citizen of any EU member state) within the territory of the Czech Republic, is obligated to notify the respective regional branch of Labor Authority in writing on:

- employment/assignment of the foreign employee – the notification duty must be fulfilled on the day of commencement of work by the foreign employee, at the latest; and
- termination of the employment/assignment of the foreign employee – the notification duty is fulfilled within 10 days from termination of the employment/assignment, at the latest.

Such foreigners have to also register their stay with the Police (with some exceptions). A visa is not required for the purpose of performing employment activities within the territory of the Czech Republic. A foreign employee may obtain a permanent or temporary “Residence Permit Certificate for a citizen of an EU member state” in advance (however, this is not an obligation).

(b) Foreign Employee - a Citizen of other than any EU Member State

Both the Czech work permit and visa (issued for the purpose of employment) are required before the employee commences employment work within the territory of the Czech Republic (certain exemptions are available, e.g. in case of relatives of citizens of EU member countries or experts).

A work permit is not required if the employee is not to be performing work within the territory of the Czech Republic for more than any 7 (seven) consecutive calendar days or in total 30 (thirty) days in a calendar year, provided that the employee is at the same time a:

- performer (performing artist), pedagogical worker, academic worker of a University;
- scientific, research or development worker, who is a participant of a scientific meeting;
- pupil or student up to 26 years of age;
- sportsman; or

- person providing goods delivery or services within the territory of the Czech Republic or delivering such goods or providing installation, guarantee or repair services under a business agreement.

In addition, certain exceptions or special treatment may apply based on international treaties concluded between the Czech Republic and a respective country.

Such foreigners also have to obtain visa (with few exceptions) and register their stay with the Police (with some exceptions). It is necessary to point out that the procedure to obtain a work permit and visa is very administratively demanding and time consuming (and may take up to 6 months).

There are certain other immigration alternatives, for example for experts or applicants for asylum.



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5. Real Estate

5.1 Definition of Property under Czech Law

Czech law recognizes two types of real property: (i) plots of land, and (ii) constructions connected to the ground with fixed foundations. All other assets, such as constructions without fixed foundations, are not considered real property under Czech law.

Under Czech law, the principle of “*superficies solo cedit*”, which treats each plot of land and anything built upon it as a single object of real estate, does not apply. Generally, according to Act No. 40/1964 Coll., Civil Code, as amended (“Civil Code”), a building (structure) does not form part of a plot of land. Therefore, it is possible that an owner of a plot of land is not the same legal or physical person as the owner of a construction built on that same plot of land. If a construction is built on a plot of land owned by another legal or physical person, it is necessary to establish rights to use that land either in the form of a lease or an easement.

5.2 Cadastral Register

All plots of land and, with certain exceptions set forth in the law, all construction thereon in the Czech Republic (including residential apartments and non-residential premises that have been categorized as separate assets/units) are registered in the Cadastral Register.

The Cadastral Register is a record of rights to real property including, in particular: ownership rights, mortgages, easements and pre-emption rights (where the latter takes effect as a right *in rem*). Leases and option agreements encumbering an ownership right are not recorded in the Cadastral Register. Neither takes effect as a right *in rem*. The Cadastral Register also contains a Collection of Documents, which includes decisions of public authorities, agreements and other deeds based on which the record in the Cadastral Register was made. The Cadastral Register is publicly accessible; anyone is entitled to access it in order to make extracts, copies and notes. Limited fees are payable. Reliance on Cadastral Register entries made after 1993 constitute a “good faith” acquisition.

5.3 Owners of Real Estate

Under Czech law, every individual and legal entity enjoys the same right of ownership of real property. The same applies to foreign citizens and foreign legal entities in the Czech Republic.

Acquisition of real property by foreign nationals, i.e., persons who are not citizens of the Czech Republic and legal entities having seat outside the Czech Republic, has been restricted by the Czech Foreign Exchange (Act No. 219/1995 Coll, as amended). Some of the restrictions remained imposed on non-Czech nationals after Czech Republic’s joining the EU in 2004. These restrictions were enabled during transition periods commencing on 1 May 2004 in which exceptions from Article 56 of The Treaty Establishing the European Community were allowed. Article 56 of the Treaty bans all restrictions on the free movement of capital and payments, both between Member States and with third countries outside the European Union, including investments in real property. A five year transition period expired on 1 May 2009 that was agreed in relation to acquisition of real property other than agricultural land or forests. Before 1 May 2009, the only way to acquire real property, except for agricultural land or forests, was set forth in Section 17 (2) of the Foreign Exchange Act.

All the restrictions on acquisition of real property other than agricultural land or forests completely disappeared on 1 May 2009, when the transition period expired. Therefore, from 1 May 2009, foreigners, both from within the European Union and outside the European Union, may acquire real property other than agricultural land or forests in the Czech Republic without any limitation.

From 19 July 2011 all restrictions on acquisition of real property also formally disappeared from the Foreign Exchange Act and obstacles remain for acquiring of real property by foreigners.

5.4 Transfers of Real Estate

In order to transfer ownership title to real property, the following formal requirements and procedures must be met and followed:

- An agreement on the transfer of real property must be made in writing. Signatures of the transferor and the transferee must be affixed in the same document and must be officially verified.
- The transfer agreement must contain a description of the real property to be transferred. For real property that is subject to registration, this will be the information recorded at the Cadastral Registry. For other real property not subject to registration, as detailed a description as possible is required.
- The transfer of real property that is subject to registration becomes effective on the date of registration of the new owner in the Cadastral Register. However, the transfer is also effective retroactively as of the date of filing of the application for registration with the respective Cadastral Office. A transfer of real estate that is not subject to registration becomes effective on the effective date of the relevant transfer agreement. Since 1 January 2012 a new formal procedure applies with respect to applications for registration with the Cadastral Register and standardized forms will be used.

5.5 Rights to Real Property Owned by a Third Party (*iura in re aliena*)

Czech law recognizes the following third party real property rights:

- Easements;
- Mortgages; and
- Pre-emptive rights.

Easements impose restrictions on owners of real property in favor of another person. The beneficiary of an easement is either an owner of another real property asset (an easement *in rem*), or a specific individual/legal entity (an easement *in personam*). Obligations arising under an easement pass to the new owners of an encumbered real property asset.

Czech law recognizes several ways to establish an easement, including by written agreement of the parties. An easement right encumbering registered real property comes into existence, however, only through its registration in the Cadastral Register.

Easements may be terminated in the following ways:

- By agreement of the parties.
The Parties may agree on the termination of an easement. A record in the Cadastral Register is required;
- By operation of law.

An easement is terminated by operation of law if the burdened real property can no longer serve the beneficiary or the real property of the beneficiary;

- By a decision of a court or other administrative body.

A court may terminate (or limit) an easement if, due to a change in circumstances, there is a material discrepancy between the restrictions imposed on the owner of the burdened real property and the benefit afforded to the benefiting real property or individual beneficiary; and

- By death or dissolution of the beneficiary.

If the beneficiary is defined as a specific individual or entity (easement *in personam*), the easement is terminated upon the individual's death or the entity's dissolution. These easements generally do not pass to legal successors of the beneficiary.

Apart from easements, as such, the law contains a large number of restrictions imposed on an owner of land. These restrictions include, by way of example, an owner's duty to allow the owner of neighboring land and buildings to enter its property in order to carry out maintenance and repairs. Similar duties to allow entry are set forth, for instance, in mining regulations, laws for protection of the landscape and the environment, and telecommunications and energy regulations. Save for rare exceptions, such restrictions are not, however, subject to registration in the Cadastral Register.

As to mortgages, under Czech law a mortgage is used to secure a debt obligation. If a debtor fails to perform such obligation, the secured creditor is entitled to satisfy his claim by foreclosing on the mortgaged asset.

Both monetary and non-monetary claims may be secured by a mortgage. The mortgage encompasses the asset and any appurtenances thereto. A mortgage may, *inter alia*, be created for a specific period, to secure a claim up to a particular amount and for a particular type of claim which will arise in the specified future. A mortgage may further secure future or conditional claims.

Mortgages may be created by a written mortgage agreement, by a court or administrative order, or by operation of law. Mortgages established on the basis of an agreement are affected by registration in the Cadastral Register (provided that the real estate is subject to registration).

In order to create a mortgage by agreement, the creditor and mortgagor must enter into a written agreement. The object of the mortgage agreement and the claim being secured must be sufficiently identified, including the identity of the debtor, if it is a different entity from the mortgagor.

The Civil Code does not specify any other information which must be included in the mortgage agreement with respect to the identity and nature of a claim. However, the claim must be identified clearly and sufficiently. Therefore, a fixed amount and a fixed period (although clearly helpful and desirable) are not necessary if there is another method which can sufficiently identify a particular claim (e.g. by reference to a contract).

If a single asset is subject to several mortgages, the mortgage that was first made must, on foreclosure, be first satisfied, unless the law specifies otherwise. The time that a mortgage was created is decisive for determining priority, even if the mortgage was created to secure a future or conditional debt.

A mortgagee may make use of mortgaged real property only with the express consent of the mortgagor. A mortgagee who has an encumbered real property asset in his custody must take due care to protect the asset from damage, loss or destruction. The mortgagee may not take any action

which would impair the value of the encumbered asset to the detriment of the mortgagor. In the event of damage, loss or destruction, the mortgagee is liable for damages to the mortgagor. If the mortgagee incurs expenses as a consequence of complying with its duty to protect an encumbered asset, the mortgagee is entitled to compensation from the mortgagor for such expenses.

If the market value of the encumbered asset decreases to such an extent that security for the debt becomes insufficient, the mortgagee may require the debtor promptly to provide additional adequate collateral. If the mortgagor fails to deliver such additional security, that portion of the debt which is not secured immediately matures.

If a secured claim is not duly and timely satisfied, the mortgagee may foreclose against the encumbered real property asset. If several different assets are encumbered to secure one claim, the mortgagee is entitled to seek satisfaction of its claim, or a part of it, by foreclosure against any of the encumbered real property assets.

Two methods of foreclosure against a mortgaged real property asset exist: (i) by means of a public auction, or (ii) by a court-organized sale.

5.6 Zoning Plan and Planning, Building and Use Permits

Czech law generally requires planning and building permits for any property development. Any use of the development, when completed, must then be additionally approved by a building-use permit. A building-use permit must then additionally approve any use of the development, when completed.

Planning permission, as a first stage permit, may be obtained only if the application for planning permission (i.e. the development project) complies with an approved urban study or zoning plan. If an urban study/zoning plan is not consistent with the intended development project, a change to the urban study/zoning plan is possible. This procedure would likely, however, be rather time-consuming.

The approval process for planning permission can be extremely complex and protracted, since a number of public authorities would be involved; these include the Fire Department, Department of Hygiene, Heritage Protection Office, Chief Architect's Office, Transport Department, Environmental Office and others. Permission itself, when issued, comes from the relevant Building Office.

For construction works, a building permit must be obtained from the Building Office. A building permit is required not only for new construction, but also for major reconstruction and renovations or alterations. Application for a building permit must be in compliance with prior planning permissions.



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6. Environmental Protection

Czech regulations governing the protection of environment are analogous to those prevailing in EU countries. As a result, any person exploiting natural resources, developing projects, building or removing structures, including residential projects, logistic centers, office and retail parks, or introducing production and manufacturing processes, products or materials into the Czech Republic, is required to carry out such activities in compliance with applicable environmental protection legislation. This means, in the first instance, obtaining respective permits related, for example, to establishing and operating air pollution sources, water treatment facilities, waste and chemical substances treatment, as well as complying with the conditions set out in the permits.

Czech legislation also requires that projects of a certain type and size, or projects that may have significant impact on the environment, may be carried out only after an environmental impact study is completed and the requisite licenses under the Integrated Pollution Prevention and Control rules have been obtained.

The treatment, transport and disposal of waste are primarily regulated in Act No. 185/2001 Coll., on Waste, including the treatment of dangerous waste, oils, accumulators, PCB, asbestos, etc. The Czech Waste Act also transposes into Czech law EU Directive No. 2002/96/EC, on Waste Electrical and Electronic Equipment (WEEE) and EU Directive No. 2002/95/EC, on the Restriction of the Use of Certain Hazardous Substances in Electrical and Electronic Equipment (RoHS). The WEEE rules relating to the obligations of manufacturers and importers with respect to labeling, collection and recycling of electric and electronic waste, including providing for financial guarantee and registration with the Ministry of Environment, came into effect in the Czech Republic on 13 August 2005.

In relation to pollution control, subject to certain special conditions regulated in applicable laws, the principle of “the polluter pays” is generally applied to cases of water, groundwater and soil contamination, as well as to other impairment of different elements of the environment (air, forests, fauna and flora). The foregoing reflects the fact that, under Czech law, environmental liability has the same features and is based on the same principles as liability for damages regulated in the Civil Code. Given the foregoing, implementation of EU Environmental Liability Directive 2004/35/CE, which was implemented into Czech legislation by Act No. 167/2008 Coll., Act on the prevention and remedying of environmental damage, did not bring major changes to the regulation of environmental liability in the Czech Republic. In fact, the Directive is based on the same “polluter pays” principle, which has been further enhanced after implementation into Czech legislation. Nowadays, certain industrial operators are imposed strict liability for environmental damage caused by their operations and have to provide financial guarantee for costs that may be incurred in case of environmental damage of a worst case scenario.

A special category of environmental harm is also recognized under Czech law in relation to privatization projects and acquisition of state property by private investors, according to Act No. 92/1991 Coll., Privatization Act. In some privatization projects, the Government may decide that an Indemnity Agreement must be concluded by the Ministry of Finance (before 1 January 2006, known as the National Property Fund) with the private acquirer of privatized assets. As a result, the acquirer is indemnified by the Ministry of Finance for costs sensibly expended in connection with the settlement of environmental liabilities occurring prior to privatization. The scope of remediation works is stipulated by the Czech Environmental Inspection on the basis of a special audit.

Furthermore, approximately 400 Czech facilities have been listed in the National Allocation Plan and are imposed the duties under Act No. 695/2004 Coll., on GHG Emissions Allowances Trading, including, in particular, obtaining a permit to release GHG emissions, as well as monitoring, verification and reporting of emissions and returning an annually adequate amount of allowances to the system.

During 2011 the Czech Government initiative regarding adoption of legislation regulating Carbon Capture and Storage (CCS) continued. The draft Act on CCS was submitted within the early stages of the legislation process with Czech Parliament and is expected to be adopted in 2012.

Lastly, the European REACH regulation applies directly in the Czech Republic, affecting around 1,000 chemical substances, and requiring their registration, evaluation and authorization with the European Chemical Agency.



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7. Competition Rules

The purpose of Czech competition legislation is to protect economic competition against elimination, restriction and other distortion, including the threat of competition. Competition laws apply to any activity or conduct which has, or may have, an effect on the Czech market, including transactions that take place outside of the Czech Republic, if such activity materially affects the domestic Czech market.

The Act on the Protection of Economic Competition (“Competition Act”) further applies to rulings of the Czech authorities according to Article 81 and 82 of the EC Treaty, and to some aspects of coordination, with the European Commission and other EU authorities. Competition laws apply both to individuals and legal entities (or associations thereof) provided that they, whether or not entrepreneurs and even entities that do not have the status of a legal entity, take part in competition or may influence competition by their activities.

In general, anti-monopoly legislation prohibits each of the following activities.

- (a) Agreements that interfere with economic competition. Such agreements typically include: agreements on price fixing, cartel agreements, production limitation agreements, agreements to restrict the market access of other competitors, divisions of the market and boycotts. Agreements that result or may result in the distortion of competition are prohibited unless exempted by the Competition Act (such as (i) agreements where the combined share on the relevant market does not exceed 10% for horizontal and 15% for vertical agreements or (ii) agreements falling within the scope of European Community block exemption regulations, such as vertical agreements, research and development agreements, agreements on transfer of technologies, insurance contracts, consultation of passenger tariffs and slot allocation at airports, contracts on the distribution and service of motor vehicles, and contracts in the field of transportation by railway, road and inland water transport and, finally (iii) agreements fulfilling conditions of an individual exemption where pro-competitive effect outweigh negative effects on competition).
- (b) Abuse of dominant position. Common examples of abuse of dominant market position include: enforcement of unfair conditions, conditioning the conclusion of contracts on acceptance of supplementary performance, dissimilar conditions to equivalent transactions, limitation of production to the prejudice of consumers, offer and sale of goods for unfairly low prices and refusal to grant access to distribution networks or other infrastructures where competitors are unable to compete without such access. In this regard, a competitor whose market share of any given product or services exceeds 40% is generally deemed to have a dominant position in that product or services market. A competitor is considered to have a dominant position on a relevant market if its market power enables it to behave, to a significant extent, independently of other undertakings or consumers. If the OEC discovers that an abuse of dominant position has occurred, it shall declare such fact by a decision and shall simultaneously prohibit such action in the future (and typically fines the dominant competitor).
- (c) Concentration of competitors not approved by the OEC. Approval of the OEC is required for any merger, consolidation or acquisition where: (i) aggregate world-wide turnover in the last accounting period of the concerned undertaking in the Czech Republic exceeds CZK 1.5 billion and at least two of the concerned undertakings reached a net turnover in the Czech Republic exceeding CZK 250 million, or (ii) net turnover reached by 1) at least one of the merged undertakings, or 2) the acquired undertaking or its part, or 3) the competitor whose business is under control, or 4) at least one entity forming the joint venture in the last accounting period in Czech Republic, exceeds CZK 1.5 billion and the worldwide net

turnover reached by another merging undertaking exceeds CZK 1.5 billion. In this regard, the OEC has the authority to approve a concentration if the applicants are able to prove that harm to competition (which may arise from the transaction) is outweighed by the advantages. Registration of such transaction in the Companies Register is possible only after approval of the OEC. Without such approval, the transaction will be deemed ineffective. In share acquisition transactions, for example, unless specifically approved by the OEC, the acquirer may not exercise control over the acquired entity until such approval has been obtained.

7.1 Sanctions

The OEC may impose fines on competitors of up to CZK 10,000,000 (or up to 10% of the worldwide net turnover in the preceding calendar year) where the Competition Act has been breached, either intentionally or negligently. If no mandatory notification was made, the OEC may also cancel the relevant underlying agreement or impose that the acquirer re-transfer the acquired shares or business to the original owner.



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8. Product Safety & Consumer Protection

8.1 General Regulations

General product safety rules are regulated in the Czech Republic by Act No. 102/2001, on General Product Safety (“GPS Act”), which came into effect on 1 July 2001. The GPS Act effectively incorporated into Czech legislation the substance of regulations contained in the EU General Product Safety Directive 2001/95/EC (“GPSD”).

The GPS Act applies to all products intended for consumer use if it is reasonably foreseeable that those products will be used by consumers. The GPS Act imposes a general duty upon producers to only market safe products. A product is considered ‘safe’ under the GPS Act if its qualities meet the requirements as set forth in applicable EU or national technical norms. In addition to the manufacturer’s obligations, the GPS Act stipulates that distributors may not market a product if they are aware, or may expect on the basis of their information and professional knowledge, that a particular product does not meet the relevant product safety requirements.

8.2 Special Categories of Products

In addition to the general regulations in the GPS Act, which transpose the provisions of the GPSD, there are a number of special product safety regulations in force in the Czech Republic relating to specific types of products (examples of such specific regulations are provided in the form of a list in the GPS Act) including, inter alia, the following:

Category of Products	Relevant Law	Supervising Authority
Products which are likely to pose a danger to public health and/or safety, property or the environment	Act No. 22/1997 Coll.	Czech Trade Inspection or other authority as stipulated in a special law
Pharmaceuticals	Act No. 378/2007 Coll.	State Institute for Drug Control, Institute for State Control of Veterinary Biopreparation and Pharmaceuticals
Medical Devices	Act No. 123/2000 Coll.	State Institute for Drug Control
Food and Tobacco Products	Act No. 110/1997 Coll.	Czech Agriculture and Food Inspection Authority
Fodders	Act No. 91/1996 Coll.	Central Institute for Supervising and Testing in Agriculture
Fertilizers	Act No. 156/1998 Coll.	Central Institute for Supervising and Testing in Agriculture
Chemicals	Act No. 356/2003 Coll.	Czech Environmental Inspection
Firearms and Ammunition	Act No. 119/2002 Coll.	Czech Proof House for Firearms and Ammunition
Cosmetics	Act No. 258/2000 Coll.	Regional Hygienic Stations, Ministry of Health
Toys	Act No. 258/2000 Coll. and Regulation No. 86/2011 Coll.	Regional Hygienic Stations, Ministry of Health

However, the general product safety regulations in the GPS Act will still apply to special categories of products to the extent that the abovementioned laws do not provide special regulation.

8.3 Consumer Protection

The general obligations of importers, manufacturers and merchandisers regarding the provision of information on products sold to consumers in the Czech Republic are regulated in Act No. 634/1992 Coll., on Consumer Protection (“Consumer’s Act”). The mandatory information specified in the Consumer’s Act, when provided to the consumer in writing, must be in Czech language.

According to Czech law, products must be marked with identification of their manufacturer or importer; however, it is not required to reflect the country in which the product was manufactured on the packages of products.

Regulation of warranty for products sold to consumers is defined in the Czech Civil Code, which was amended by Act No. 136/2002 Coll., effective as of 1 January 2003. This amendment effectively incorporated into Czech legislation the substance of regulations contained in the Directive of the European Parliament and Council 1999/44/EC on certain aspects of the sale of consumer goods and associated guarantees.

According to the amended Civil Code, a seller (i.e. an individual or legal entity acting within the scope of its business or other entrepreneurial activity) is liable for any defects of goods sold to a consumer that reflect “inconsistencies with the agreement,” provided that such defects appear within the mandatory **24-month warranty period**. Moreover, a seller’s liability for defects of consumer products, as stipulated in the Civil Code, cannot be excluded or restricted by mutual agreement between the seller and the buyer, although such liability can be expanded contractually.



For detailed information on Czech Republic product safety & consumer protection matters please contact:

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