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Taxation of Business Income in the Czech Republic

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Objects of PIT

- Income from dependent activity (employment), incl. emoluments of office-holders (function benefits);
- Income from independent (i.e. business other gainful) activity;
- Capital (property) income;
- Rental (lease) income;
- Other income.

Taxpayer

- Tax residents – natural persons with a residential address in the Czech Republic or individuals who usually stay in the Czech Republic (it means for at least 183 days in the relevant calendar year, either continuously or intermittently); these persons are liable to tax on income arising from sources in both the Czech Republic and abroad;
- Tax non-residents – natural persons not mentioned above as tax residents, student from abroad or patients staying in the Czech Republic for the purpose of medical treatment; they are liable to tax on incomes arising only from sources in the Czech Republic

Objects of taxation in case of business incomes

- agriculture production, forestry and fish farming,
- business (trade)
- other commercial activities (for example experts, interpreters, arbitrators, bankruptcy trustees, etc.)
- shares of partners in profits of a general partnership and general partners' shares in profits of a limited partnership
- income from the use or provision of industrial or other intellectual property and from copyright,
- income from pursuit of an independent profession
- income from rent of business property

Tax base

- incomes reduced by the expenses incurred to generate, assure and maintain income
- **lump sum expenses:**
 - 80 % of the income from agricultural production, forestry and fish farming and from handicraft industry;
 - 60 % of the income from other industry and trades;
 - 40 % of the income from other business (for example lawyers, doctors, etc.) and other incomes like incomes from intellectual property, etc.;
 - 30 % of the income from rents of business property

- the main purposes of the lump sum expenses are practical aspects and administrative simplification, not the tax relief
- this institute is overused and sometimes even misused

For example me as author of the textbook: I have no real expenses, but I have to tax only 60 % of my income.

- lump sum expenses can be used only if the maximum value of lump sum expenses does not exceed:
 - 1.600.000 CZK in case of incomes from agricultural production, forestry and fish farming and from handicraft industry;
 - 1.200.000 CZK in case of incomes from other industry and trades;
 - 800.000 CZK in case of incomes from other business and other incomes like incomes from intellectual property, etc.;
 - 600.000 CZK in case of incomes from rents of business property

- this limitation is not applied in practice very often as small businessmen usually do not reach the income higher than 2 billion CZK
- at least officially, because until November 2016 there is no existence of a duty to issue tax bills in the Czechia: there is no legal obligation to issue a tax bill, unless the customer asks for one.
- nobody needs the bill: employed persons have no possibility to deduct their expenses while calculating the tax and self-employed persons are usually using lump sum expenses and that is why they do not ask for tax bills, too.
- this practice leads to illegal reduction of taxable incomes and in the end to lower tax revenue

- another limitation of lump sum expenses:
 - if the sum of partial tax bases where the lump sum expenses were applied (i.e. possibly income from independent activity and rental income) is higher than the sum of the other partial tax bases, it is not possible to apply tax reduction for a spouse living with the taxpayer in one household and tax preferences for children
 - it is quite easy to avoid this rule, especially if the taxpayer is employed in the same time, because of the construction of the partial tax base from dependent activity
 - the other possibility is to use the spouse or children as the cooperative person(s) – they can use their own basic tax reduction instead

- the limitation of lump sum expenses impact on those businessmen who are single, childless, or if their spouse is on maternity leave
- these exemptions are creating several possible and legal, but different tax duties, and the taxpayer is forced to calculate the tax several times in different ways to find the best (i.e. lowest) tax duty

- as a problem I find different rates of lump sum expenses for different types of incomes
- benefits of lump sum expenses are causing in other problem, in the Czechia known as Svarcsystem

Ways to reduce the number of entrepreneurs using lump sum expenses

- an obligation to issue tax bills would lead to higher taxable incomes and higher expenditures
- the lump sum expenses should be lower in general
- more differences between the types of incomes
- the lump sum expenses should be used only by those who are not the VAT payers
- every taxpayer using lump sum expenses should have at least one employee

Tax rate

- the basic rate: 15 %
- since 2013 so called special solidary surcharge 7%
 - average salary multiplied by 48

Correction Components

- **incomes** generally **not liable to** personal income **tax**
- **tax exemptions**
- **tax allowances** to get modified (reduced) tax base
 - the value of gifts (2 – 15 % of the tax base)
 - pension insurance (maximum 12.000 CZK)
 - private life insurance premiums (maximum 12.000 CZK)
 - interest paid in the taxable period on a mortgage/loan
 - Remunerations for exams verifying the result of continuing education (max. 10.000 CZK)

- **items deductible from the tax base**
 - tax loss in five previous taxable periods
 - 100 % (or even 110 %) of costs for research and development
 - limited cost for professional training of students
- **tax reductions**
 - 24.840 CZK for each taxpayer
 - 24.840 CZK for a spouse with limited income
 - 2.520 CZK / 5.040 CZK for disable persons
 - 16.140 CZK for the ZTP/P card holder
 - 4.020 CZK for the student
 - 18.000 CZK / 60.000 CZK for disabled employee
 - costs paid to the kindergarten (max. minimum wage)

- **tax preferences for children**
 - 13.404 CZK / 17.004 CZK / 20.604 CZK
 - if the tax after this reduction would be in minus, the tax preference is divided into two parts:
 1. tax reduction up to zero tax
 2. tax bonus (for economically active taxpayer up to 60.300 CZK), i.e. s/he “receives taxes from state”!

Formula

- Partial tax base § 6
- + **Partial tax base § 7**
- + Partial tax base § 8
- + Partial tax base § 9
- + Partial tax base § 10
- Tax base
- - Tax allowances and items deductible from the tax base
- Modified tax base (rounded down to whole hundreds)
- Tax brutto I (15 % of the tax base + possible 7 % as special solidary surcharge)
- - Tax reductions
- Tax brutto II ≥ 0
- - Tax preferences for children
- Tax netto / Tax bonus
- - / + Advance tax payments / Tax bonuses
- After payment / Over payment

Tax administration

- Financial Office determined by the residential address of the taxpayer
- **tax return** before 1.4. / 1.7.
- self-application!!!
- tax payment : within the same period
 - advance payments
- **revenue** is distributed between municipal budget, region budget and state budget

Conclusions

- 3 partial tax bases:
 - income from dependent activity (employment)
 - income from independent (i.e. business other gainful) activity incl. rental income
 - other incomes incl. capital income
- limit the number of entrepreneurs using lump sum expenses
- Electronic Revenue Registry and an obligation to issue tax bills
- percentual progressive tax rate
- limit the number of correction components
- **GOAL:** to pay taxes in time and according to law



Thank you for your attention

