

# PETERKA PARTNERS

THE CEE LAW FIRM

## HOW TO SET UP A BUSINESS IN THE CZECH REPUBLIC

CZECH REPUBLIC  
RUSSIA POLAND

SLOVAKIA  
ROMANIA

UKRAINE  
BELARUS

BULGARIA  
HUNGARY

# **HOW TO SET UP A BUSINESS IN THE CZECH REPUBLIC**

## **1) ESTABLISHING A LEGAL ENTITY IN THE CZECH REPUBLIC**

One way of doing business in the Czech Republic is to set up a legal entity. Legal entities that are established for commercial purposes are called business corporations. They include commercial companies and cooperatives. Commercial companies can be further divided into partnerships (unlimited partnerships and limited partnerships) and capital companies (limited liability companies, joint stock companies and European companies). In partnerships, their members are mostly jointly and severally liable for the debts of the company, except for limited partners in limited partnerships. In capital companies, members and shareholders are not liable for the debts of the company. A corporation is formed on the date of its entry into the Commercial Register.

### **Limited liability company**

The most commonly used type of business corporations are limited liability companies. They may be founded by one or more members. The minimum amount of registered capital is only 1 CZK. The registered capital of the company is divided into business shares that belong to individual members according to their contributions, unless otherwise stated by the company statutes.

The company is formed by the conclusion of a memorandum of association in the form of a notarial deed, while it is incorporated by registration in the Commercial Register held by the respective regional court. The company bodies of a limited liability company have a general meeting (supreme body), executives (statutory body) and an optional supervisory board. To establish and operate a company successfully, it is necessary to obtain a Trade Licence.

### **Joint Stock Company**

A Joint Stock Company is a company whose registered capital is divided into shares. Shares are issued to individual shareholders. The company is formed by the conclusion of articles of association and is incorporated by the registration in the Commercial Register.

There are two ways a Joint Stock Company can be managed – in a dualistic system or in a monistic system. The dualistic system of management is much more frequent; in such a case the general meeting of the Joint Stock Company forms the board of directors (statutory body) and the supervisory board. In the monistic system of management the general meeting of the Joint Stock Company forms the administrative board. Consequently, the administrative board elects the statutory director. In both systems of management the general meeting remains the supreme body.

The minimum registered capital of joint stock companies is 2,000,000 CZK (aprox. 80,000 EUR). A joint stock company guarantees all of its assets for its liabilities. As for shareholders, they are not required to be liable.

## **Representation**

The structural unit is referred to as a branch. Branches are registered in the Commercial Register. But there is an addition to make it clear that this is only a branch, not another legal entity. The branch has its manager appointed by a founding legal entity and acting on the basis of the power of attorney granted to the manager. Branches are recorded in the Commercial Register.

## **2) NATURAL PERSON**

It is possible to operate a business as a natural person in the Czech Republic. Natural persons are required to be liable for their debts in full.

## **3) TRADE LICENCES**

A business licence issued by the Trade Licensing Office is required for the business of both natural persons and legal entities. A foreign natural person may also set up a business in the Czech Republic. A foreigner doing business in the Czech Republic must meet the following conditions:

- be 18 years old or older
- be eligible for legal acts
- be of integrity (clean criminal record in the state where the person has citizenship)
- in the case of work activities requiring appropriate education or training to prove these conditions

In the Czech Republic, the Licence is conceived as a condition for the operation of a licensed trade (concession in the Czech Republic). This means a trade which is tied to an official concession and which cannot be operated without that concession. All licensed trades in the Czech Republic are governed by the Trade Licensing Act. Annex 3 to this Act lists all licensed trades, including the subject matter of their business, the required professional and other specific capabilities, the conditions that are required to be met and the state administration bodies which express their opinion on the concession (in some business sectors such as banking, a concession usually issued by the State is required.).

## **4) ACQUISITION OF REAL ESTATE IN THE CZECH REPUBLIC**

Under Czech law, the two most common real estate relationships are, namely (i) ownership; and (ii) rental of real estate.

### **Acquisition of real estate by a foreigner**

Foreigners including members of non-EU countries, can be a part of the acquisition of real estate, agricultural and forest land located in the territory of the Czech Republic. At present, a foreigner may,

unless a special law provides otherwise, acquire ownership of any real estate in the Czech Republic, both a foreigner as a legal entity and as a natural person. Thus, the need to set up a trading company, which was practically the easiest way for foreigners to acquire property in a legal way, and thus the main obstacle to free real estate transactions on Czech territory by foreign investors, has also disappeared. Now, foreigners do not have to investigate when buying a property how the ban, or restrictions, on the acquisition of real estate, may be bypassed. They do not even need to reside as a legal entity in the Czech Republic.

## **5) LABOUR LAW – BASIC PRINCIPLES**

The regular weekly working time in the Czech Republic is forty (40) hours. The minimum monthly wage in the Czech Republic may not currently be lower than 12,200 CZK (approximately 500 EUR). For most employees, however, a much higher minimum is payable – it is called the guaranteed wage. It is graded according to the complexity, responsibility and severity of work to eight degrees, also called minimum wage rates. The salary is paid in CZK and monthly.

The employer may determine a trial period in the employment contract. According to the general rules, the trial period should not exceed three (3) months. A longer trial period of up to six (6) months can be agreed in employment contracts for senior executive positions. The minimum annual paid holiday in the Czech Republic is four (4) weeks according to the Labour Code.

A fixed-term contract expires on the expiry of the agreed period, even if the employee is pregnant or the employee is ill. During the trial period, the employee and the employer can terminate the employment contract without giving any reason. Once the trial period passes, employees may terminate the employment contract at any time at their sole discretion on the basis of a written notice of at least two months' notice, while the employer is entitled to terminate the employment only for reasons expressly provided by the law. The employer may terminate the employment contract only in the case of a fundamental breach of the employee's duties (immediate termination), for several and repeatable breaches of the employee's duties in the case that the employee has been notified about these breaches and made aware of the possibility of unilateral termination of the employment contract (a two-month notice period) and, further the employment contract may be unilaterally terminated by the employer for organizational reasons (a two-month notice period). In the last case, the employee has a claim to severance pay. The employment contract can be also terminated by mutual consent.

## **6) PUBLIC PROCUREMENT**

The purpose of a public procurement system is to regulate contractual relations between the state, local authorities and suppliers of goods, works and services. Regarding the basic eligibility to enter the tender procedure, the law states which contractor is not eligible. It is such a contractor who has been convicted in the country of its registration for a criminal offense listed in Annex 3 to the Public Procurement Act in

the last five years before the start of the tender procedure. The law applies impunity only to the country of residence, it is not stated "in relation to the Czech Republic". Foreign suppliers can therefore apply for tenders in the Czech Republic. In the tender procedure, there is a prohibition on discrimination, so it should not happen that one supplier will have priority over another, even if it is a choice between a Czech supplier and a foreign supplier.

## **7) PROTECTION OF COMPETITION – BASIC PRINCIPLES**

In the Czech Republic, competition is governed primarily by the Act on the Protection of Competition, and the supervising authority is the Office for the Protection of Competition, which controls and supervises the competition itself and also supervises compliance with the competition law in statutory cases and the regulations of the European Union.

The Act on the Protection of Competition is also applied to proceedings in matters of competitors which may affect trade between Member States of the EU, and also is applied to the matters of competitors which have taken place abroad which distort or threaten to distort competition in the territory of the Czech Republic. However, it does not apply to actions (agreements of competitors, abuse of a dominant position, or mergers of competitors) whose effects are exclusively on the foreign market, unless an international treaty which the Czech Republic is bound to states differently.

The Competition Act bans in particular the following practices in the field of competition:

- abuse of a dominant position (the existence of a dominant position does not constitute a breach, but the dominant position should not be misused to jeopardize the interests of other competitors on the market or violate the interests of an indeterminate number of consumers);
- negotiation in conformity and cartel agreements (this is forbidden, e.g., fixed prices or market partition);
- vertical agreements (between the seller and the buyer, should not lead to restrictions of competition, e.g., limiting the buyer to buy another competitor's goods);
- economic coordination (this activity is forbidden if the coordinating person does not belong to the coordinated entity group and its outcome is similar to the effect of negotiation in conformity and cartel agreements); and
- Unfair competition (generally prohibited, including, for example, spreading misleading or false information about competitors and other entities, misleading or untrue comparisons of goods from different entities, and misuse and disclosure of business secrets).
- The relevant rules for the approval of transactions are laid down in the Competition Act. It also determines in which cases the consent of the Office for the Protection of Competition must be obtained with the realization of a certain transaction (e.g., mergers, acquisitions) and in which cases it is sufficient only to inform the Office for the Protection of Competition about a certain transaction or other action.

- If there is a breach of competition law, the competent State body may (i) require the cessation of the breach of law and the issuance of any revenues for a breach of competition law, (ii) impose a fine, (iii) prohibit the activity and (iv) to initiate criminal proceedings in which imprisonment (up to 5 years) may be imposed on legal representatives if it is a serious case.

## **8) TAXATION SYSTEM**

### **Corporate Income Tax**

Companies having their seat or place of effective management in the Czech Republic, i.e., Czech tax residents, are taxed on their worldwide income. Czech tax non-residents are taxed on Czech-source income only and are subject to specific rules. There are no provisions for group corporate taxation, i.e., consolidated returns cannot be filed, and each group company subject to Czech taxation must submit a separate tax return.

The standard corporate tax rate is 19%; a special tax rate of 5% is applied to specified collective investment funds. A withholding tax at the rates of 35, 15 or 0% are applied under certain circumstances. The withholding tax rates may be modified by provisions of double taxation treaties. Any gain on the sale of share investments generally is subject to corporate income tax of 19% unless the (extensive) participation exemption applies. Similar exemption rules apply to dividends. In general, qualifying criteria include EU/EEA tax residency, having one of the listed legal forms required, and that at least 10% of the shares have been held by the parent company for at least 12 months.

### **Transfer Pricing Rules**

Transactions between related parties should be conducted in accordance with the arm's length principle. The arm's length principle should govern the evaluation of transfer prices among associated enterprises. Companies are obliged to disclose their related party transactions in financial statements and, in particular, in an appendix to the corporate income tax return containing information about all foreign related party transactions – subject to some limitations. This information is electronically reported directly to the tax authorities.

The Czech Republic, as a member of the Joint Transfer Pricing Forum of the European Union (EU JTPF) and the Organisation for Economic Cooperation and Development (OECD), follows the OECD principles and guidelines for the content of TPD (Master file and local file). The Ministry of Finance and the General Tax Directorate have issued several methodological instructions in this respect; they are not legally binding but they serve as useful guidelines for taxpayers.

In the Czech Republic there is no legal obligation to have transfer pricing documentation prepared.

## **Investment incentives**

The total amount of investment incentives is up to 45% of eligible costs, depending on the location and size of an enterprise.

Investment incentives and subsidies include:

- Job-creation grants – Financial support for the creation of new jobs (3,800 – 11,500 EUR per new job);
- Training grants – Financial support for the training and retraining of new employees (up to 50% of eligible training costs);
- Full corporate income tax relief for up to ten years for new companies, partial relief for existing ones.

## **Personal Income Tax**

Taxable income includes the following:

- Income from dependent services (employment);
- Income from independent services (entrepreneurial activities);
- Income from capital (interest, dividends, etc.);
- Rental income;
- Other income.

For individuals, the tax year corresponds to the calendar year. For income tax purposes, income is taxed in the year when payment is actually received or, in the case of non-monetary benefits, in the year when the benefit is received. Employment income received in January relating to work performed in the previous year must be included in the tax base of the previous year.

The income of individuals is subject to a flat tax rate of 15 percent. The 15 percent flat tax on employment income is calculated based on the supergross salary, which is the gross salary increased by the social security and health insurance contributions payable by the employer. An additional 7 percent (a “solidarity tax”) is applied on income (the sum of gross salary and the self-employment tax base) exceeding the maximum annual assessment base for social security contributions (1,438,992 CZK in 2018).

Resident and non-resident individuals may claim a basic personal tax allowance of CZK 24,840 per year. Czech tax residents may claim a tax allowance of CZK 24,840 for a spouse under certain conditions, tax allowances for children, for students, for placing a child into a private pre-school activity and other tax allowances. In addition, various deductions from taxable income may apply, for instance, for interest paid on a mortgage, for private contributions paid to pension schemes and private life insurance, for gifts to charity, etc.

### **Public social security and health insurance**

The Czech health insurance rate is 4.5% and social security contribution rate is 6.5% (for the employee) and 9% for health insurance and 25% for social security (for the employer) of the employee's gross salary. Entrepreneurs contribute a percentage of the entrepreneurial tax base.

Social security contributions provide funding for three separate funds: pensions, unemployment benefits and sickness, together with other benefits. Entrepreneurs can choose whether or not to contribute to the sickness fund. There is a cap on social security for both employees/employers and entrepreneurs (CZK 1,438,992 in 2018).

### **Value Added Tax**

EU membership has greatly impacted Czech VAT rules and procedures, as EU directives, regulations and case law apply and must be adhered to by the taxpayers and tax authorities.

The standard VAT rate is 21 percent and applies to most goods and services. Two reduced rates are applied in the CR. The first reduced rate of 15 percent applies to, e.g., food products, public transportation services, social housing construction, and transfers of social housing, unless these are tax-exempt. The second reduced rate of 10 percent applies to essential baby nutrition, pharmaceuticals for human and veterinary purposes, books and newspapers.

### **Excise Duties**

The Czech excise duty system is harmonized with EU legislation. This tax applies to hydrocarbon fuels and lubricants, spirits and distilled liquors, beer, sparkling wine and tobacco products that are produced in or imported to the Czech Republic. The tax is quite high.

### **Energy Taxes**

These taxes are levied on supplies of electricity, natural and other gases, and solid fuels.

### **Tax on the Acquisition of Real Estate**

The tax is payable by the acquirer. The tax rate is 4% of the higher of the agreed price and a reference value.

### **Land Tax**

Tax on immovable property is payable by owners of immovable property located in the Czech Republic. This tax rates are low compared to other developed countries.

### **Road Tax**

A road tax is generally payable by the operator of a vehicle registered in the Czech Republic and operated for commercial purposes. These tax rates are low compared to other developed countries.



## **9) DISPUTE RESOLUTION AND JUDICIAL SYSTEM**

The judicial system in the Czech Republic is divided into three stages. It is possible to file an appeal against the decision of the court of first instance, and then it is possible to defend the appeal. There is no relationship of superiority and subordination in the system of judgments. The final decision is followed by the enforcement of the decision. There is no jury system in the Czech Republic, courts are run by professional judges. In civil and administrative proceedings, the presence of an attorney is not required in most cases, in criminal proceedings however it is.

### **Arbitration and arbitrability**

In commercial contracts, an arbitration clause is often concluded, according to which all disputes arising from a particular business contract are to be settled before an arbitration court, not a general court. In the Czech Republic, international and national arbitration may be conducted before a permanent court and an ad hoc court. These international courts have been established and operate in accordance with the Arbitration Act, based on the UNCITRAL Model Law on International Commercial Arbitration.

Not all disputes are arbitrary. Arbitration courts have limited authority on insolvency disputes, disputes related to the enforcement of decisions and consumer disputes.

### **Recognition and enforcement of decisions**

The need to recognize and enforce a judgment can occur in a situation where a natural person or legal entity seeks to enforce a foreign court's decision or an arbitration award.

The Czech Republic recognizes arbitration awards issued in a foreign state and the Czech courts perform them as domestic judgments. This procedure is based on the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and related Czech laws. Similar rules are applied in the states acceding to this Convention as is the case of Czech Arbitration Awards.

## **10) INTERNATIONAL PROTECTION OF FOREIGN INVESTMENT**

The protection of investment at the international level is ensured by multilateral and bilateral agreements, including:

- The Convention from the Seoul Conference, which set up the Multilateral Investment Guarantee Agency – MIGA (MIGA), 1985, to protect foreign investment against political risks,
- The Washington Convention on the Settlement of Investment Disputes between States and Citizens of Second States, 1965, which established the International Centre for Settlement of Investment Disputes,
- The Trade-Related Investment Measures (TRIMS), 1994, which seek to prohibit government measures against foreign investment by restricting the implementation of trade relations in

- breach of the GATT 1994 (now the World Trade Organization), and measures incompatible with the obligation to grant national treatment and the abolition of quantitative restrictions,
- Bilateral Agreements on Investment Promotion and Protection – the Czech Republic is currently party to approximately 80 bilateral agreements, including an agreement with the Russian Federation. The Czech Republic is a member of the World Trade Organization (WTO), but has ceased to act and act alone after joining the EU. The EU is considered as a customs union from the point of view of the WTO principles, as representatives of the EU in the WTO are members of the European Commission. Russia did not become a member of the World Trade Organization (WTO) until 2012 and the related legislative changes have not yet come into effect due to the long transitional period under WTO rules.

### **Protection of investments at the national level and possible restrictions**

There is no special law in the Czech Republic to protect foreign investment. Legal relations are governed by the Civil Code, the Commercial Companies Act, and other legal regulations.

\*\*\*

This information reflects the state of the Czech law as of September 30, 2018.

The above information provides only a general overview of the most common questions asked when entering the Czech market. The above information does not constitute legal consultation or advice, nor can it be considered a comprehensive overview of Czech law. In case of any specific questions or need for legal assessment, assistance or advice in a particular case please contact our company.



# PETERKA PARTNERS

THE CEE LAW FIRM

[www.peterkpartners.com](http://www.peterkpartners.com)