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DRAFT BILL ON CHANGES TO THE TAX AND INSURANCE ACTS IN CONNECTION WITH REDUCING THE PUBLIC BUDGET DEFICIT

Changes to the Income Tax Act

Changes to the VAT Act

Changes to the Inheritance, Donation and Real Estate Transfer Tax Act

Changes to the General Health Insurance Premiums Act

Act on Pension Savings Insurance Premiums and Changes to Related Acts

SPECIAL ISSUE ON THE DRAFT BILL ON CHANGES TO THE TAX AND INSURANCE ACTS AND PENSION INSURANCE PREMIUMS IN CONNECTION WITH REDUCING THE PUBLIC BUDGET DEFICIT

This special issue of Tax News provides a brief summary of the basic changes to be introduced by the government bill amending the tax and insurance acts in connection with reducing the public budget deficit (the so-called "consolidation package"). The consolidation package passed in the Chamber of Deputies with 101 votes on 7 November 2012. This simple majority of votes of all deputies will ensure the package is adopted by the Chamber of Deputies even despite its expected rejection by the Senate and a presidential veto.

Most of the proposed measures are temporary and will apply from 2013 through 2015. After that period, income tax and VAT will both be subject to an already valid act that amends legislation in connection with introducing a single collection point.

Taxation of Sole Proprietors Will Bring the Greatest Impact

Temporary Introduction of Solidarity Tax

Taxpayers whose aggregate employment-generated income (gross salary) and sectional tax base from business or any other independent gainful activity (income minus costs) exceed 48 times the average salary[1] will be subject to a 7% "solidarity tax" surcharge on the amount exceeding the limit (i.e. 15% + 7% in 2013 and 2014, and 19% + 7% in 2015). There will be a CZK 1,242,432 cap in 2013 (CZK 103,536 per month). At the same time, taxpayers subject to the solidarity tax surcharge will be required to file a tax return.

Permanent Cap on Flat-Rate Costs & Expenses

Sole proprietors will still enjoy the opportunity to deduct costs and expenses on a flat-rate basis. However, professions applying the 40% flat-rate costs and expenses deduction (such as attorneys-at-law, auditors, tax advisors, experts, writers, artists, insolvency trustees) will be subject to an overall cap of CZK 800,000. Income from leaseholds applying the 30% flat-rate costs and expenses deduction will be subject to an overall cap of CZK 600,000. In other words, the flat-rate costs and expenses applicable to income exceeding CZK 2 million per year will at all times be lower than 40% or 30% of the generated income. In other circumstances, such as income generated from a licensed trade, farming, or forestry, there will be no cap on flat-rate costs and expenses.

Limited Spouse-, Children-, and Pensioner-Related Discounts

Starting in 2013, taxpayers who apply a percentage-based discount will no longer be able to apply a tax discount to a spouse and take advantage of child-related tax relief if the sum of their sectional tax bases to which the flat-rate costs and expenses were applied exceeds 50% of their total tax base.

From 2013 through 2015, working pensioners will lose the right to a personal annual discount if they receive old-age or third-degree disability pension on 1 January of the relevant taxation period.

Permanent Increase of Withholding Tax for Tax Residents of Countries That Have Not Entered into a Double Taxation Treaty with the Czech Republic

Income paid to foreign tax residents from Czech sources will be subject to higher withholding tax of 35% (the current rate is 15%). However, the increase only applies to tax residents of countries that have not entered into a double taxation treaty or a tax information exchange treaty with the Czech Republic.

Czech tax residents continue to be subject to the 15% withholding tax rate.

[1] as determined under the Social Security Insurance Act

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Changes to the VAT Act

VAT will increase from the current 14% to 15% (reduced rate) and from 20% to 21% (basic rate) in the period from 1 January 2013 until 31 December 2015. As of 1 January 2016, a uniform VAT rate of 17.5% is planned.

The basic VAT rate will newly apply to baby diapers and certain health care products.

Changes to the Inheritance, Donation and Real Estate Transfer Tax Act

As of 1 January 2013, the real estate transfer tax is to increase from the current 3% to 4%.

Changes to the General Health Insurance Premiums Act

From 1 January 2013 until 31 December 2015, the maximum assessment base for general health insurance premiums will be abolished, which will cause mandatory payments to increase. The increase will impact all insurance premiums payers (sole proprietors, employees, and employers) if the insured's assessment base exceeds 72 times the average salary (the likely amount for 2013 is CZK 1,863,648).

Act on Pension Savings Insurance Premiums and Changes to Related Acts

The Chamber of Deputies overrode the presidential veto on 7 November 2011 and approved the original text of the draft bill on pension savings insurance premiums (Lower House print 692) and the accompanying act on amendments to acts in connection with adopting the pension savings insurance premiums act (Lower House print 693).

The adoption of these acts will in fact effect launch the second pillar of the Czech pension system, or in more precise words, the collection side of it. New mandatory cash payments – pension savings insurance premiums – will be introduced to replace a part of the pension insurance premiums. The pension savings insurance premium base is to be based on the pension insurance premiums under the act on pension insurance premiums and contributions to the state employment policy.

The pension savings insurance premium rate is 5%. The rate comprises a 3% component that is to be transferred from the pension insurance premiums (pension insurance premiums for all participants in the pension saving schemes will be 3% lower compared to the premiums of other insureds with the same type of income). The remaining 2% component consists of the funds contributed to the scheme by the participant himself.

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