LTA
LEGAL TAX AUDIT

NEWSLETTER
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LEGAL - TAX - ACCOUNTING - AUDIT

YOUR SAFE HARBOUR

UPDATE ON WORK PERFORMANCE AGREEMENTS

The consolidation package has brought major changes to work performance agreements (DPP) in relation to mandatory social security and health insurance payments. The changes were supposed to take effect from 1 July 2024. As experts pointed out already during the legislative process, the changes would mean extraordinary administrative burden for taxpayers and introduce inexplicable differences between calculation of social security and health insurance payments. For this reason, a rider was added to another bill, an amendment to the Investment Companies Act, when under debate in the Chamber of Deputies. The bill has now been passed by the Chamber of Deputies and is heading to the Senate. The proposed effective date of the new legislation is 1 January 2025.

What is still going to apply from 1 July 2024?

- Employers are obliged to keep records of all concluded DPPs and the income paid under them.
- Employers are obliged to inform the Czech Social Security Administration (ČSSZ) about each DPP in each calendar month, even if no income is paid to the employee from the DPP in that month.

What was supposed to apply from 1 July 2024, but will be abolished if the bill is passed?

- 2 limits for mandatory payment of sickness insurance were introduced depending on the number of employers that the employee worked for:

  - 25% of average monthly salary, rounded down to whole CZK 500 (i.e., CZK 10,500 in 2024) if an employee had a DPP with only one employer,

  - 40% of average monthly salary, rounded down to whole CZK 500 (i.e., CZK 17,500 in 2024) if the employee had DPPs with several employers.

- In order to assess whether these limits have been exceeded, the total of the monthly income from all DPPs concluded by the employee (for all employers) was calculated.
- If the employee's income in the given month exceeded one of the above limits, all income earned in the given month was to be subject to social security and health insurance payments.

What will apply with respect to social security and health insurance payments from 1 January 2025 if the bill is passed?

- The above rules will be abolished and new rules for social security and health insurance payments from DPPs will apply from 1 January 2025.
- DPP will in principle be treated like employment.

  - If the aggregate amount of income earned under all DPPs with one employer does not exceed CZK 4,000, the relationship will be treated as small-scale employment and will not be subject to social security or health insurance payments.

  - If the employee's income exceeds CZK 4,000, the income will be subject to social security and health insurance payments. If the CZK 4,000 limit is reached or exceeded, the DPP cannot be considered a small-scale employment.

UPDATE ON WORK PERFORMANCE AGREEMENTS

- The bill introduces a „notified DPP“ which will be subject to different rules for payment of social security and health insurance.

  - Said rules will apply on a voluntary basis if the employer registers the DPP with the ČSSZ.

  - For a notified DPP, a single limit of 25% of the average monthly salary rounded down to whole CZK 500 (CZK 10,500 in 2024) will apply.

  - An employee's income under a notified DPP up to CZK 10,499 will not be subject to social security and health insurance payments. Insurance payments will be paid from income exceeding CZK 10,500.

  - The limit will apply to all income received from all DPPs entered into by the same employee with one employer.

  - The rules will apply only to one employer in a given calendar month, the one who notifies the DPP to the ČSSZ first.

  - Employers will be able to verify with the ČSSZ whether another employer has or has not notified a DPP for the same employee.

What will apply with respect to taxes from 1 January 2025 if the bill is passed?

- Withholding tax will apply to the income received under a notified DPP up to CZK 10,499. In case of higher income, tax advances will be paid.

- For DPPs which have not been notified, the withholding tax will apply if the total income of the employee from one employer from a DPP, DPČ and employment contracts is maximum CZK 3,999 a month. Tax advances will be paid if the income exceeds this threshold.

The amendment to the Investment Companies Act, which includes the rider containing said changes to the regulation of DPPs, has passed through the third reading in the Chamber of Deputies and is waiting to be debated in the Senate and signed by the President. We will keep you posted on any developments.

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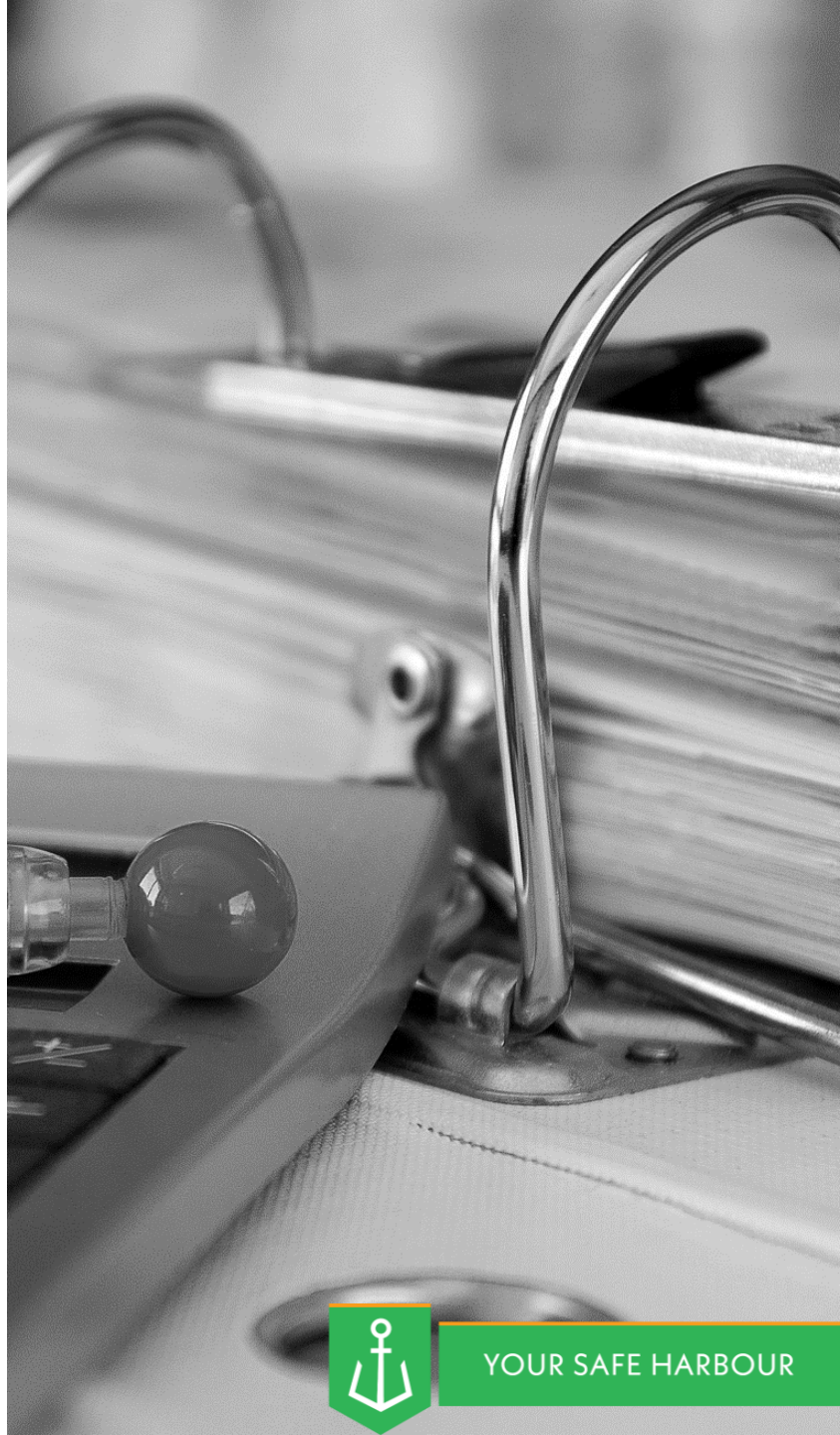

PERSONAL TAX REPORTING OBLIGATIONS

Taxpayers must file their personal income tax returns and pay any additional tax due before the deadline prescribed by the law. However, some individuals have an additional reporting obligation to the tax office and non-compliance may result in a hefty penalty. The following events occurring in the previous calendar year must be reported to the tax office:

Exempt income exceeding CZK 5 million

If a natural person receives a tax-exempt income exceeding CZK 5,000,000, they must report it to the tax office within the deadline for filing the tax return for the year in question and include the following information:

- amount of the income
- description of the circumstances of acquisition of the income
- date of acquisition of the income

The income may be reported on form no. 25 5252 which is published on the Financial Administration website or in the form of a letter stating the above information or in person on the record taken by the tax office.

Taxpayers who are not required to file a tax return must report the income no later than on 1 April of the calendar year following the year in which they received it. Individuals who do file a tax return must report the income before the deadline for filing the tax return - the deadline is extended if the tax return is filed electronically (4 months after the end of the tax year) and also if the tax return is filed by a tax adviser (6 months after the end of the tax year).

The reporting obligation applies to, for example, income received from a sale of real estate, business shares or securities for which the time test for tax exemption has been met, income received from inheritance or donations. The limit of CZK 5 million is assessed separately for each individual income. It is not necessary to report the income if the tax office is able to obtain all the required information from a public register - e.g. a sale of a house registered in the Land Register of the Czech Republic, provided that the income and the date when it was acquired are included in the information recorded in the register.

Forgetting to report the income does not pay off. Late reporting will carry a fine of 0.1% of the amount of the unreported income; if the tax office needs to call upon the taxpayer to report the income, the fine may be up to 15% of the unreported income.

Means used to fund own housing

Income from the sale of real estate for which the time test for tax exemption (2 years or 10 years) was not met is exempt from income tax, provided that the funds obtained from the sale will be or have been used to fund the acquisition of property in order to satisfy one's own housing needs. The exemption applies only if:

- within the deadline for filing the tax return for the calendar year in which the taxpayer received the income, the taxpayer reports the income to the tax office, and at the same time
- the taxpayer uses the income to fund their own housing in the calendar year in which the income was received, in the year preceding or no later than at the end of the calendar year immediately following the year in which the income was received.

PERSONAL TAX REPORTING OBLIGATIONS

The above, which is a prerequisite for obtaining the tax exemption, may be reported to the tax office in person on the record or in writing by a letter or by using form no. 25 5259 which is published on the Financial Administration website. The reporting obligation also applies to individuals who are not obliged to file a tax return (deadline: 1 April of the following calendar year). Failure to meet the reporting deadline will mean that the taxpayer will not be able to exempt the income generated from the sale of property from taxation.

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YOUR SAFE HARBOUR

EMPLOYEE'S PROBLEMATIC PERSONALITY AS A LAWFUL REASON FOR TERMINATION

Employers who have so far fought in vain against employees who, due to their problematic personality, are unable to work in a team and poison the atmosphere at the workplace, have found a sympathetic ear at the Supreme Court. The Court's decision ref. no. 21 Cdo 3366/2022 dealt with the lawfulness of termination for a failure to comply with the requirements of the job, which was justified by the employee's inability to communicate with a supervisor, failure to cooperate with colleagues, unwillingness to take responsibility for own work and arrogant behaviour and insults and slandering directed at colleagues and the director of the company. The court documents show that the employee was quarrelsome, incapable of self-reflection, focused on irrelevant matters at the expense of work tasks and prone to shifting responsibility to other employees, and that such behaviour corrupted the team to such an extent that some colleagues refused to continue working with said employee.

Termination under Section 52(f) Labour Code

The employer decided to address the situation by terminating the employee under Section 52(f) of the Labour Code. This provision contains several grounds for termination, specifically:

- Non-compliance with requirements laid down by the law for the performance of the agreed work – e.g., the employee not being allowed by the law to perform the activity in question, for example if a professional driver loses his/her driving licence;
- Long-term non-compliance with the employer's requirements through no fault of the employer - such requirements are not based on legal regulations, but set individually by employers according to their needs and may be changed from time to time; however, such requirements must always be justifiable given the nature of the work performed;
- Non-compliance may also consist in the employee's unsatisfactory performance, in which case the employee must be requested in writing to remedy the situation and only if no improvement occurs within a reasonable period of time, may the employment be terminated for this reason.

Even experts doubted whether the "request for remedy" must also precede termination for general non-compliance, i.e., termination that does not lie in the poor performance of the employee. For example, if an employer decides that employees at a certain position must know a foreign language at a certain level, it was not clear whether the employer must first provide the employee with some time to be able to learn the language and comply with the requirement. Caution advised that in such a case, the employer should comply with the requirement to "notify first" and inform the employee about his/her lack of compliance prior to terminating the employee for that reason.

Supreme Court ruling

In the present case, the Supreme Court addressed the question whether the lack of ability to communicate and cooperate can be classified as a reason for termination under Section 52(f) of the Labour Code and whether in such a case the employee must first be given time to remedy the situation.

EMPLOYEE'S PROBLEMATIC PERSONALITY AS A LAWFUL REASON FOR TERMINATION

The Supreme Court first emphasized that the application of this reason for termination does not require a breach of work duties (although it is possible that the employee's failure to comply with the requirements might also manifest itself in the breach of some duties). It is also irrelevant what the reason for non-compliance is. It is sufficient that the reason does objectively exist. However, an employee may also be in breach of his/her work duties at the same time. In such a case, it is up to the employer to decide whether to terminate the employment for one or the other reason or for both. At the same time, if the employer decides to terminate the employment for non-compliance due to the employee's personality traits that persist for a prolonged period of time, the employer may do so without any prior warning. Thus, persisting serious personality issues on the part of an employee, especially if the employee works in a managerial position, do not have to be tolerated by the employer and the employer is free to terminate the employment with said employee without warning.

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YOUR SAFE HARBOUR

UNJUST ENRICHMENT AFTER TERMINATION OF LEASE

A lease is a contractual relationship in which the tenant pays rent to the landlord for the use of a specific property, typically real estate. However, what happens if the tenant continues to occupy or use the property after the lease terminates without having the legal title to do so? In such a situation, the landlord is entitled to have the unjust enrichment on the part of the tenant returned. But how is the amount of unjust enrichment determined?

Section 2999 of the Civil Code offers some cues. Paragraph 1 of said provision sets forth that "If it is not reasonably practicable to return the object of unjust enrichment, the impoverished party is entitled to monetary compensation equal to the regular price of the object“. Paragraph 2 further provides that 'If the impoverished party performed the contract in exchange for consideration and the object of unjust enrichment cannot be returned, compensation shall be granted equal to the amount of that consideration'. According to the explanatory memorandum to section 2999, paragraph 2 is meant to be an exception to paragraph 1, i.e. if paragraph 2 can apply, paragraph 1 will not apply. Simply put, if the lease expired on 31 January 2024 and the tenant continues to (unlawfully) occupy the property without extending the lease, the tenant should pay the landlord a monetary compensation in the amount of the rent agreed in the lease whose term expired. There is no reasonable reason why the impoverished party should not receive compensation equal to the agreed price.

This is however not what happens in reality. Courts continue to apply paragraph 1 of said provision and thus award monetary compensation in the amount of the regular price, which is determined by an expert. Not only the Supreme Court (e.g. decision ref. no. 28 Cdo 3207/2021), but also the Constitutional Court (e.g. decision ref. no. I. ÚS 530/22) maintain, that an expert determines the regular price correctly, and it is therefore not necessary to take into account the existing (contractual) price agreed for the use of the property.

The courts thus continue the practice established under the previous 1964 Civil Code and resort to expert opinions, which is not only uneconomical but also completely unnecessary if the parties had agreed the price between themselves. Therefore, when filing actions for eviction and return of unjust enrichment, the claimants must take into account the current court practice, where the amount of compensation is determined on the basis of the “regular price”. Courts are of the opinion that, in a situation where an expert's opinion is available in the proceedings determining the price of regular rent, it is not appropriate for the court to determine the price of regular rent on its own, since, according to the long-term practice of the Supreme Court, this is appropriate only where the amount of the claim can be determined only with extreme difficulty or cannot be determined at all.

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CHANGE OF REGULAR WORKPLACE AND PAYMENT OF TRAVEL ALLOWANCES

While the place of work may be agreed in the employment contract in a relatively broad manner and thus reflect the employer's needs and the nature of the work performed (for some positions, the place of work may be agreed as broadly as the entire territory of the Czech Republic or even territories of several countries), an employee's regular workplace must be located in one particular municipality (or it may even be determined as a specific address within a given municipality). In case of any business travel outside the municipality of the regular workplace, the employee is entitled to travel allowances.

According to Section 34a of the Labour Code, the employee's regular workplace may be agreed in the employment contract; in such a case, it can only be changed by agreement between both the employer and the employee. If the parties do not agree a regular workplace in the employment contract, the regular workplace is defined as the place where the employee performs the work agreed in the employment contract. However, if the place of work is agreed more broadly than one municipality, the regular workplace will be the municipality where the employee's business travel most often starts.

In a recent judgment dated 23. January 2024, ref. no. 21 Cdo 2608/2023, the Supreme Court dealt with a question of how the regular workplace determined pursuant to said statutory provision in the absence of a contractual arrangement between the parties may be changed. The Court came to the following conclusion, which is rather unfavourable for employers: if the regular workplace is determined pursuant to the statutory rules set forth in Section 34a of the Labour Code, it is no different than if the regular workplace was agreed in an employment contract. Once so determined, the regular workplace may also be changed only by agreement between the parties, not unilaterally by the employer by simply changing the place from which the employee's business travel usually starts.

Therefore, if, for example, the Central Bohemian Region is agreed between the parties as the place of work and the employee starts his/her business travel from the employer's branch located in Beroun, the employee's regular workplace will be Beroun. The employee may be transferred to the branch in Kladno by a unilateral decision of the employer (as this new location is still within the agreed place of work). However, Beroun will nonetheless continue to be the employee's regular workplace, unless the employer and the employee agree to change it to Kladno.

HR departments should therefore remember that regardless of how the employee's regular workplace was determined in the past, it can only be changed by mutual agreement between the employee and the employer. Employee's refusal to change his/her regular workplace to another location may result in a significant increase in the amount of travel allowances that the employer is obliged to pay to the employee.

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RULING OF SUPREME ADMINISTRATIVE COURT: BENEFICIAL OWNER OF LICENCE FEES

The tax office did not grant a UK company's request to exempt income arising from licence fees collected in the Czech Republic for 2017, 2018 and 2019 from tax on the grounds that one of the conditions for granting the exemption was not met, namely that the UK company did not prove that it was the beneficial owner of the fees. The Municipal Court in Prague and subsequently also the Supreme Administrative Court upheld the tax office's decision. This decision follows and confirms the Supreme Administrative Court's 2019 ruling in a similar case on beneficial ownership of (sub)licence fees.

In the present case, the rights (Avon trademarks, trade names, copyrights and patent rights) were granted within the Avon group - by two American companies to a British company (for Europe, Africa and the Middle East) and by a British company to its Czech subsidiary (for the Czech Republic); in simple terms, these rights were licensed and sub-licensed. The price of the sub-licence paid by the Czech company to the UK was 6% of the Czech company's net sales, the price of the licence paid by the UK company to the US was 5.68% of net sales; the licence fees matured one month after the sub-licence fees.

Given the fact that the British company is both authorized and obligated under its license agreement with the U.S. companies to collect licence fees from the Czech company and also to pay licence fees to the U.S. companies for the same licensed rights, the Supreme Administrative Court assessed the situation as essentially the British company being under a contractual obligation to transfer the vast majority of the licence fees received from the Czech company to another entity. The Supreme Administrative Court therefore upheld the decision of the court of first instance that the British company was not the beneficial owner of the licence fees collected from the Czech company because it was not entitled to freely determine how the licence fees received would be used and it could not fully use them and enjoy them at its own discretion. The British company does not actually benefit economically from the fees received, as it is obliged to transfer 94.6667% (i.e., 5.68% of the 6%) of the fees collected from the Czech company to the American company. The Supreme Administrative Court considers the remaining 5,3333 % of the fees collected from the Czech company a remuneration paid to the British company for the performance of its obligations under the licence agreement entered into with the American companies.

The Supreme Administrative Court addressed the objections raised by the British company as follows:

- As the UK company is left with only a very small portion of the (sub)licence fees it receives, since it transfers the vast majority of them (94.6667%) to another entity, it cannot freely determine how they will be used.
- The Supreme Administrative Court does not find it relevant whether the licence fees received by the British company are aggregated with its other income. Nor is it relevant in the present case whether the British company is obliged to meet its obligation (to pay the licence fees) irrespective of whether it receives payment from the Czech company (under the sub-licence) or not.

RULING OF SUPREME ADMINISTRATIVE COURT: BENEFICIAL OWNER OF LICENCE FEES

The fact is that the British company is the sole shareholder of the Czech company and is therefore surely able to ensure that the Czech company meets its obligations arising from the licence.

In practice, the above decision of the Supreme Administrative Court poses a significant risk to intra-group licensing models for intangible assets.

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NEWS FROM LTA

- Senior associate Alice Mlýnková has been appointed partner at LTA. The appointment took effect in March. Alice is a renowned expert, particularly in the area of employment law. She is an excellent communicator praised by clients for her ability to express complex legal issues in simple terms, her friendly disposition and deep knowledge of their business.

- In March, the 2024 Talent Meeting conference, organized by the international network MGI Worldwide, was held in Frankfurt am Main. Our colleagues who joined the event appreciated the inspiring speakers and interesting encounters as well as ample opportunities to network with colleagues from other member countries. Our colleague Nina participated in the Workation project and combined her holiday in Barcelona with a work placement in an MGI partner office.

- Congratulations to our colleague Daniel Vrábel who has successfully passed his bar exam! Dan joined LTA as a student in 2017 and it has been a pleasure to see him grow within LTA. We are happy that he will soon join the ranks of our attorneys.

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