

Fundamentals Level – Skills Module

Taxation (Czech)

Monday 1 December 2008

Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

ALL FIVE questions are compulsory and MUST be attempted.

Tax rates and allowances are on pages 3–5.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

Paper F6 (CZE)

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The question paper begins on page 3.**

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest CZK if the law does not require otherwise.
2. All apportionments should be made to the nearest month.
3. All workings should be shown.

TAX RATES AND ALLOWANCES

The following 2008 tax rates and allowances are to be used in answering the questions in this paper.

Individual income tax

Individual tax rate 15%

Individual income tax credits

Personal	CZK 24,840
Child	CZK 10,680
Student	CZK 4,020

Tax depreciation periods from 2005

Group 1	3 years
Group 1a	4 years
Group 2	5 years
Group 3	10 years
Group 4	20 years
Group 5	30 years
Group 6	50 years

Depreciation rates under the straight-line method from 2005

	1st year %	following years %	for increased input price %
Group 1	20	40	33.3
Group 1a	14.2	28.6	25
Group 2	11	22.25	20
Group 3	5.5	10.5	10
Group 4	2.15	5.15	5.0
Group 5	1.4	3.4	3.4
Group 6	1.02	2.02	2

Depreciation rates for the first three groups in the case of an increase by 20% in the first year:

	1st year %	following years %	for increased input price %
Group 1	40	30	33.3
Group 2	31	17.25	20
Group 3	24.4	8.4	10

Depreciation rates under the accelerated method from 2005

	1st year	following years	for increased tax residual value
Group 1	3	4	3
Group 1a	4	5	4
Group 2	5	6	5
Group 3	10	11	10
Group 4	20	21	20
Group 5	30	31	30
Group 6	50	51	50

Depreciation periods for intangible assets

Audiovisual work	18 months
Software and the results of research and development (R&D)	36 months
Start-up costs	60 months
Other intangible assets	72 months

Tax depreciation periods up to 2004

Group 1	4 years
Group 2	6 years
Group 3	12 years
Group 4	20 years
Group 5	30 years
Group 6	50 years

Depreciation rates under the straight-line method up to 2004

	1st year %	following years %	for increased input price %
Group 1	14.2	28.6	25
Group 2	8.5	18.3	16.7
Group 3	4.3	8.7	8.4
Group 4	2.15	5.15	5.0
Group 5	1.4	3.4	3.4
Group 6	1.02	2.02	2

Depreciation rates under the accelerated method up to 2004

	1st year	following years	for increased tax residual value
Group 1	4	5	4
Group 2	6	7	6
Group 3	12	13	12
Group 4	20	21	20
Group 5	30	31	30
Group 6	50	51	50

Corporate income tax

Corporate tax rate	24%
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Value added tax (VAT)

Standard rate	19%
Reduced rate	5%
Registration threshold limit	CZK 1,000,000

Social security and health care insurance contributions

Social security	Employee's contributions	8.0%
	Employer's contributions	26.0%
Health care	Employee's contributions	4.5%
	Employer's contributions	9.0%

Repo interest rate

Rate applicable as of 1 January 2008	3.5%
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ALL FIVE questions are compulsory and MUST be attempted

1 Nautica Co is a company tax resident in Sweden but with a permanent establishment in the Czech Republic (hereafter referred to as 'Nautica PE'). Nautica PE builds small sporting yachts and also runs a travel agency organising adventure boat trips. Nautica PE's tax year is the same as the calendar year and its registered address is Vratislavova 15, Prague 2.

The following information is applicable to Nautica PE for the year 2008:

- (1) Sold boats for CZK 6,385,000.
- (2) Sold services for CZK 1,650,000.
- (3) Purchased services for CZK 888,250.
- (4) Purchased goods and materials for CZK 4,955,650.
- (5) Paid management fees to its parent company, Nautica Co, in Sweden in the equivalent of CZK 530,000.
- (6) Nautica Co is a 100% subsidiary of Nautica International, which is a tax resident of Monaco. Nautica Co's liabilities towards Nautica International's shareholders are all attributable to the Czech permanent establishment, Nautica PE. Nautica Co distributed and paid a dividend in the equivalent of CZK 3,000,000 (gross) out of its 2007 profits to Nautica International. This profit was generated and the dividend paid through Nautica PE. There has been no double tax treaty negotiated between the Czech Republic and Monaco.
- (7) Nautica PE had to pay a fine of CZK 25,000 for a breach of the law that regulates the operation of yacht transport on Czech lakes.
- (8) Nautica PE paid salaries and wages inclusive of mandatory social security and health care insurance contributions of CZK 3,105,000. All of these mandatory social security and health care insurance contributions were paid within the prescribed statutory limits. This figure only covers the social security and health care insurance contributions on the salaries and wages, not the contributions (if any) relating to the payments referred to items (9) and (10) below.
- (9) Nautica PE has five employees. In addition to salaries and wages Nautica PE paid them the following benefits, all of which were agreed in their employment contracts:
 - (i) Contribution to their pension schemes of CZK 50,000 per employee annually.
 - (ii) Contribution to their life insurance schemes of CZK 10,000 per employee annually.
 - (iii) Meal vouchers for CZK 50 per employee per working day, the total cost of which amounted to CZK 55,600.
- (10) The five employees also received the following benefits, no claim for which was incorporated in either their employment contracts or any other internal regulation of Nautica PE:
 - (i) A membership card for the Prague Yacht Club, the cost of which is CZK 9,000 per employee annually.
 - (ii) In April 2008, a payment (in cash) of CZK 70,000 per employee as a special bonus.
- (11) One boat just finished and ready to be delivered to the customer was destroyed by fire. The cost of the boat (included in the figures given in (3) and (4) above) amounted to CZK 345,000; the price agreed with the customer who had ordered the boat was CZK 462,000. Nautica PE paid a contractual penalty of CZK 20,000 to the customer because they were not able to deliver the boat within the agreed time. Nautica PE received compensation of CZK 365,000 from an insurance company.
- (12) The accounting depreciation charge of CZK 620,000 is the same as the tax depreciation charge.
- (13) According to Nautica PE's books, the following debts were unpaid as of 31 December 2008:

Due date	Amount in CZK	Creditor	Goods/services supplied
18 April 2005	584,980	Timber Ltd.	Supply of wood
2 October 2006	15,000	Uklid, s. r. o.	Cleaning services
1 August 2007	75,000	Mr Kolar	Painting of boats
15 March 2008	240,000	Transeurope, s. r. o.	Transportation services
- (14) Nautica PE organised a party for their Czech clients where they organised an auction. Nautica PE committed themselves to send all the money collected in the auction to Bariery (a Czech non-profit organisation established to assist disabled people). The costs of the party amounted to CZK 320,000 and Nautica PE collected and sent to Bariery CZK 800,000. In addition to the money from the auction, Nautica PE made a gift of CZK 200,000 to Bariery from its own resources.

- (15) In March 2008 Nautica Co sold land in Ostrava, in the Czech Republic, held by Nautica PE for CZK 12,000,000. Nautica Co had acquired the land for CZK 12,800,000 in January 2005.
- (16) Nautica PE paid 2008 corporate income tax advances of CZK 750,500 during the 2008 tax prepayment period.

Required:

- (a) (i) **Prepare Nautica PE's 2008 corporate income tax return.** (18 marks)
- (ii) **As the certified tax adviser representing Nautica PE, state when Nautica PE's 2008 corporate income tax return is due, which is the competent authority; and how any tax due (overpaid) will be settled.** (3 marks)
- (b) Nautica International plans to reorganise their business and transfer the business of Nautica PE to a Czech tax resident company, Yacht Club, a. s. in exchange for shares in that company. At the same time, Nautica International intends to sell 30% of the shares in Nautica Co to a US tax resident, Navigation Inc.

Required:

State the conditions that must be satisfied for Yacht Club, a. s. to be able to claim a deduction for the tax loss incurred by Nautica PE in 2005 and so far unused by Nautica PE and explain how if only part of this unused loss can be claimed by Yacht Club, a. s. how this part would be calculated.

Note: in answering this part, you should assume that the 2008 corporate income tax legislation will continue to apply. (9 marks)

(30 marks)

2 Mr Mares and Ms Janotova are both Czech tax residents. They have been equal (50:50) partners of a general partnership (verejina obchodni spolecnost) Maja, v. o. s. (hereafter referred to as 'Maja') since 1998.

Maja produces natural cosmetics. Since January 2001 Maja has held 51% of the shares in Kosmetyka Naturalna, a Polish tax resident and 30% of the shares in Naturalia, a Slovak tax resident. Maja's tax year is the same as the calendar year.

(1) The following information is applicable for Maja for the year 2008:

- (i) Accounting income of CZK 25,125,230.
- (ii) Accounting expenses (all tax deductible) of CZK 14,652,745.
- (iii) The accounting depreciation charge is the same as the tax depreciation charge.
- (iv) Maja owns business assets as follows:
 - An office building (depreciation group 6). Maja acquired the building in December 2004 for CZK 16,000,000 and refurbished the building (technical improvement) for CZK 4,000,000. The refurbishment works started in September 2005 and were completed in January 2007.
 - A licence to produce nettle shampoo. Maja purchased the licence from a Belgian company in January 2003. The licence agreement is for 10 years, i.e. until December 2012. The cost of this licence consists of the initial payment in the equivalent of CZK 1,800,000 and a royalty in the equivalent of CZK 310,000 per year.
 - A technological plant (depreciation group 2) acquired in 2007 for CZK 4,500,000.

Maja uses the accelerated method for the depreciation of assets where allowed.

- (v) In May 2008 Maja received dividends in the equivalent of CZK 360,000 (net) from Kosmetika Naturalna and CZK 200,000 (net) from Naturalia. Tax at the rate of 10% was withheld in Poland, but no tax was withheld in Slovakia.

(2) The following information is applicable for Mr Mares for the year 2008:

- (i) He received a dividend in the equivalent of CZK 90,000 (net) from a Dutch company, AXM. Tax at the rate of 10% was withheld in the Netherlands in compliance with the Czech–Dutch Tax Treaty.
- (ii) He received interest of CZK 120,320 from Ms Janotova, to whom he had lent CZK 2,000,000 in 2006.
- (iii) He owns a house in Prague, in which there are five flats. All the flats are let out and Mr Mares received income of CZK 1,720,000 and incurred expenses linked to the maintenance of the house of CZK 230,000 in 2008. Mr Mares inherited the house from his father in 2006 and its price for the purposes of the calculation of the inheritance tax due was CZK 38,000,000. Mr Mares depreciates the house (depreciation group 5) using the straight-line method.
- (iv) Mr Mares owns three cars, a Toyota Land Cruiser, a Skoda Octavia and a Porsche 911. He bought the Toyota in June 2007 for CZK 950,000 and the Porsche in March 1999 for CZK 3,200,000. In November 2007 he sold the Toyota for CZK 1,200,000 and the Porsche for CZK 2,500,000. None of these three cars is included in Mr Mares's business assets.
- (v) Mr Mares is a silent partner in a company, Chilli&Pepper, s. r. o., a Czech tax resident. According to the partnership agreement he is to receive a share of CZK 300,000 every year. He received his 2007 share on 25 May 2008.
- (vi) Mr Mares is married and lives in a common household with his wife Klara. Klara is severely disabled (she needs 24-hour assistance) and does not work. In 2008 she received CZK 75,860 in total from the social security system and had no other income. The spouses Mares have no children.
- (vii) In 2008 Mr Mares paid advances for income tax of CZK 130,000 per quarter. He paid all of these advances within the prescribed time limit.

Required:

- (a) (i) Calculate Mr Mares's 2008 total and final income tax liabilities. (19 marks)
- (ii) Explain how Maja, v. o. s.'s dividend income will be taxed. (1 mark)
- (iii) State what kind of documentation Mr Mares is obliged to keep as regards both the income generated through the partnership and his other types of income. (2 marks)
- (b) List SIX kinds of income, other than dividend income, that are subject to final withholding tax when received by a natural person. (3 marks)

(25 marks)

- 3** Company Stella, a. s. (hereafter referred to as Stella) is a manufacturer of glass products and a Czech monthly value added tax (VAT) payer. Stella's manufacturing site is located in Jarni 35, Desna where it also has its registered seat. All goods for domestic customers are packed in the factory shop (at the same address as the registered seat) and delivered to, or collected by, customers directly. The goods for international customers are sent to a distribution centre at Cernokostelecka 251, Prague 10, where the goods are packed and then delivered to international customers in Europe or sent to overseas customers.

The following information is applicable to Stella for May 2008. All amounts (including advance payments) are stated exclusive of VAT.

- (1) Sold and delivered goods for CZK 1,640,000 to Czech customers.
- (2) Sold and sent goods for CZK 2,800,000 to Japanese customers in Tokyo.
- (3) Sold and delivered goods for CZK 720,000 to customers in Bonn and Mannheim. Both these customers are registered as VAT payers in Germany.
- (4) Accepted an order for goods for CZK 36,000 from Crystal, s. r. o. a Czech VAT payer and received an advance payment of 10% on 15 May 2008. The goods were produced and were collected by the end of May 2008 and the remaining (90%) of the price was paid by Crystal, s. r. o. at Stella's factory shop on 2 June.
- (5) Received purchased materials for CZK 380,000. The materials were ordered and 10% prepaid in February 2008; and delivered and the remaining 90% of the price was paid in May 2008.
- (6) Purchased goods and services for CZK 950,000, all of which were ordered, delivered and paid for in May 2008.
- (7) Purchased a personal car (category M1) to be used by one of the company's directors for CZK 820,000 from a Czech dealer of Volkswagen group, with a registered seat and central garage at Jarov, Prague 3. The car was ordered and the contract signed on 10 May 2008. The car was manufactured in Ingolstadt and collected by one of Stella's employees from the garage at Jarov, Prague 3 and the director started using it on 30 May 2008.
- (8) Concluded an insurance contract in respect of the personal car in (7) above on 25 May 2008. Insurance premiums of CZK 45,000 a year are due under the contract by the end of May each year; and the first payment was made on 30 May 2008.
- (9) Purchased software for designing glass products for CZK 53,000 from Artdesign, s. r. o., whose registered seat is Vlnita 15, Prague 4. The software was ordered, paid for and delivered on May 2008. A qualified employee of Artdesign, s. r. o. installed the software on Stella's computer network at Stella's premises in Desna on 25 May 2008.
- (10) Stella has all the necessary documents in respect of all of the above transactions as required by the VAT legislation.

Required:

- (a) **Prepare Stella, a. s.'s May 2008 VAT return and state by when the VAT due should have been paid.** (6 marks)
- (b) **Assuming that Stella, a. s. did not pay its May 2008 VAT liability until 25 July 2008, calculate the penalty that will be payable in addition to the VAT liability and explain how the penalty should be paid.** (3 marks)
- (c) **Advise what Stella should do if the invoice for the software was not received from Artdesign, s. r. o. until 28 June 2008 and the date of taxable supply marked on the invoice was 28 May 2008.** (3 marks)
- (d) **In the case of each of the following, state the place of taxable supply:**
 - (i) the goods sold to Czech customers (item 1);
 - (ii) the goods sold to Japanese customers (item 2);
 - (iii) the goods sold to the German customers (item 3);
 - (iv) the goods sold to Crystal, s. r. o. (item 4);
 - (v) the purchase of the car (item 7); and
 - (vi) the supply of the software (item 9).(3 marks)

(15 marks)

4 Greco Holding GmbH has decided to establish a subsidiary in the Czech Republic. This Czech subsidiary will be responsible for the development and production of a new product.

During the first fiscal year it is expected that the subsidiary will have no income but will incur estimated costs, all of which will be related to the development of the new product, as follows:

Estimated costs	CZK
Acquisition of land	45,000,000
Acquisition of depreciable assets	65,000,000
Corresponding tax depreciation charge	9,750,000
Salaries and wages	12,320,000
Directors fees	6,800,000
Goods purchased (all tax deductible)	21,000,000
Services purchased (all tax deductible)	18,500,000
Royalties	5,500,000
Representation and entertainment costs	750,000

Required:

- (a) **Explain the relief available in respect of research and development costs, including the conditions that have to be met in order for a company to be able to claim the deduction.** (11 marks)

- (b) **Indicate how each of the estimated costs listed will be treated for the purposes of the relief and calculate the maximum deduction available to Greco Holding GmbH's subsidiary based on the estimated data.** (4 marks)

Note: you should assume that the legislation applicable in 2008 will continue to apply.

(15 marks)

- 5 Ms Kratka is a Czech tax resident. She is a professor at the Charles University in Prague where she has a part time employment contract. She is also employed with the architect studio Design, s. r. o. (hereafter referred to as 'Design').

The following information is applicable to Ms Kratka for the year 2008:

- (1) She has signed the declaration on income with the Charles University.
- (2) She receives a salary of CZK 15,000 a month from the Charles University.
- (3) The Charles University contributes CZK 500 a month to the pension schemes of each of its employees.
- (4) She receives a salary of CZK 25,000 a month from Design.
- (5) In addition to her salary Design provided her with the following benefits in 2008:
 - (i) Contributions to her pension scheme of CZK 36,000 (CZK 3,000 per month).
 - (ii) Contributions to her life insurance scheme of CZK 8,000 (all paid in December 2008).
 - (iii) Tickets to the theatre and to concerts at a cost of CZK 1,800 (all paid from the social and cultural fund of Design) in May 2008.
 - (iv) A bonus payment for work done in 2007 of CZK 64,000, paid in May 2008.
 - (v) A payment of CZK 26,500 made to Ms Kratka in December 2008 to pay for a skiing weekend in Austria for her son.
- (6) In May 2008 she received CZK 80,000 for a study of an industrial building centre based on a contract for work done (dohoda o provedení práce) concluded with the municipality of Hostivice. The documented expenses relating to this work amounted to CZK 12,000.
- (7) Also, in May 2008 she received CZK 420,000 for the plans of a house she had prepared for the family Staringer, who are tax residents of Germany, based on a contract concluded between her and the spouses Staringer. She rendered these services as a certified architect in accordance with the special law. This income was not subject to tax in Germany. The documented expenses relating to this work amounted to CZK 67,000. During 2008 she only went to Germany twice to see the place where the house should be built and she spent a total of five days there.
- (8) She paid health care insurance contributions in relation to her 2007 business income in the amount of CZK 14,560 in April 2008. She also paid health care insurance and social security advance payments for 2008 in the amount of CZK 60,000.
- (9) Every month she writes an article for the Bulletin of Architects. Under a contract concluded with the publisher for the whole year, she received CZK 1,500 for each contribution; CZK 18,000 in total for 2008.
- (10) She is a member of the supervisory board of Architects, a. s. and receives annual remuneration of CZK 50,000 for this work, which is payable at the end of March each year.

Required:

- (a) In relation to Ms Kratka's employment with Design, s. r. o., calculate for the month of December 2008:
- the payroll tax due by Design, s. r. o.; and
 - the social security and health care contributions to be withheld by Design, s. r. o. (6 marks)
- (b) Calculate Ms Kratka's 2008 individual income tax base. (9 marks)

(15 marks)

End of Question Paper