

Fundamentals Level – Skills Module

Taxation (Czech)

Monday 2 June 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 tax rates and allowances are to be used in answering the questions.

Individual income tax – 2007

Taxable income	Tax payable
CZK 0 – 121,200	12%
CZK 121,201 – 218,400	14,544 + 19% from the tax base over 121,200
CZK 218,401 – 331,200	33,012 + 25% from the tax base over 218,400
CZK 331,201 and above	61,212 + 32% from the tax base over 331,200

Individual income tax credits – 2007

Personal	CZK 7,200
Child	CZK 6,000
Student	CZK 2,400

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 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 R&D results	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 – 2007

Corporate tax rate	24%
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Value added tax

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

Social security and health care contributions – 2007

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

Self entrepreneurs:

Social security	29.6%
Health care	13.5%
Illness insurance	4.4%

ALL FIVE questions are compulsory and MUST be attempted

1 Novak & syn, s. r. o. is a company established in 1996 specialising in the breeding of roses. The company is a Czech tax resident and has been applying the fiscal year 1 September to 31 August since 2003. Novak & syn, s. r. o. is represented by a tax adviser when submitting its tax return. The following information is applicable for the fiscal year 2006/2007 (1 September 2006 to 31 August 2007):

- (1) Novak & syn, s. r. o. sold goods and services for CZK 14,672,900.
- (2) Novak & syn, s. r. o. received interest from a bank account in the amount of CZK 80,000.
- (3) Novak & syn, s. r. o. received a net royalty for the right to breed their hybrids in the equivalent of CZK 142,500 from a Danish tax resident. Tax at 5% was withheld in Denmark in accordance with the relevant tax treaty. Expenses relating to this royalty amounted to CZK 30,000 and they are included in the figures below.
- (4) Novak & syn, s. r. o. purchased goods and services for CZK 6,848,341.
- (5) Novak & syn, s. r. o. purchased new hybrids and the right to breed them from a permanent establishment of a US tax resident company, Roses, Inc situated in Sobeslav for CZK 140,000. The payment to the permanent establishment of Roses, Inc was due and paid on 25 February 2007. Novak & syn, s. r. o. owns the breeding rights as of 1 March 2007.
- (6) Novak & syn, s. r. o. paid salaries and wages amounting to 2,500,000 CZK and the relevant obligatory social security and health insurance for employees within the prescribed time limits.
- (7) Mr Jan Novak and Mr Pavel Novak are statutory representatives of the company (jednatelé). In August 2007 the company paid each of them the amount of CZK 350,000 for their duties.
- (8) Novak & syn, s. r. o. has been using two cars – an Audi A4 and a Volvo V40. Both cars are in depreciation group 1a.

Novak & syn, s. r. o. acquired the Audi in March 2006 for CZK 1,400,000 and uses the accelerated method of tax depreciation for this car.

The Volvo is used on the basis of a financial lease contract assigned to Novak & syn, s. r. o. in April 2007. The contract was originally concluded between the lessor and the company Clara, s. r. o. in March 2005 for 48 months. Clara, s. r. o. paid CZK 383,999 at the beginning and monthly payments as agreed in the amount of CZK 20,000 per month. Clara, s. r. o. paid its last payment in March 2007 and Novak & syn, s. r. o. started using the car as of April 2007. The car will be sold to the lessee at the end of the 48th month for CZK 1 according to the contract. Novak & syn, s. r. o. paid Clara, s. r. o. CZK 150,000 for the assignment of the lease contract.

- (9) Novak & syn, s. r. o. owns a mower, purchased in 2005 for CZK 170,000, for which it uses the straight-line method of depreciation. The mower is in depreciation group 2 and the depreciation charge was increased by 20% in the year of acquisition.
- (10) Novak & syn, s. r. o. built two greenhouses in June 2003. The construction costs of each greenhouse amounted to CZK 200,000. In March 2007 Novak & syn, s. r. o. added an automatic air conditioning system to one of the greenhouses, the costs of which amounted to CZK 45,000. The company uses the straight-line method for depreciation of both greenhouses, which are in depreciation group 3.
- (11) The accounting depreciation charge is the same as the tax depreciation charge.

(12) Novak & syn, s. r. o. has had the following receivables:

Due date	Amount in CZK	Accounting provision created in previous years in CZK	Tax provision created in previous years in CZK	Debtor	Title
15 May 2004	80,000	80,000	40,000	Gardens, s. r. o.	Reconstruction of a company garden
15 May 2007	11,000	0	0	Gardens, s. r. o.	Contractual penalty
15 August 2005	50,000	25,000	10,000	Mr Kudrna	Supply of roses
15 December 2005	70,000	0	0	Mr Holec	Supply of roses
15 January 2007	250,000	0	0	Rosana, a. s.	Supply of roses

All the above mentioned debtors are unrelated parties to Novak & syn, s. r. o. Court proceedings have been initiated as regards the receivables from Mr Kudrna and Mr Holec.

Novak & syn, s. r. o. assigned the receivables relating to the company Gardens, s. r. o. to the company Exekuce, a.s. on 30 June 2007 for CZK 17,100 (CZK 16,000 for the main receivable and CZK 1,100 for the receivable from the contractual penalty).

(13) Novak & syn, s. r. o. incurred a tax loss in the amount of CZK 50,000 in the tax year 2005/2006.

Required:

- (a) (i) Calculate the 2006/2007 corporate tax liability of Novak & syn, s. r. o. and state when the tax return is due. Use all tax deductible items in the maximum allowable amounts. (25 marks)
- (ii) Calculate the tax prepayments of Novak & syn, s. r. o. for the tax year 2007/2008 and state when they are due. (2 marks)
- (b) State the obligations Novak & syn, s. r. o. should have fulfilled in order to comply with the Czech tax legislation when making the payment to Roses, Inc. Your answer should include a calculation of the amount due and state the due date. (3 marks)

(30 marks)

- 2 Ms Havlova is one of two partners of a limited liability company Fineco, s. r. o., rendering financial advisory services. The company has a registered seat at Americka 7, Praha 2. Ms Havlova has her permanent home in Pribram. Ms Havlova is employed with Fineco, s. r. o. and she has signed the statement for income tax purposes with the company. At the same time Ms Havlova is one of three statutory representatives of the company (jednatel).

In 2007 she received from the company the following income:

- (1) A salary of CZK 35,000 per month based on the employment contract concluded between Fineco, s. r. o. and Ms Havlova. She worked for Fineco, s. r. o. for 12 months.
- (2) A statutory representative's fee of CZK 1,527,000 in December 2007.
- (3) Travel allowances within the statutory limit of CZK 180,000.
- (4) A distribution of Fineco, s. r. o.'s 2006 profit in the amount of CZK 425,000 (net).
- (5) Ms Havlova stays in an apartment in Belgicka 18, Praha 2, rented by the company, from Monday to Friday. The company pays a monthly rent of CZK 20,000 directly to the owner of the flat.
- (6) Fineco, s. r. o. pays gym membership for all its employees, including Ms Havlova, the costs of which are CZK 15,000 per employee per year from the social and cultural fund (after tax).
- (7) Fineco, s. r. o. pays for all its employees, including Ms Havlova, pension insurance contributions in the amount of 10% of their gross salary and life insurance premiums of CZK 15,000 per employee per year (paid each December). The contracts on pension insurance and life insurance fulfill all the conditions prescribed by the income tax legislation.

In addition, the following information is applicable to Ms Havlova for the year 2007:

- (i) Ms Havlova owns a chalet in Harrachov. She lets the chalet occasionally and she received a rent payment of CZK 25,000 in 2007.
- (ii) Ms Havlova received payments for legal services she provided to the company ABC, a. s. in February, June and October in the overall amount of CZK 1,500,000.
- (iii) Ms Havlova collects contemporary art and paintings. In September 2007 she sold two paintings for CZK 65,000. She had acquired the paintings in February 2002 for CZK 50,000.
- (iv) Ms Havlova has a loan (stavebni sporeni) for the reconstruction of her house in Pribram, where she lives. In 2007 she paid interest of CZK 43,750 on this loan.
- (v) Ms Havlova has a son Petr Havel (she is a single mother). Petr is 25 years old and he studies medicine at the Charles University in Prague. He lives with his mother in Pribram. Petr had no taxable income in 2007.
- (vi) Ms Havlova paid no health insurance and social security advances during 2007.

Required:

- (a) **Prepare Ms Havlova's 2007 tax return and calculate the tax base, the total tax liability, the payroll tax withheld by her employer and her tax due.** (17 marks)
- (b) **Calculate Ms Havlova's 2007 health insurance contributions and social security contributions to be paid in addition to those withheld by her employer, given that Ms Havlova does not pay the illness insurance.** (4 marks)
- (c) **Calculate how much tax Ms Havlova would save if her son acted as a cooperating person and the maximum possible amount of income was allocated to Petr Havel.** (4 marks)

(25 marks)

3 Investment, a. s. was established on 31 January 2006 and registered in the commercial register on 15 April 2006. Investment, a. s. provides financial and advisory services, sells and buys real estate and lets real estate. The following information is relevant:

- (1) Investment, a. s. bought 3,500 m² of land for CZK 15,000,000 on 20 February 2006 and a house in Vinohrady for CZK 35,000,000 on 15 March 2006.
- (2) The company owns and lets five houses and one administrative building in Prague. Investment, a. s. has been receiving rent of CZK 550,000 for the apartments and CZK 350,000 as rent for the offices, each month since April 2006. All rents are due on the 12th day of each month. Investment, a. s. pays a total of CZK 27,000 for electricity, CZK 37,000 for gas and CZK 14,000 for water as monthly advances for all the let buildings.
- (3) From February 2006 to August 2006 Investment, a. s. had only income from rents. From October 2006 to April 2007 it also had the following income (in addition to the rental income):

Date of taxable supply	Invoice	Title	Amount in CZK
2 September	41/2006	Financial services	2,800,000
27 September	46/2006	Financial services	13,500,000
15 October	52/2006	Financial services	7,500,000
6 November	61/2006	Advisory services	1,050,000
25 November	70/2006	Financial services	850,000
12 December	76/2006	Advisory services	300,000
4 January	1/2007	Financial services	3,000,000
21 January	12/2007	Advisory services	420,000
28 January	19/2007	Advisory services	80,000
15 February	32/2007	Financial services	5,200,000
20 February	38/2007	Advisory services	650,000
8 March	43/2007	Advisory services	200,000
16 March	49/2007	Financial services	4,200,000
20 April	55/2007	Financial services	15,000,000

No special arrangement was agreed as regards VAT on rental income.

- (4) In relation to the rendering of advisory services, Investment, a. s. purchased legal services from a company with its registered seat in Luxembourg and no permanent establishment in the Czech Republic, in February 2007, for the equivalent of CZK 1,200,000. Investment, a. s. purchased legal services from a Czech company in January 2007 for CZK 820,000, in February 2007 for CZK 220,000 and in March 2007 for CZK 80,000.
- (5) Investment, a. s. purchased equipment for their offices for CZK 1,600,000 in February 2007, from an Indian company with no permanent establishment in the Czech Republic.
- (6) Investment, a. s. purchased depreciable assets for CZK 3,000,000 in January 2007, including one personal car, the acquisition cost of which amounted to CZK 750,000.
- (7) In addition to the above, Investment, a. s. purchased services for CZK 850,000 relating to the rendering of financial services, and purchased goods and administrative services for which the VAT deduction is generally allowed, relating to all their activities, for CZK 450,000 in February 2007, and CZK 680,000 in March 2007.

All the above mentioned figures are stated exclusive of valued added tax (VAT).

Required:

- (a) **State, giving reasons, when Investment, a. s. was obliged to register with the tax administration for value added tax (VAT) purposes, when Investment, a. s. became a VAT payer and what will be the company's tax period, assuming that it will choose as long a tax period as possible.** (4 marks)
- (b) **Calculate Investment, a. s.'s first VAT liability or refund and state when it would be paid.** (11 marks)

(15 marks)

- 4 Mr Jirout is a Czech tax resident. He is employed with Vehicles, GmbH an Austrian tax resident and works in their premises in Mistelbach (Austria).

The following information is applicable for the year 2007:

- (1) In 2007 he received a salary in the equivalent of CZK 1,500,000 for his work and paid tax in the equivalent of CZK 510,000 in Austria in accordance with the double tax treaty between the Czech Republic and Austria, and mandatory social security and health care contributions in the equivalent of CZK 195,000. The exemption method with progression is to be applied for the elimination of double taxation according to the treaty.
- (2) Mr Jirout owns a vineyard in Sedlec (Czech Republic). He grows grapevines and produces wine, some of which he sells. In 2007 he sold 450 bottles of wine, for which he received CZK 60,000. He incurred costs of CZK 35,000 (all tax deductible) in relation to the wine production.
- (3) On 18 October 2006 Mr Jirout purchased 20 shares in Bianca Ltd, a tax resident of the United Kingdom, for CZK 14,000 each. On 3 April 2007 he sold 10 of the shares for CZK 18,000 each. No tax was due on this gain in the UK. Mr Jirout paid a fee of CZK 10,000 to his financial advisor in connection with the sale of the shares in Bianca Ltd. The shares were not part of Mr Jirout's business assets.

In November 2007 Mr Jirout received a dividend of CZK 5,950 net of 15% tax withheld in the UK in accordance with the double tax treaty between the Czech Republic and the UK.

Required:

- (a) **Calculate the 2007 tax liability of Mr Jirout and state whether he will pay any tax advances in the Czech Republic during 2008.** (10 marks)
- (b) **Mr Jirout has a tax adviser. He applied for the certificate of tax paid in the UK on 15 June, but had not received anything by 25 May. State how he should proceed as regards the application of the foreign tax credit for Mr Jirout's dividend income, including the relevant dates.** (2 marks)
- (c) **In the case of each of the following alternative situations, explain when, at the latest, the tax authority may check and reassess Mr Jirout's 2004 tax liability.**
 - (i) **Mr Jirout reported a tax base of CZK 25,000 and a corresponding tax liability for the tax year 2004 and submitted his tax return on 25 March 2005.** (2 marks)
 - (ii) **Mr Jirout reported a tax loss of CZK 50,000 for the tax year 2004 and submitted his tax return on 25 March 2005.** (1 mark)

(15 marks)

- 5 The board of directors of Maxima, a. s., a company operating in public relations, decided that its employees' benefits in addition to those granted by the Union contract will be as follows in the tax year 2007. Maxima, a. s. currently employs 300 persons, all of them full time.

Benefit	Estimated costs per tax year	Target group of employees
(1) Language courses at the British Council in Prague and the French Institute in Prague	CZK 6,000,000 (CZK 20,000 per employee)	All
(2) MBA courses at the Toronto School of Economy	CZK 10,000,000 (CZK 1,000,000 per employee)	10 employees selected according to given criteria
(3) Meal vouchers	CZK 4,320,000 (CZK 60 per employee per working day)	All
(4) Influenza vaccination	CZK 90,000 (CZK 300 per employee)	All
(5) Financial contribution for holidays	CZK 7,500,000 (CZK 25,000 per employee)	All
(6) Gym membership	CZK 30,000 per employee	All
(7) Transportation of employees from/to Maxima's premises	CZK 500,000	Employees working after 9 p.m. and before 6 a.m.
(8) Kindergarten/school fees for employees' children in selected private establishments	CZK 6,000,000 (assuming 50% of children will choose to attend selected establishments CZK 50,000 per child)	Employees with children (240)
(9) A new coffee machine for employees' use (replacing the old one on the 2nd floor)	CZK 25,000	All
(10) Pension insurance contributions in the amount of 10% of gross salary	CZK 2,400,000	All
(11) Life insurance contributions in the amount of 1% of gross salary	CZK 240,000	All
(12) New wrist rest mouse pads	CZK 90,000 (CZK 300 per mouse pad)	All
(13) New Blackberry sets and subscriptions	CZK 600,000 (CZK 30,000 per device)	Partners and senior managers (20)
(14) New Peugeot 407s	CZK 2,700,000 (CZK 900,000 per car)	Team leaders (3)

Required:

Write a memo to Maxima, a. s.'s financial director explaining whether the above costs may be deducted against the company's taxable income when calculating its 2007 corporate income tax liability and if so, state under what conditions.

Note: marks will be awarded for the layout and clarity of the memo.

(15 marks)

End of Question Paper