

Taxation of income of individuals as company participants

Probably the most of individuals only have income from a dependent activity or individual undertaking, however, the category of company participants is not to be neglected as it presents in several cases a source of rather higher income than a regular employment can provide and it facilitates several tax pushdown strategies. Their description as well as a wider delimitation of the taxation of individuals as company participants among the Czech taxation system are the aim of this thesis.

The whole topic is divided into five parts where apart from introduction and conclusion the fundamental terms of related commercial law, the basic institutes of taxation of individuals' income and finally the taxation of individuals as company participants itself are to be presented.

The company according to the Czech law is defined as a corporation arisen from a contract having a commercial aim. A list of exceptions exists than to these three capacities. A participant on a company is a person to whom rights and duties from the company's existence arise and whose participation is presented through the pertinence to the partnership contract or though financial contribution into the capital stock. The total of patrimonial and other rights is legally represented by a transmissible share on the company and ends in a settlement amount in case of cessation of the participation without a successor or liquidation balance after the company's liquidation.

The tax is an obligatory nonequivalent and nonpurpose contribution into the public budget based on a legal provision where the obliged person is a resident or nonresident (with a limited liability) taxpayer, the taxable object is a situation specified by the law, converted into a financial sum forming a tax base and derived than in proportion to such sum, i. e. multiplied by a concrete tax rate.

The company participant is taxed as if they performed a dependent activity while exercising any kind of work for the company. Therefore, the tax is counted as if the obligatory health and social insurance was derived and all the tax allowances can be applied. Quite voluminous judicature was already published on the theme of a company participant entering into business relations as an individual entrepreneur with the company. Such individual activity of the participant has to be exercised in a different commercial branch compared to the company's line of business. If not it shall be assessed always as a dependent activity.

The most typical income for the company participant is the capital income (dividends, share on profits) taxed with a withholding tax right at the moment of its distribution. However, the participants of companies where their personal contribution on the company's everyday business (unlimited and limited partnership) is demanded are taxed in the same way as independent individual entrepreneurs. The related expenses can be applied to reduce the tax base.

Several specific kinds of income – profits transferred to the parent company as well as the compensation paid to participants nonpertinent to controlling contract – are similarly taxed as capital income using the withholding tax.

Different tax systems are employed at the moment of alienation of the share on company. Is the share involved in the individual's business property, it is taxed as income from independent activity, therefore related expenses are to be considered. Contrarily, when the share does not form a part of the business property, its transfer is taxed as other income with the possibility to discount the expenses necessary for its obtention but not yet for its maintenance. Transmission of stocks of the incorporated companies is tax exempt under particular circumstances. The stocks have to be maintained for at least six months and the total share of the company shall not exceed 5 per cent.

The income in form of settlement amount or liquidation balance in case of corporations is taxed as other income and is submitted to the withholding tax. The acquisition cost can be deducted from the tax base. The participants of limited (those with unlimited liability) and unlimited partnerships are taxed as individuals even on the level of taxation of profits. These companies do not submit tax returns themselves, all income is taxed on the partners' level. This also is the reason why no further taxation occurs at the moment of cessation of the partner's participation or liquidation.

The voluntary conveyance of the share on a company or its transfer to successors in heritage proceedings is taxed pursuant to Inheritance and Gift Tax Act. Significant exemptions are made in this occasion to the benefit of relatives. This also leads to the effort of public authorities to extensive interpretation of the Income Taxes Act so that these issues fall into its scope. At the moment there are important discrepancies between these two acts that shall be surmounted with the new Income Taxes Act approval.