Location, Location, Location:
Where To Set Up Shop

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Location, Location, Location: Where to Set up the Shop

Czech Republic

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The relevant criterions seem to be everywhere the same, in particular

1. Is the location in a market area or in a near a market area
2. Access from home country
3. What is the environment for doing business there

   (i) Procedures to establish legal presence and to perform transactions
   (ii) Rents and price niveau
   (iii) Taxes and other duties
   (iv) Salaries and obligatory contributions for employees
   (v) Availability of local personnel

Applicability of these criterions in the Czech Repuablic

Ad 1. **Market position and geographical location**

The Czech Republic is a rather small market. The territory covers 78,864 sq km. Its total population is 10,300,000. However, as a member of the European Union the Czech Republic is a part of the European Union market, with no customs barriers. The Czech Republic is situated in the geographical center of Europe and borders Slovakia, Germany, Poland and Austria. It is, therefore, a good base for further expansion to other central and European countries.

The economy of the Czech Republic is characterized by a strong industrial base, self-sustained agriculture and fairly developed other branches of the economy. GDP growth is 2003 - 3.7 %, 2004 – 3.8 %, 2005 – expectation 4.5 %. In 2004 it was some 70 % of the old EU, 100 % of EU 25. Inflation rate was in 2004 2.6 %, 2005 some 2.2 %. Unemployment rate was 2003 7.8 %, 2004 8.3 %.

Foreign trade balance is in 2005 for the first time positive. Most important exports are motor vehicles, machinery and other equipment, the most important imports are machinery and other equipment, chemicals, chemical products.

The Czech Republic is the target for foreign capital investments, which amounted in 2004 to 4.463 mil. USD and reached 4.2 % of GDP. The total of foreign direct investments was USD 11.5 billion from 1993 to the end of 2004. Per capita it is the highest in the region. The main investors are the Netherlands, Germany and Austria; by sector manufacturing, trade and repairs, real estate and other business activities, financial intermediation and insurance.

This is due to investment incentives adopted by the Government for manufacturing, for business support services and technology centers, i.e. tax incentives, job creation grants, training and retraining grants, land transfer at symbolic price.

Resource of income is also tourism, there are around 7 million tourists in the Czech Republic every year.

Ad 2. **Access from home country**

Access is easy by air and by railway (very dense railway network), the highway system is still under construction, still incomplete is the highway connection to the east of Germany, Poland and Austria.

Ad 3. **Environment for doing business**

(i) Procedures to establish legal presence

Czech legislation enables foreign persons to conduct business in the Czech Republic under the same conditions as Czech persons.

Natural persons from European Union on European economic area may be come traders under the Czech law and carry on business in the Czech Republic after obtaining a trades license from the Trade Licensing Office.

Legal entities: A foreigner can found or co-found a Czech company or may join an existing Czech company. All Czech companies and their branch offices have to register in the Court Commercial Registry. Before that the founders must obtain a trades license. A foreign company may register a branch, especially to assess further opportunities. The branch must have a seat, defined scope of activities and appoint a manager who may be a foreigner.

A mostly used legal entity is a limited liability company (private company limited by shares). It may be founded by only one person (natural person or legal entity). The minimum registered capital is CZK 200,000 (some 8,300 USD). The legal régime of such company is similar as in other countries.

To establish a legal presence in the Czech Republic (branch or a subsidiary) requires some documents from the parent company, notarial deed, trades licenses and Court registration. All this takes some 6 weeks as from receipt of the documents from the parent company.

Law enforcement is rather slow and highly recommended are arbitration clauses in contracts.

Ownership of real property
With the exception of agricultural or forest land, foreign individuals/companies may acquire any type of real property if they have a business or a branch in the Czech Republic or individual EU nationals holding a residence permit in the Czech Republic. Non EU nationals need a residence permit or they may register a commercial company that will be the owner of the real property.

Employment of foreigners
EU citizens may work in the Czech Republic under the same conditions as the Czech citizens.
Czech citizens face up to 7 years restrictions in most EU countries, like Austria and Germany (other foreigners may be employed in Czech Republic only with a work permit and a residence permit).

Czech foreign exchange regulations and investment protection agreements guarantee the transfer of profits and capital abroad.

(ii) Rents and price niveau

There is large availability of office and other non-housing premises, the rents are similar as those in neighbouring countries. Rents for apartments are controlled for municipal housing, other housing is based on market rents, which are also similar as in other neighbouring countries.

Price niveau is similar as in neighbouring countries in hotels, transportation and certain restaurants, but consumer prices are generally much lower than in Germany and Austria.

iii) Taxes and other duties

Corporate income tax is in 2004 26 %, in 2005 24 %. Personal income tax is 15 % to 32 % of the annual taxable base.

VAT is 19 %, reduced rate of 5 % for specific services and products.

Foreign investment protection and safeguards against double taxation are guaranteed through a large number of intergovernmental bilateral agreements and these are honored.

iv) Salaries and obligatory contributions for employees

Wages and salaries are much lower than in West European countries, the average wage is only some 750 USD. The minimum wage only 320 USD. Only the salaries of top managers are equivalent to those in Western Europe.

Mandatory contributions to the social insurance system are rather high. The employer portion is 35 %, employee portion 12.5 %. All foreign companies registered in the Czech Commercial Register must pay a total 35 % of the Czech employees gross salaries towards social security and health insurance funds.

v) Availability of local personnel

Foreign companies still find in the Czech Republic local employees, either for their manufacturing facilities as well as for positions in other sector of business. This is due to a fairly high level of education, qualification and adaptability of human resources, with competitive advantages in low wages. Many people speak English, especially younger generation, or German or some other foreign language.

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The EU perspective

Chris Bryant
Crosby Renouf, Brussels

For any business seeking to expand into a different country, the choice of location is critical. There are many factors to consider and balance. When doing so within the EU, the business must be aware not only of legal considerations on a national level, but also those at EU level.

The EU has established a single market comprising the territories of 25 countries (known as "Member States"). They are Austria, Belgium, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, The Netherlands, Poland, Portugal, Slovakia, Slovenia, Spain, Sweden, and the United Kingdom. The single market also extends to Norway, Iceland and Liechtenstein (which are part of the European Economic Area) and bilateral agreements exist with Switzerland to apply single market rules in certain policy areas.

Any business seeking to establish in an EU Member State must be aware of the key features of how the EU works, so that they may maximise the benefits available to them and avoid or overcome any potential problems.

This paper sets out just a few examples of the considerations to think of, both in terms of legal advantages offered by establishment in an EU Member State and some of the pitfalls to look out for.

- **The EU single market**

In principle, any EU business has the right to establish elsewhere in the EU. Most Member States also have no restriction on non-EU business establishing themselves or setting up subsidiaries.

The EU single market is also based upon the freedom to provide services and the free movement of goods. Once established in the EU, a business selling goods has the right to market those goods throughout the EU. In doing so, depending on the nature of the business, it may have to comply with certain requirements based upon EU Directives. Furthermore, businesses in the EU have the right to provide their services throughout all EU Member States, particularly where requirements have been harmonised at EU level. A proposed Directive currently going through the legislative process aims to make it even easier to provide services, by enabling businesses where there is no harmonisation to provide services throughout the EU if they comply with the requirements of their country of origin.

- **Tax**

Most direct taxes are still dealt with on a national rather than an EU level. However, there are some aspects of EU law that should not be ignored when considering the tax aspects of a choice of location. Moreover, where a business faces problems linked with national taxation the possible application of EU principles should not be overlooked. For example, there is a case currently going through the European Court of Justice which, it is widely predicted, will allow companies established in one Member State with operations in several Member States to offset losses incurred in those other Member States.

- **Regional Aid / State Aid**

The EU has a system of "structural funds" aimed at reducing the disparities in socio-economic development in different regions. Some of these funds are available to private companies, usually as part of co-financing packages, in order to promote investment and job creation. The availability of these funds could be considered in choosing a location. Higher levels of funding are usually available in Objective 1 regions (i.e. the least prosperous regions).

Funding may also be available from national or local governments. However, in such cases, care must be taken to ensure that the funding does not unfairly distort competition and thereby constitute illegal state aid which is prohibited under the EC Treaty competition provisions. Consideration should be given to the best ways of structuring funded deals in order to ensure that the funding is not caught by the State aid rules. Failure to do so or to obtain clearance from the European Commission following notification by central government could mean that the aid can be challenged by the Commission and / or by competitors.

- **Agency / Distributor Issues**

The appointment and termination of an agent (even where the relevant agency agreement contains a choice of law clause designating the law of a non-EU country) is subject to mandatory EU protection rules benefiting the agent.

In addition, some EU Member States (such as Belgium for example) have local laws providing for mandatory compensation and indemnity payments to exclusive distributors situated in that Member State when the distribution agreement is terminated, irrespective of any choice of law clause.

- **Social security payments**

Most social issues, such as employer social security payments, are not harmonised across the EU and are set at national levels. Rates vary widely throughout the EU. However, in all Member States they must comply with requirements of equal treatment for men & women and for people of different nationalities. Furthermore, where a business has more than one base in the EU, it may be able to temporarily second staff from one Member State to another and benefit from lower social security rates in the seconding state.

- **Employment law provisions**

Various EU Directives lay down employment law provisions placing obligations on employers in respect of their workers. These Directives cover areas such as collective redundancy, working time and health and safety.

- **Enforcement**

Sanctions for breaches of EU law (such as e.g. environmental law) and the way they are enforced vary from one Member State to another. This may have a bearing on a company's choice of location. However, following a recent judgment in the European Court of Justice, it is possible that penalties for breaches of EU law may well be harmonised in the future.

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CHOOSING A SITE IN THE UNITED STATES
Environmental Issues In Acquiring Commercial/Industrial Property

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I. Environmental Risks - Property Categories: Depending on the past and future uses of a parcel of property, the property's value can be greatly affected by its environmental condition. Asbestos, lead paint, oil contamination, solvent contamination, and a myriad of other environmental conditions can turn a perceived asset into a liability.

A. Industrial Property: general manufacturing, chemical industry, petroleum industry, pharmaceuticals, biotech sites, machinery and equipment, quarries.

B. Commercial Property: shopping centers, gas stations, dry cleaners, apartment complexes, hotels.

C. Other Properties with Environmental Issues: agricultural land (farms), golf courses, waterfront properties, residential subdivision development, former landfills, recycling facilities.

II. Environmental Liability in USA: If an international company merges with or acquires the stock of a company with leases or title to real estate in the U.S., it could be purchasing more than it bargained for. A federal law passed in 1980 created strict liability for purchasers, owners, past owners and operators of contaminated property for , the costs of the government required cleanup of the contamination, among others costs. Generally, if you acquire contaminated property you also acquire the liability. Many state laws have the same liability scheme.

A. Federal Law: Comprehensive Environmental Response, Compensation, and Liability Act, 42 USC Sec. 9601, et seq. (Superfund Law)

1. **Innocent Purchaser fiction - due diligence requirement**
2. **Strict liability scheme - persons liable**
3. **Contribution/indemnification provisions**
4. **Defenses**
5. **Lender/fiduciary liability**
6. **Petroleum exclusion**
7. **Parent/Subsidiary liability**

B. State Law:

1. **State "superfund" laws - differences with federal law (petroleum exclusion, lender liability**

2. **State common law**

3. **State/federal pollution prevention laws - wetlands protection, water pollution prohibitions, forests, smart growth laws (existing infrastructure)**

III. <u>Avoidance of Liability</u>: It is possible to avoid environmental liability by structuring the acquisition to protect purchasers, take advantage of government sponsored voluntary cleanup programs and put in place several recognized devices for additional protection.

A. Structure of Transaction: stock purchase, asset purchase, merger

B. Brownfields law protections and Voluntary Cleanup Programs

C. Indemnification, Release and Covenant Not To Sue

D. Pollution Insurance

Where To Set Up a Shop

- **Why not in Switzerland?**
- **A few good reasons to do so:**
  - Political, economic and strategic reasons
  - Legal reasons
  - Tax reasons

Political, economic and strategic reasons

- **Stable political environment,**
  - No unexpected new laws or amendments
  - Low unemployment rate (~ 4%[?])
  - No ground for corruption
  - Low criminality
- **Geographical location: in the heart of Europe**
  - Companies in the logistic or supply sector
  - Headquarters
  - 4 official languages
  - Modern infrastructure

Political, economic and strategic reasons (2)

- **Specialized industries/employees**
  - Medicaments, finance, technologies
  - Strong in research and development
- **High quality standard of living**
  - Geneva and Zurich among the top ten cities of the world
  - Berne as top 3 city of the world capitals
  - Draw for executives and highly qualified employees and their families
  - Freedom of movement of people and goods within the boarders of Europe Community

Legal reasons

- **Transparent, moderate labor law**
  - Low risk of strikes
  - No strong labor unions
  - Social security in place
- **Enhanced credit status of companies formed in Switzerland**
  - Strict formation prerequisites
    - Swiss bank account mandatory
    - Incorporator’s liability
  - External auditors mandatory (Inc.)
  - Commercial accounting mandatory

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Legal reasons

- **Limitation of personal liability to invested capital**
  - However:
    - corporate veil piercing possible
    - Directors' liability
  - No class actions
- **Anonymity of shareholders**
  - Bearer shares: no registration; shareholder right contingent on mere possession

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Legal reasons

- **Effective state prosecution and law enforcement**
- **Transparent registry regulations and lean administrative machinery**
  - Expedite procedure for register entries, additions and amendments
  - reasonable register fees

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Tax reasons

- **No stamp duty for formation or capital increase (up to CHF 250’000 in total)**
- **Tax relief / concessions possible for companies for public benefit**
- **VAT of actually 7.6%**