SME - Small and Medium-sized Enterprises in the Czech Republic

Authors:
Petra Rydvalová and Kateřina Maršíková
English correction: David Gardner
2011

ISBN ………………………………………..
Contents

1. BUSINESS ENTERPRISES IN THE CZECH REPUBLIC SINCE 1918 ...................................................................................................... 5
Guide to the chapter..........................................................................................................................5
1.1 Years 1918 – 1989 .............................................................................................................. 6
1.2 Situation and development after 1989 ............................................................................... 7
   Period of a new economy ........................................................................................................... 7
   Internet e-business .................................................................................................................... 7
1.3 Definition of the SME ........................................................................................................... 8

2. THE DECISION TO START ONE’S OWN BUSINESS ................. 10
Guide to the chapter........................................................................................................................ 10
2.1 Legal conditions for starting a business ........................................................................... 12
2.2 Qualifications and competence ....................................................................................... 12
   2.2.1 Business according to trade licensing law ................................................................. 12
   2.2.2 Other business activities ............................................................................................ 13
2.3 Business liability (legal form) ......................................................................................... 14
Summary ..................................................................................................................................... 15

3. ENTREPRENEUR AS EMPLOYER ........................................... 18
Guide to the chapter........................................................................................................................ 18
3.1 Human resources in SME; terminology ........................................................................... 19
3.2 The models of personnel activities in SME ..................................................................... 20
3.3 Remuneration in the Czech entrepreneurial environment ................................................. 21
3.4 Responsibilities of the entrepreneur as employer .............................................................. 23
Summary ..................................................................................................................................... 23

4. FINANCIAL MANAGEMENT OF SMALL AND MEDIUM-SIZED ENTERPRISES ........................................................................ 24
Guide to the chapter: ...................................................................................................................... 24
4.1 Founding budget ................................................................................................................ 25
   4.1.1 Budget for Start-up Capital ......................................................................................... 25
   4.1.2 Estimated budget for the calculation of profit (loss) .................................................... 26
   4.1.3 Anticipated efficiency of enterprise ......................................................................... 26
4.2 Finances and their monitoring ............................................................................................ 27
   4.2.1 Assets and capital structure ....................................................................................... 27
   4.2.2 Depreciation of tangible and intangible assets ............................................................ 28
   4.2.3 The efficiency of the enterprise ................................................................................ 30
4.3 Profit and its management .................................................................................................. 30
   4.3.1 Price and pricing policy ............................................................................................. 30
   4.3.2 How to asses the proceeds? ....................................................................................... 33
4.4 Taxes and fees (as of 30.9.2011) ....................................................................................... 34
Table list

Table 1: New definition of SME in the EU ............................................. 9
Table 2: The necessary conditions for starting a legal form .................. 17
Table 3: The minimum wage ............................................................. 22

Figure list

Figure 1: Diagram – Business liability choice ...................................... 16
Key to symbols

- **Guide to the study** – author’s comment and follow-up information

- **Example** – from practice

- **Concept** – keep in mind

- **Summary**

- **Literature** – list of sources

- **Check** – questions

- **Essential information** – learn!

- **Correspondence homework**

- **Retrospective extra project**

- **Mind map** – this displays the contents of the chapter
1. Business enterprises in the Czech Republic since 1918

In the year 1918 Czechoslovakia was one of the most industrialised countries of the Austro-Hungarian Empire. What is the history of private business in the Czech Republic? (See Rydvalova, P., 2002)

Guide to the chapter

The contents of each chapter are shown on a mind-map:

Key words:

Business plan; E-business; History of private business; National income; Small and Medium-sized enterprises.
1.1 Years 1918 – 1989

Czechoslovakia as a newly established state was one of the most industrialised countries in the Austro–Hungarian Empire. The Austro–Hungarian Empire was therefore able to compete with other highly developed countries in Europe.

The government of the newly established Czechoslovakia operated a democratic system based on a capitalistic market economy. However, its economy was one of those strictly controlled by the capitalistic system in Europe between the two world wars. Mrs Teichová finds confirmation of this fact in the land reform of 1919 that meant a strict control of foreign currencies, as well as a further program of nationalisation of industry and banks, also in 1919. Detailed information about industry and private enterprises since the year 1930 is available. When we look at it we can see (based on the number of employees) that 99% of industrial enterprises qualify as middle-class enterprises. 20% of them are companies with less than 5 employees.

In the year 1930, only about 38.5% of national income came from the activities of SMEs (small and medium-sized enterprises). Individual entrepreneurs besides tradesmen can be found in the food processing and wood-processing industries (see chart 1). Industries were more concentrated and rationalised after the year 1933 (see the cartel law). At first, cartels were known mainly in heavy industry; in the following years they had spread to other industries. At the beginning of the world crisis, about 70% of Czech local enterprises were concentrated in cartels. This caused a reduction in opportunities for medium-sized enterprises. Cartel structures were used a lot during the German occupation of the Second World War. There was 81% foreign participation in all Czech enterprises and banks in "German hands". The importance of SMEs decreased a lot during the War.

Confiscation of foreign enterprises caused sequential destruction of private business after the Second World War (see Košice programme 1945).

The period 1945 – 1989 can be divided into these phases:

- 1945 – 1948 “Social market economy” (coexistence of market and plan).
- 1948 – 1965 Centrally planned economy (majority of employees in raw-materials sector; heavy industry caused later service sector development).
The economy during these 40 years was based on other priorities than those of the market economy in general. This system had planning as its main priority. The main objective was not to secure sales, but to fulfil planned requirements (not based on market research).

**1.2 Situation and development after 1989**

Only big companies could develop in the centrally planned economy. The conditions became friendlier to SMEs after 1989. In the year 1989, only 19 000 enterprises were registered. In 1992, at the beginning of transformation (new companies, a little privatisation, restitution, the disruption of big state enterprises), this number increased to more than 1 million registered enterprises; and in 1996 to 1.5 million. These enterprises focused mainly on the following business activities: agriculture, logging, the building industry.

Nowadays, the number of registered enterprises is about 1.2 million. It is not the number of practically working companies. Some of the businesses are registered but do no work. There are some businessmen whose activities are only temporary (enterprise in addition to employment, earning a little extra to supplement the pension).

**Period of a new economy**

The period 1998 – 2000 brought new phenomena to Czech business: the Internet, information technologies and a completely new approach based on the latest methods of communication. The opportunity for the commercial use of the Internet came with the concept of e-business and e-commerce. The new economy – the e(lectronic)-economy - is the ideal of the new information society, as a wide new area of global electronic trade. There is a long way to go to achieve this situation; it is necessary to have electronic organisation (value exchange in electronic form) or e-business.

**Internet e-business**

Electronic- or e-business is comprehended as:

- The Internet as a tool of enterprises (Internet access, software supply, hardware for e-business, web-design services, etc.).
- The Internet as a support for enterprises (marketing and advertising, elements of complex e-business – simplification and resource for competitive advantage over traditional enterprises).

There is a great opportunity for young people, students, and so on, to use e-business.
The reasons are:

- Knowledge of computer technologies, typical of the young generation.
- Low cost of starting business.
- People doing this kind of business do not depend financially on it (they often get support from their parents).

Beginners in e-business face three possible futures for their Internet activities:

1/ If their business is based on a good idea, they have quality knowledge and experience, and enough capital (without need of additional support), they will be successful and self-sufficient.

2/ E-business entrepreneurs (often individuals) are chosen by big companies which buy their businesses for a lot of money. The internet increases the chances for these entrepreneurs.

3/ The business fails and they have to close down.

E-business and classical business are very similar. They must answer the same questions:

- How and when will the business “earn money”?
- What can threaten the business aim?
- How is it possible to avoid these problems?

But there are still some differences between them:

- E-business offers the opportunity to start at little financial cost.
- The most open market is for entrepreneurs, with many opportunities for business activities.

The E-business entrepreneur must realise that the profit from e-business is not on the Internet itself but in the real world.

### 1.3 Definition of the SME

What are Small and Medium-sized enterprises (acronym SME)?

On 1 January 2005, the conditions changed and a new definition of SME became valid (see Table 1 below). The new definition, approved by the European Commission in Brussels, divides small and medium-sized enterprises into micro, small and medium-sized enterprises according to new economic criteria for the purpose of business and creation of ERA (European Research Area). This change replaced the definition of 1996.
Table 1: New definition of SME in the EU

<table>
<thead>
<tr>
<th>Enterprise Category</th>
<th>Number of employees</th>
<th>Annual turnover</th>
<th>or</th>
<th>Annual balance sheet total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medium-sized</td>
<td>&lt; 250</td>
<td>≤ 50 mil. €</td>
<td>≤ 43 mil. €</td>
<td>(in yr. 1996: 40 mil.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(in yr. 1996: 27 mil.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Small</td>
<td>&lt; 50</td>
<td>≤ 10 mil. €</td>
<td>≤ 10 mil. €</td>
<td>(in yr. 1996: 7 mil.)</td>
</tr>
<tr>
<td>Micro</td>
<td>&lt; 10</td>
<td>≤ 2 mil. €</td>
<td>≤ 2 mil. €</td>
<td>(not defined)</td>
</tr>
</tbody>
</table>


The new definition of SME divides them into the following three groups according to independence criteria:

- linked enterprises, when one company owns most of the capital or voting rights in the other company,
- partner enterprises, when one company is an upstream enterprise and owns more than 25% of the capital or voting rights in a downstream enterprise,
- autonomous enterprises that do not meet the two above mentioned criteria of independence.

Therefore, from 1 January 2005, organizations where more than 25% of the capital or voting rights are owned by public investment companies, risk capital companies, universities, non-profit centres, institutional investors to regional development or local councils, are considered to be independent organizations.

In the UK, small businesses make up about 98 per cent of all business activity with similar figures across the European Union.

Benefits of the small business
- creating employment
- increasing spending power
- SMEs can offer specialised services
- Specialised knowledge of the local business environment
- Assistance in regional and local growth
- SMEs are able to innovate easily, they are less bureaucratic, more flexible
2. The decision to start one’s own business

Where do small businesses come from?

One of the obvious starting points for a small business would be the individual who comes up with an idea for a product or service which should have place at a market.

There are two main factors to start own business

- PUSH factor (the impulse come from someone who is redundant from their job)

- PULL factor (personality of the individual finds difficult to work for someone else).

Other motives for starting up a small business could include an individual's prior experience, exposure to role models (family background with entrepreneurial activity) or level of education (both very well educated people and those who left formal education at the earliest opportunity).

Starting a business involves the following activities:

- Searching for an opportunity and the clear settings of goals.
- Establishing the legal terms.
- Evaluating economic potential and financial risk.
- Managing disposable resources and their effective allocation.
- Acquiring knowledge, hard and soft skills, and competitiveness.
- Building contacts and establishing co-operation.

Risk of own business:

- personal loss of assets;
- no guarantee that a product or service will capture a share in the market place;
- insufficient start-up capital;
- lack of knowledge and information.

Guide to the chapter

The contents of each chapter are shown on a mind-map:
To start own business…

Choice: become employed or start own business?

How to manage it correctly?

What is the subject of the business? What competencies and qualifications are necessary?

What evidence is needed?

Legal person (Czech acronym PO) = company

Natural person (Czech acronym FO) = entrepreneur

What are the legal requirements? (Business liability)

Legal person (Czech acronym PO) = company

Only filing for tax purposes

Keep accounts

What is the business?

Key words:
Branch; Business; Code of civil law; Employee; Entrepreneur; Law; Legal person; Management; Natural person; Trade; Trades licensing act.
2.1 Legal conditions for starting a business

First we specify the difference between an employee and a business person. Then it is necessary to make clear legal regulations applicable to a business subject.

For the choice between employment and starting a business we have to define a "natural person" and a "legal person" according to Czech civil law.

**The definition of a natural person:** He/she is a citizen born in the Czech Republic. The natural person must be 18 years old to achieve full legal capacity.

**The definition of an entrepreneur (physical person):** Entrepreneurs are natural people devoted to business (so-called self-employed people; Czech acronym OSVČ). They have entrepreneurial resources, which they use for the realisation of business plans, but they accept the business risk.

Entrepreneurs carry the business risk.

Their personnel property is a business liability.

**The definition of legal (juridical) person:** This is a business entity (corporation).

In the Czech Republic, people may carry out business in two ways - as a natural person (self-employed) or as a legal entity.

2.2 Qualifications and competence

It is necessary to know which law applies to the business. Most businesses come under the trade law. Therefore, before starting a business, the entrepreneur has to obtain a business licence, in most of the cases it is a trade licence.

2.2.1 Business according to trade licensing law

What is a trade?

The trade is an activity performed consistently, independently, in one's own name, on one's own responsibility, with the aim of making a profit while following the conditions set by a law. This definition is valid for both natural and legal persons.
The Trade Licensing Act identifies the following **types of trade**:

- **Notifiable trades with liability to notify.** These include
  - Unqualified trades (80 unregulated branches of production and related trade); criteria are only general conditions for operation of the trade.
  - Skilled trades (handicrafts); criterion is qualification or experience.
  - Restricted trades (more regulated); criteria are both qualifications and experience.

- **Concession trades (Licensed trades).** Criteria – obligatory qualification; the government wants control, with insurance, and there are special criteria to fulfil.

The Trade Licensing Act sets out the general conditions for pursuing a trade. These are common to all types of trade:

- minimum age of 18 years,
- legal capacity (must be competent to act legally),
- good character (no criminal record).

The general and special conditions must be fulfilled by the legal entity’s legally responsible representative.

If the entrepreneur (natural or legal person) wants to get a business licence (trade licence or concession) they must submit a request to the Trade Licensing Office. This is a contact point between business owners and public administration. The trades are recorded in the **Trade register**.

### 2.2.2 Other business activities

Other business activities that are not trades include the **pursuit of the so-called liberal professions**. These include the activities of lawyers, doctors, vets, notaries, patent agents, tax advisors, experts, interpreters, stockbrokers, etc. These activities are regulated by other specific laws.
2. 3 Business liability (legal form)

In the Czech Republic, the main legal text relating to the rights of companies is the Commercial Code.

The legal forms of business are as follows:
- sole owner, e.g. trader (Czech acronym OSVČ),
- silent partnership,
- limited liability company (Czech acronym s.r.o.),
- limited partnership (Czech acronym k.s.),
- unlimited partnership (Czech acronym v.o.s.),
- joint-stock company (Czech acronym a.s.),
- cooperative.

Sole owner – natural person (Entrepreneur)

The natural person (individual entrepreneur) can carry on business activities in their own name on the basis of a valid trade licence or other permission. In the case of a foreign non-EU individual, registration in the Commercial Register is also required.

Silent Partnership

A silent partnership is established by a written contract between a silent partner and a Czech entrepreneur. The silent partner invests in the Czech business and awaits the results – a share of the profits. Silent partners are only liable for losses to the extent of their original investment.

Limited liability Company

This legal form can be established for 1 to 50 individuals or legal entities (known as shareholders). The constitutional documents of a limited liability company are a Founding contract (where there is only a single member) or a Memorandum of Association (where there are two or more members). Both documents must be notarized. Each of the members guarantees the companies obligations to the contributing companies (creditors), but cannot be asked to contribute more than the nominal value of the shares registered in their names. The minimum registered capital for a limited liability company is CZK 200,000. Limited liability companies must establish reserves to the amount of at least 10% of the registered capital. The supreme authority of the limited liability company is the general meeting.
**Joint-stock company**

The minimum share capital condition is CZK 2 million for companies set up without a public offer for share subscription. The shares may be issued either in certificated or uncertificated (paperless) form. All joint-stock companies are required to establish reserves of at least 20% of their share capital.

**Limited and unlimited partnership**

The partners must draw up a partnership agreement. **Limited partnerships (Czech acronym - k.s.)** must have a general and a limited partner. Each of the general partners can act on behalf of the limited partnership and guarantees the obligations with unlimited liability (i.e. with his property). Each limited partner is required to make a contribution to the partnership’s registered capital of at least CZK 5,000.

In an **unlimited partnership** (Czech acronym v.o.s.), all partners (minimally two) are jointly and severally liable for the partnership’s obligations. Partnership profits are shared equally unless otherwise specified in the partnership agreement. There is no minimum capital requirement.

**Cooperative**

A cooperative must have five or more individual members, or at least two members that are legal entities. There is no maximum number of members. The minimum initial capital is CZK 50,000. The supreme authority of the cooperative is the member’s meeting. The decision making system of the member's meeting is: "one member, one vote".

**Summary**

For the start-up of the business both natural and legal persons must fill in a Single Registration Form. This form integrates administration for trade licensing, social security, health insurance, tax registration for VAT, road tax, property tax and so on.

The business liabilities of the legal person are filed in the **Commercial register**. Special forms for the registration all types of company are on the Ministry of Justice website.

Web portal BusinessInfo.cz: See “Step by step guidelines for starting a business” [online]:
Figure 1: Diagram – Business liability choice

Decision of the entrepreneur that he wants to run a business

Do I want to run a business on my own?
- Yes
  - Do I have funds available at my disposal?
    - Yes
      - Will I guarantee the obligation with my own property?
        - Yes
          - Natural person (e.g. trade)
        - No
          - Limited and unlimited partnership
            (Start a so-called personnel company; Czech acronyms: v.o.s.,
            a.s.)
    - No
      - Limited and unlimited partnership
        (Start a so-called personnel company; Czech acronyms: v.o.s.,
        a.s.)
  - No
    - Do I want run a business as a natural person?
      - Yes
        - Legal person – Corporate enterprise
          (Czech acronyms: s.r.o., a.s.)
      - No
        - Cooperation without legal entity or silent partnership

No
Questions (tasks)

Complete the Table 2:

Table 2: The necessary conditions for starting a legal form

<table>
<thead>
<tr>
<th>Legal form</th>
<th>Sole owner (e. g. trader)</th>
<th>Limited liability company</th>
<th>Limited partnership</th>
<th>Unlimited partnership</th>
<th>Cooperative</th>
<th>Joint-stock company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Necessary conditions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of founders</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minimum registered capital (CZK)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liability on engagements</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income tax</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Certificate of incorporation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bookkeeping</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reserve fond (liability)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Annual auditing</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Publication of the final accounts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Legal regulations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Suggest advantages and disadvantages of private family ownership of a business

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
3. Entrepreneur as Employer

We meet with a series of sub-problems in the framework of SME management. These sub-problems don’t exist for big concerns. The reason for these problems in small businesses is the fact that ownership and management of small enterprises are in “one person’s hands”, and the managers and owners have got other personal aims. The various aspects of personnel management in Small and Medium-sized Enterprises are:

- The simple and transparent structure of management and organization;
- The option to create business networking in groups, for reasons of larger economic and land capability (horizontal concentration), and vertical clusters with a joint strategic concept;
- The ability to prepare and train highly skilled personnel;
- The SME managers are very technical experts of the business subjects but they often don’t have knowledge and management skills concerning strategy, planning etc.

Guide to the chapter

The contents of each chapter are shown on a mind-map:

Key words:

Employee; Employer; Expensiveness (costliness) of the staff; Fire protection; Labour code; Labour protection; Management of human resources (HR) in the SME; Organizational structure; Personnel management; Recruitment of staff; Remuneration for work; Wages.
3.1 Human resources in SME; terminology

Personnel (staff)
These are people employed in an organization. It is possible to classify personnel in various ways (qualification, position in the organization, and so on).

Employment
The most frequent way of establishing employment is by the preparation and signing of a labour contract between the employee and employer.

The employee is a person (in Czech Republic from 15 years old) who has signed a labour contract with the employer.

The employer is a so-called self-employed person (in Czech OSVČ; physical person) or legal (juridical) person who is offering work in the firm.

The labour contract is a bilateral legal act, which has to fulfil nominal and content terms. The terms of the labour contract are:
- The kind of the work to be performed;
- The place of work;
- The start date of the work.

Beside these constitutional terms of the labour contract, it is possible to arrange other conditions (e.g. fixed-term contract; conditions for business trips; shift-work and so on).

Contract for work completed outside employment
- The employment agreement. This is the Contract of services for work performed outside the relationship up to 150 hours a year for one employer (Czech acronym “DPP”);
- Agreement of work activity (Czech acronym “DPČ”). This agreement shall be for work of a repetitive nature with a maximum half-time for one employer.
Social Insurance

The social insurance system in the Czech Republic includes the basic required pension insurance and sickness insurance. Apart from the social security framework, contributions to the state employment policy are also collected within the scope of the system.

*For “Self and social security” – See [online]*


Employer liability for occupational accidents and occupational diseases

Occupational injury (or illness) could afflict any employee. For the protection of employees, therefore, the Labour Act therefore establishes quite high employer liability for workplace injuries (or illnesses) of employees.

3.2 The models of personnel activities in SME

The development phase of personnel functions in SME and the creation of the personnel department are dependent not only on business size but also on the model of personnel management.

The Passive model (first phase) involves minimal personnel functions in the business process. It means to realize only those administrative personnel activities that are required by law.

The Reactive model (second phase) is when the administrative personnel functions are expanded to include a motivational system with incentive measures.

The Active model (third phase) includes the satisfaction of the personnel requirements of the business and measures to prevent personnel problems. The aim of this model is personnel system tuning (optimisation) for business strategy realization.

The Proactive model (fourth phase) comprehends personnel functions as a broad system, as the management of human resources. The person responsible for managing human resources is the executive.
The above-mentioned models can be implemented in order to start the process of the management of human resources. The several personnel activities can be structured within the personnel department in the SME as follows:

- Personnel administration (employment contract, wages administration, personnel reporting, the personnel information system).
- Personnel marketing (working station profile, entrance and selection procedure, market research into labour mobility).
- Personnel planning (personnel costs planning and scheduling).
- Personnel development (orientation of new workers, education and training, workers evaluation, personnel activity analyses, and so on).
- Organizational development (making organizational structure, working conditions, combination compensation, measuring output indicators etc.).

3.3 Remuneration in the Czech entrepreneurial environment

The common remuneration principles (for all worker groups) are defined in the Labour code. It means, for example: protection against unjustified low wage, and so on.

**Wages** are an expression of the value of the workforce in money. There are two basic types of wages:

- time wage (based on the number of the man-hours),
- job salary (based on predetermined norms).

Furthermore, there exist proportionate wages (commission) and contractual wages (agreed in the work contract). The amount of remuneration is required by law (wage floor/minimum wage) and determined by the labour market.

**Minimum wages (wages floor) and wage grades**

The minimum wage has got two basic functions in relation to employees and employers. Its Socio-protective function protects workers from poverty and makes it possible to retain social contacts. Employers should ensure equal conditions of wage competition.

The Economics-test function means the lowest level of wage costs and insurance.
The mount of minimum remuneration in the Czech Republic (in 2011) is 8000 CZK a month (approximately 312 EUR).

According to the extent of the effects of some employees’ limited ability to work, the minimum gross wage shall be: (Businessinfo.cz, 2010):

- 90% (7200 CZK, respectively 43.30 CZK/hr.) – for first job of workers aged 18-21 years, but only 6 months from the date of employment;
- 80% (6400 CZK, respectively 38.50 CZK/hr.) - young workers aged 15-17 years;
- 75% (6000 CZK, respectively 36.10 CZK/hr.) - for the employee as beneficiary of an invalidity pension (the 1. – 2. degree),
- 50% (4000 CZK, respectively 24.10 CZK/hr.) - for the employee as beneficiary of an invalidity pension (3. degree).

By the Labour Code and Regulation governments establish the minimum wage for all organizations in the business sector, where the wage conditions are not negotiated in collective agreements. These levels are graded according to the complexity, responsibility and difficulty of the work performed, in 8 groups. See table 3.

<table>
<thead>
<tr>
<th>Kind of work</th>
<th>Minimum wage (CZK/hr)</th>
<th>Minimum wage (CZK/month)</th>
<th>Base characterization</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>48.10</td>
<td>8000</td>
<td>unskilled work, manual tasks</td>
</tr>
<tr>
<td>2.</td>
<td>53.10</td>
<td>8900</td>
<td>homogenous work step-by-step instruction</td>
</tr>
<tr>
<td>3.</td>
<td>58.60</td>
<td>9800</td>
<td>Self-solving day-to-day problems</td>
</tr>
<tr>
<td>4.</td>
<td>64.70</td>
<td>10800</td>
<td>wider range of skilled activities</td>
</tr>
<tr>
<td>5.</td>
<td>71.50</td>
<td>12000</td>
<td>skilled specialized work</td>
</tr>
<tr>
<td>6.</td>
<td>78.90</td>
<td>13200</td>
<td>complicated systems work</td>
</tr>
<tr>
<td>7.</td>
<td>87.10</td>
<td>14600</td>
<td>system activities complex, transfer and application of methods</td>
</tr>
<tr>
<td>8.</td>
<td>96.20</td>
<td>16100</td>
<td>creative work with psychic intensity</td>
</tr>
</tbody>
</table>

Czech Government Regulation No. 567/2006 Coll. (It was revised 2007-08-29)
3.4 Responsibilities of the entrepreneur as employer

At the start business entrepreneurs have to ensure safety in the workroom or plant (place of business), according to Business law and the Trades licensing act (see http://www.mpo.cz/default_en.html).

They have the further statutory duty to register data pool with the tax administrator (tax office) and sign employees up for insurance (Insurance company, Czech Social Security Administration – see http://www.cssz.cz/en/obligations-of-employers/).

In the case of employment workers have to comply with the Labour code – see http://www.mpsv.cz/files/clanky/3221/labour_code.pdf.

The employer has the duty to ensure the protection of health at work; he has to teach workers about safety and hygiene at work. See http://www.mpsv.cz/en/.

The Entrepreneur-employer has the statutory duty to report vacancies to the labour office.

Summary

It is possible to find further information from the web site of the Ministry of labour and social affairs. See http://www.mpsv.cz/en/1604.

Extensive information and consultation for entrepreneurs as employers are provided here:

- Enterprise Europe Network – contact points – Czech Republic.
- EURES – contact points (The European job portal).
4. Financial management of Small and Medium-sized Enterprises

After an entrepreneur acquires information from market research, clarifies the legal issues and determines the operational aspects of his business plan, he will need to express this information monetarily and so obtain an overview of the basic economic relations, financial needs and cash flows in the process of establishing an enterprise and commencing its activities. These business calculations produce a so-called economic mini-plan (founding budget), which serves the entrepreneur during the period of establishing the enterprise and works with only a minimum of indicators. Reading this chapter is more time consuming and requires at least a basic knowledge of law and business economics.

Guide to the chapter:

The contents of each chapter are shown on a mind-map:

Key words: price, taxes, efficiency, property, capital, insurance, profitability, balance sheet, income statement, founding budget, profit, loss
4.1 Founding budget

The reason for preparing a founding budget is the need to create an overview of the one-off financial resources necessary for establishing a business until the company receives the first payments from its customers. The purpose of the founding budget is to specify and quantify the financial resources necessary to start a business and it is therefore an integral part of the business plan. The required content of the founding budget differs according to sources.

A founding budget has two basic components:

- Calculation of necessary start-up capital;
- Anticipated budget revenues, expenses and profit (loss).
- It should also include the expected cash flow and the return on invested capital (e.g. calculation of economic profit, taking into account the opportunity cost).

Starting a business can be divided into several stages:

1. Founding a company
2. Commencement of business
3. Stabilization of business

The way of financing corresponds with the listed stages – from start-up capital to the subsequent normal method of financing.

4.1.1 Budget for Start-up Capital

While creating a budget for start-up capital, an entrepreneur should be able to create the following reports:

- An overview of tangible and intangible assets, ie. cost price for provision of the premises (buildings, land, equipment, machinery, ITC, vehicles, storage equipment, administration and retail space, etc.). This concerns the area of investments (property that serves the enterprise for more than one year and is not acquired with the aim of resale). Only a small proportion of these expenses is directly accountable as expenditure in the current year. The larger proportion goes to cover the tangible and intangible property which is depreciated based on the chosen depreciation system (see below) over several years.
- An overview of the required current assets (production materials and supplies, goods, etc.).

- An overview of the requirements for operational resources (rent, wages, health and social insurance, deposits to energy suppliers, telecommunications, taxes, fees, promotion, etc.). These should be specified according to the kind of business and for the period 1 to 6 months before the company begins to receive liquid funds.

Further, it is necessary to ensure the possibility of cover, i.e. the structure of funding identified needs.

4.1.2 Estimated budget for the calculation of profit (loss)

The calculation of expected profit in year 1

The calculation of economic profit in the first year of business is determined simply by comparing projected revenues and costs (fixed and variable, and direct and overhead). In the case of entrepreneurs who keep 'only' tax records, it is the comparison of income with expenditure.

4.1.3 Anticipated efficiency of enterprise

As mentioned before, an entrepreneur should find out determine the anticipated efficiency (by comparing the output value with the input value) of his business. The choice of the contents of the input and output values determines the economic efficiency (e.g. expected revenues to costs or actual costs to the costs at an optimal combination of production factors).

\[
\text{Economic efficiency} = \frac{\text{output value}}{\text{input value}}
\]

It is clear that a small business entrepreneur will not carry out a complex financial analysis to monitor the efficiency of their business. The founding budget should include the evaluation of return on invested capital and the basic financial indicators (return on equity, total capital, etc.).

Concerning the optimal level of current assets, an entrepreneur should monitor the money turnover cycle (the period between purchase of material and receipt of payment for finished products), which means determining the time during which the company finances are tied up in current assets. We use the indicators time inventory turnover, receivables turnover, etc.
Determination of the value of cash flow is very important for entrepreneurs. It can be derived indirectly from profit (net income), adjusting costs and revenues, which does not mean cash outflows and cash receipts. The second method is direct compiling of the cash-flow, tracking cash expenses and cash receipts.

Subsequently, for the financial management of their business the entrepreneur should carry out a deeper evaluation of its performance and monitor it with groups of ratios: liquidity indicators, debt, activities, profitability, or even market value. It is necessary, of course, to consider the complexity of financial analysis in terms of company size.

### 4.2 Finances and their monitoring

#### 4.2.1 Assets and capital structure

**What is the asset structure of a company?** It's basically the ratio of individual assets of a company.

**What does the asset structure of a company depend on?** The asset structure of an enterprise (i.e. its assets) is determined both by the industry and the type of business (e.g. in a commercial company stocks of goods predominate, in a power station or engineering company the capital assets, ...), and further the financial policy of the company. The entrepreneur must try to find the optimum amount of his property. In the case of current assets, technical factors must be monitored, such as the length of the production cycle, production batch size, supply opportunities, type of materials processed, manufactured assortment range, etc.; but also customer demands for delivery of products, at the same time they must have ready cash for financial obligations.

**What is the capital structure of a company?** This is the structure of resources (liabilities) from which a company's property was created. From the perspective of those who put this capital into the company, it is divided into equity (if it was put in by the founder or a group of entrepreneurs) and loan capital (when a creditor puts money in the business). This classification applies when starting a business (see founding budget), as well as when enlarging the business assets and financing its current needs. The ratio between equity and loan capital is different for different types of business. It depends on the type of industry, the asset structure, business profitability, the bank interest rates, and finally the subjective attitude of entrepreneurs or managers of the enterprise.

**What does the size of the entrepreneurial capital depend on?** The amount of capital depends on the size of company, the degree of mechanization, automation, the speed of capital turnover (the faster the turnover, the lower the capital), sales organization, etc. One of the goals of business is property and financial stability.
At this point it is good to remember the obligation to issue records, documentation and archiving of undertakings. Some businesses have to keep accounts, for others tax records are sufficient. The obligation to keep accounts is required by accounting law, and applies to the following entities:

- Legal entities based in the Czech Republic;
- Foreign persons doing business in the Czech Republic;
- State bodies;
- Entrepreneurs registered in the Commercial Register;
- Entrepreneurs whose turnover exceeds the limit of CZK 25 million per year;
- Other natural persons on whom this requirement imposes a special legal regulation.

Businesses not listed can keep accounts voluntarily, or under the law on income tax they may only record their income, expenses, assets, debts and obligations, regarding the tax records.

**Balance sheet (annual)**

A company's balance sheet is a written overview of company's assets and its resources as of a specific date. The side listing property is called “assets”, the side listing capital and resources is called “liabilities”. The above founding budget is an exceptional balance sheet; other exceptional balance sheets are created for mergers, company break-ups, liquidations, etc.

<table>
<thead>
<tr>
<th>Assets</th>
<th>Structure of balance sheet on specific date</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>The value of all items in which the company has invested</td>
<td>All sources from which assets are acquired</td>
<td></td>
</tr>
<tr>
<td>- fixed assets</td>
<td>- Equity (capital, funds, retained earnings, current year profit (+, -))</td>
<td></td>
</tr>
<tr>
<td>- current assets</td>
<td>- Foreign capital (long-term and short-term liabilities and loans)</td>
<td></td>
</tr>
<tr>
<td><strong>Sum of assets = Sum of liabilities</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**4.2.2 Depreciation of tangible and intangible assets**

Expenditure in tangible and intangible assets is gradually transferred to the company by depreciation expenses. There are various options for depreciation. For the purposes of determining a tax base, it is tax deduction. In addition, there is depreciation for the internal purposes of the company using so-called accounting
depreciation (see Accounting Act), which determines the actual depreciation of the given property according to the experience of the enterprise in a way that is closer to reality. Depreciation is the monetary expression of the gradual wear and tear of a property over a certain period. The main purpose of depreciation is therefore to show the process of the gradual transfer of the value of such a property as an expense. As part of the operating costs, depreciation influences pricing, the overall expenses of the company and also, therefore, the amount of profit.

**Forms of tax depreciation: steady and accelerated.**

What does tax depreciation mean?

A large number of entrepreneurs do not realize that tax depreciation only reduces the tax base in the given period by a certain percentage of the purchase price of the investment. At the end of the year, they quickly buy so that the tax office (the state) will take the least possible tax. Certainly it is necessary to invest in the company, and why pay unnecessarily high taxes on revenue? Be aware, however, that the entrepreneur buys this property out of their net profit and the tax base is lowered only by a certain proportion of this investment. For the purposes of income tax, the depreciation of tangible assets (which are registered as the taxpayer’s property and used for the acquisition of taxable income) is included in the income costs (expenses for creating income). To determine the amount of depreciation the entrepreneur must know:

- The structure of assets, their purchase price and acquisition date of each individual item.
- Classification of assets into depreciation groups (see Table Y) and whether to use the steady or accelerated depreciation method for individual groups; see the aforementioned law on income tax.

For legal purposes, **tangible assets** means movables and fixtures with independent technical and economic purposes, whose input price exceeds 40,000 CZK and which have been operationally and technically functioning for more than one year (not kept in stock).

**Intangible assets** are items falling under industrial property rights, projects, software and other technical or economically useable knowledge, where the input price of individual assets exceeds 60,000 CZK and their period of use is longer than one year.

Who has the right to depreciate tangible and intangible assets? - A taxpayer who holds title to the property or holds the right of ‘management’ of the property with defined exceptions. The classification of property in depreciation groups is performed
by the taxpayer in accordance with the Annex of the Income Tax Act, and so the depreciation period is determined.

**Table 5: Depreciation Group for determining the tax depreciation**

<table>
<thead>
<tr>
<th>Depreciation group</th>
<th>Depreciation period</th>
<th>Characteristics of property</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>3 years</td>
<td>Agricultural and office machines, PC</td>
</tr>
<tr>
<td>2.</td>
<td>5 years</td>
<td>Production machines, cars, trucks, buses, tractors ...</td>
</tr>
<tr>
<td>3.</td>
<td>10 years</td>
<td>Steam boilers, cranes, elevators, electrical distribution equipment, rolling stock ...</td>
</tr>
<tr>
<td>4.</td>
<td>20 years</td>
<td>Buildings made of wood, plastic piping, electrical and telecommunication lines, power plants, ...</td>
</tr>
<tr>
<td>5.</td>
<td>30 years</td>
<td>Brick buildings, roads, bridges, dams, ...</td>
</tr>
<tr>
<td>6.</td>
<td>50 years</td>
<td>Hotel buildings, shopping centers, office, museums, libraries, ...</td>
</tr>
</tbody>
</table>

The method of tax depreciation (even or accelerated), which can be chosen by the entrepreneur for each newly acquired asset according to their needs, cannot be changed during the depreciation period. Depreciation rates and the depreciation method are described in the law on income tax.

**4.2.3 The efficiency of the enterprise**

Profit and Loss statements can use either the breakdown of costs by elements of cost or by their purpose and monitor three areas of business: operational, financial and non-recurring.

Information on the efficiency of an enterprise is obtained primarily from the income and expenses statement or profit and loss statement for the reporting period. The observed result (profit or loss = income - expenses) during the reporting period is subsequently transferred to own resources on the balance sheet. Profit and loss can be either a generic breakdown or a purposeful breakdown of costs, and concerns three business areas: operational, financial and exceptional income.

**4.3 Profit and its management**

**4.3.1 Price and pricing policy**

A company owner who believes that the calculation of prices and budgets does not concern him, and blindly sets the prices of their products or services, is very detrimental to his own enterprise, as either of the following might happen:

a) overly high prices that do not correspond with the quality or availability of a product or service will 'send' potential customers to the competition.
b) unduly low prices will not cover the business's current and future needs.

Businesses put goods on the market at prices determined by the structure and relation between supply and demand. The seller sells the goods for a price that will ensure a profit, and for the buyer, price has a great effect on their purchasing behaviour. The final price is the result of an ‘agreement’ between buyer and seller. A pricing policy includes decisions in the following areas:

- initial pricing of a product;
- change in price based on change in demand and expenses;
- change in price based on behaviour of competition.

Pricing is based on the general marketing strategy of a company – the marketing mix – which means it depends on a company's size and its market position. Large companies with a significant market share base their strategy on achieving low cost, or high innovation potential, or a combination of the two approaches. This is also reflected in their pricing policy. Companies that follow the leading companies on the market often use the strategy of conformity. Their behaviour on the market and pricing follows the behaviour of the leading companies. Small and medium enterprises that cannot compete with their large rivals on the open market often use a strategy of concentrating on certain well-defined market segments that are not profitable for large companies. Here, these companies set relatively high prices and often also achieve higher-than-average profit. The main types and methods of pricing strategies can be divided into the following groups according to their predominant orientation to profit, demand or competition.

1. Cost-plus pricing – a standard percentage is added to the cost that covers marketing costs and gross profit. The advantage of cost-plus pricing is its simplicity and transparency, its disadvantage that it does not take into account demand and competition. For calculating the price, the formula for cost breakdown is used. This is done in terms of relation to output:

a) if the costs can be determined directly, **direct calculation** is used,
b) if the overhead costs have to be somehow ‘dissolved’ in the price, **surcharge calculation** will be used. The way of dissolving them into prices using a particular base of dissolution must, therefore, be agreed upon. Most often, it is **direct wages** that are used as a base of dissolution. In this method of apportion of the overhead costs, we determine what percentage of overheads in a given period of time is born by direct costs. This method is most often used by craft businesses, small-scale manufacturers, traders and service-providers – in other words, where wages are the largest part of the calculation; these are wage-demanding activities. Further, it may be dissolution based on **material cost**. This method is used in
material-intensive industries – where material consumption exceeds direct wages. Most overheads are then tied up in storage and acquisition of material.

2. **Break-even-analysis.** This method looks for a price that would lead to a pre-planned profit.

3. **Demand-oriented pricing.** In this case, the customers’ expected value of a product (perceived value pricing) is taken as the basis for the price, not the costs or intensity of demand. This method requires a good knowledge of the market and the concerned segment, as the expected price and sales volume are the basis for the planning of production capacity, investment and costs. The buyers’ opinion on the suitability of a price can be discovered either by direct questioning or through a scoring of value accepted by the buyer for various offered products.

4. **Going rate pricing.** This pricing method is based on monitoring the prices of the competition; costs and demand become only outer margins. In this case, a company focuses on the prevalent price and its changes on the market regardless of the change in cost of their product. Most common in this category of pricing is focusing on the average price of the competition on the market. This method is preferred by smaller businesses as it prevents price shocks. It is useful for cases where costs are difficult to measure.

5. **Sealed bid pricing.** The contents of bids for public tenders remain secret until the closing day. This method is based on predicting the behaviour of the competition, how big their interest is in obtaining the contract, and what level of profit they are willing to accept.

The above given prices aim at minimizing the variation in prices. The final amount can be adjusted with regard to psychological factors. Further, it is necessary to check if the price is in accordance with the company’s overall pricing policy and its image. It is also important to consider the effect of price on suppliers, distributors, and the competition, and their reactions. The final price, however, does not reflect the relationship to individual customers and the specific conditions of some businesses. These conditions express various kinds of price adjustments, deductions, rebates (quantity connected, commercial, seasonal) and bonuses.

If the entrepreneur is a VAT payer, the appropriate VAT rate must be added to the price (see Law on value-added tax). If the product is also subject to excise duty, the price will be adjusted by this corresponding amount, too.
In the previous chapters, business was defined as an activity carried out independently by an entrepreneur in their own name on their own responsibility with the purpose of gaining a profit (see Commercial Code). Therefore, when setting up a business, an entrepreneur must be able to estimate their profit. The revenues of an enterprise at first consist mostly of proceeds from sales of:

- products
- services

4.3.2 How to asses the proceeds?

One of the methods of forecasting proceeds is the method of expected volume of sales of individual products and their predicted sale price. An entrepreneur should use information gained from market research, their ability to establish contacts with customers and suppliers, their knowledge of preliminary production capacity, and the options of expansion … and of course, their experience gained in their field of business and forecasts concerning its development and expected changes.

In addition to the expected sales volumes (amount x price) of products, business activities, provisions of work, services and other sources of revenue, an entrepreneur must define their cost needs for achieving the anticipated sales volume.

Breakdown of costs:

a) Fixed and variable costs

In the first business year of a small or medium enterprise, it is important to monitor costs in terms of their dependence on the volume of activities carried out. This is a breakdown of costs into fixed and variable costs.

Fixed costs are business expenses that are not dependent on the company's volume of production. Variable costs are the expenses that change in proportion to the volume of production. We do not include the initial purchase of stock, but only the cost of current consumption.

b) Direct and indirect costs

Entrepreneurs more often use the breakdown of costs into elements of direct and indirect costs (overheads). Direct costs are directly related to one concrete kind of a product. Indirect costs are not directly related to a concrete output (cost object) and this is why they are expressed as overheads. These are costs that cater for the running of a production process in a broader context.

Allocation of profit
Out of the profit (tax base) an entrepreneur pays the income tax of a natural or legal person. Out of the profit after tax, they have to cover loan repayments and other compulsory payments and charges (penalties, fines, payments to a superior authority within the company, etc.). After that, they are left with the net profit that is available to the company. In the case of business companies, the annual general meeting decides about its allocation. Some types of business companies have an obligation to keep reserve funds. Among company funds are – reserve funds, bonus fund, construction fund, etc. Afterwards, there is an option to freely use the profit (retained earning), which can be invested etc.

4.4 Taxes and fees (as of 30.9.2011)

The Czech tax system divides taxes into direct and indirect taxes. Direct taxes relate to the amount of the income realized, indirect taxes relate to consumption, goods and services. The chapter will focus on the issue in general. We will create a basic overview of the questions related to taxes in the Czech Republic.

4.4.1 Income tax

This act is regulated by the Income Tax Act. In terms of the Czech tax system, this is a direct tax. It specifies a natural person income tax and tax on corporate income. Generally, it can be stated that it defines: tax base; tax optimization for natural persons in the form of reallocation of income and expenditure to a spouse in a joined household - so-called cooperating persons; non-taxable income and its amount; tax rules for gifts; obligations on declaring liability for taxation; tax rates; tax deposits; types of eligible expenses (in the case of the business tax records of natural persons there is the option of fixed expenses in relation to a specific business activity) and tax deductible expenses (in the case of bookkeeping); conditions of flat rate tax; deductible items; tax relief; etc.

The following are subject to natural person income tax:
- income from employment and functional benefits (employees),
- income from enterprise and other self-employment (self-employed persons),
- investment income
- rental income
- other income

A Self-employed person (OSVČ) is a person who carries out self-employed activities or co-operates in carrying out self-employed activities, if income and expenses can be allocated to them in accordance with Act on Income Tax.
In the case of legal persons registered in the Commercial Register, the income (revenues) from all activities and the management of all corporate assets (unless stated otherwise in the Act) are subject to the tax on corporate income.

4.4.2 Road tax

This direct tax is paid for using double-tracked road vehicles and their trailers with a Czech license plate for business on domestic roads. It also applies to vehicles intended for transporting goods with a maximum permissible weight, regardless of whether they are used for business or not. The tax is paid by the vehicle owner, whose name is written on the vehicle registration certificate!

4.4.3 Value added Tax

You have already learned what a value added tax is in general economics and the theory of business. Value added tax or VAT is a state-ordered surcharge to a price. This indirect tax creates the largest income for the state out of the whole tax system. Registration for VAT is compulsory if a company's turnover exceeds 1 million Kč in 12 successive months.

4.4.4 Consumption tax

Products that ‘sell well’ despite their high taxation are subject to this tax, mostly for health and ecological reasons. Note that consumption tax is included in the base for the calculation of VAT.

Naturally, entrepreneurs are subject to other taxes, too, such as property tax or taxes placed on gratuitous acquisition of property.

4.4.5 Fees

Fees can be divided into:

- Administrative fees, concerning for example trade permits, the issuing of licenses and permits.
- Local fees, in accordance with municipal regulations at the address of the premises. This is an area that cannot be described in general terms; an entrepreneur is obliged find out the regulations and requirements in the municipality concerned. These might be charges for providing temporary accommodation (hostels, hotels, motels…), for the use of public spaces (parking
spaces…), accommodation capacity, entrance fees, permission to enter, and so on.

- Legal fees relating to business, e.g. Application for registration in the Commercial Register, etc.

### 4.4.6 Insurance

The questions of risk in business are covered in chapter 3. Insurance against risk can be divided into:

a) **State-organized insurance** (social, health and accident)

The obligation to pay health, accident and social insurance is a key element of state-organized insurance. This kind of insurance is often referred to as social security. (In this, it also differs from regular private insurance). These kinds of insurance, apart from accident insurance, are usually funded by contributions paid by employees and employers, sometimes state subsidized. Accident insurance is funded by employers only.

b) **Private insurance** (commercial)

Private insurance is provided by commercial insurance companies; this is why it is called commercial insurance. These policies are concluded beyond the state-organized insurance. This is so-called non-life insurance, such as property insurance, liability insurance etc.

1) **Health insurance**

By law, every citizen of the Czech Republic must be insured for health care provided by health facilities (i.e. the insurance company pays the costs of medical care). The law specifies who is a self-employed person, where to register for health insurance, payments for employees, the amount of the premium, deadlines for the payment of the premium, penalties for failure to comply with registration duty and order of payments owed.

An employee has the right of free choice of insurance company. An employer pays a certain part of the insurance monthly to a particular health insurance company. The health insurance premium is calculated out of employee's gross pay; part is deducted from the gross pay and part is included in the company expenses.

After the registration or announcement of the commencement of self-employment, an entrepreneur (self-employed person) starts paying deposits on health insurance payments for themselves and their employees. The deposits are entered into the accounts at the beginning of the following year. In the first business year, an entrepreneur pays a minimum amount for health insurance. At the end of the year,
they must submit an ‘Overview of income’ to the health insurance company together with a copy of their processed income tax return, on the basis of which a monthly deposit for the following year is calculated. In the case of a loss, the minimum monthly deposits are paid again in the following financial year. For more information, see the individual health insurance companies.

2) Social security insurance and contribution to state employment policy
Out of this insurance, regular monthly payments are received by an insured citizen if they cannot conduct any profit-making activity. The Social Security Act specifies in what cases social insurance must be paid, where to register, registration schedules, the amount of the insurance premium in the first business year, payments for employees, schedule of payments, penalties for failure to comply with reporting obligations, and the order of payments owed. Prescribed rates are again calculated from employees’ gross pay and consist of two parts. The first part is deducted from employees’ wages, the other is paid by the employer and included in the company’s costs. The insurance (coverage) consists of three parts: sickness insurance (not compulsory for entrepreneurs; however, if an entrepreneur wants to pay for pension insurance, they have to pay for sickness insurance, too), pension insurance and a contribution to the state employment policy.

As with health insurance, social insurance is also paid by an employer for their employees in every job, the exception being employees working under the ‘Agreement for Performance of Work’. The income resulting from this agreement is subject to income tax, but no health or social insurance is deducted from it. For more information see ‘Česká správa sociálního zabezpečení’ (Czech Social Security Administration) at http://www.cssz.cz/cz/tiskopyly/.

3) Insurance for employer’s liability for damages caused by accidents at work and occupational diseases
The previous two kinds of insurance protect every citizen against adverse life situations. Nevertheless, employees may also be exposed to the risk of accident or occupational disease. It is an employer’s obligation to prevent these. Nevertheless, these things happen, and it is an employer who bears the responsibility for, and takes the consequences of, such a situation. This kind of insurance protects not only them, but also their employees. This is why an entrepreneur must be insured against such cases. The damages are then paid by an insurance company (with the employer paying a certain percentage). The premium is calculated by the employer and paid in advance for the following quarter.
Table 6: Estimated profit (simplified form)

<table>
<thead>
<tr>
<th></th>
<th>Pessimistic variant</th>
<th>Optimistic variant</th>
<th>Average variant</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues from own products</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in inventory</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other revenue</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct material</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct wages</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health and social insurance for factory employees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Overhead costs</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw materials – auxiliary</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- office supplies</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- work hygiene</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- cleaning</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- tools</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- fuels</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- protective equipment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Power consumption</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Repairs and maintenance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Travel</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freight</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Telecommunications</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overhead wages</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health and social insurance scheme for workers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Road tax</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Property tax</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Property and liability insurance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amortization of intangible assets (tax)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation of tangible assets (tax)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Leasing – repayments</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on loans</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total overheads</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total costs</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total gross profit</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income tax for natural or legal persons</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net disposable profit</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
4.5 Assessment of the economic mini-plan for the first business year

Evaluation of a business plan that is based on acquired knowledge is best shown by the following example.

Task: Prepare an overall business budget for a company founded as a legal entity (Ltd.) in January 2010. To start-up the business, a production facility had to be purchased worth 2 million CZK. For the purposes of income tax, it will be depreciated using a steady depreciation rate (2nd depreciation group - 11% in the first year, 22.25% in the following year); required current assets to the amount of 800 000 CZK; the entrepreneur owns capital to the amount of 1.8 million CZK. Based on a survey and a qualified estimate, the forecasted product sales are 800 pieces for the month of January to June; 400 pieces for July and August; 800 pieces for September and October and 1 000 pieces for November and December, with a possible selling price of 400 CZK per item. Material consumption is 80 CZK per item. Monthly, energy worth 60 000 CZK is used. The company has 5 employees at 12 000 CZK monthly salary each. It has secured a loan with an annual interest rate of 10%, and a maturity of 10 years with the same annual amortization. At the time of starting the business, the entrepreneur had the opportunity to be employed for a net monthly income of 25 000 CZK, and could save their money with a 2% annual interest rate.

Note: you know that social and health insurance (SHI) is 34% of total gross wages and the tax rate on corporate income tax for 2010 was 19%. You also have the accompanying table, which can help you solve the example.
1) Calculation of assets and their financial cover can be specified using the table 7.

**Table 7 Calculation of assets and financial cover**

<table>
<thead>
<tr>
<th>Calculation of assets and their financial cover as of 1.1. 2010 (in million CZK)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed assets</td>
</tr>
<tr>
<td>Current assets</td>
</tr>
<tr>
<td>Total assets</td>
</tr>
</tbody>
</table>

2) For the calculation of revenues, expenses and profit, the following simplified table 8 can be used.

**Table 8 Calculation of revenues, expenses and profit**

<table>
<thead>
<tr>
<th>Calculation of revenues, expenses and profit as of 31.12.2010</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Item</strong></td>
</tr>
<tr>
<td>Revenues</td>
</tr>
<tr>
<td>Sales of products</td>
</tr>
<tr>
<td>Costs</td>
</tr>
<tr>
<td>Materials</td>
</tr>
<tr>
<td>Wages</td>
</tr>
<tr>
<td>HSI</td>
</tr>
<tr>
<td>Power consumption</td>
</tr>
<tr>
<td>Tax depreciation</td>
</tr>
<tr>
<td>Interest expense</td>
</tr>
<tr>
<td>Total costs</td>
</tr>
<tr>
<td>Profit</td>
</tr>
<tr>
<td>Income tax (legal entity)</td>
</tr>
<tr>
<td>Disposable income</td>
</tr>
</tbody>
</table>

3) For the allocation of profits and assessment of efficiency we will use a simplified form of the cash-flow document. See table 9.

**Table 9 Profit allocation**

<table>
<thead>
<tr>
<th>Profit allocation and assessment of efficiency</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Item</strong></td>
</tr>
<tr>
<td>Net (disposable) income</td>
</tr>
<tr>
<td>Tax depreciation</td>
</tr>
<tr>
<td>Annual amortization of loan (repayments)</td>
</tr>
</tbody>
</table>
The tables show the details of all three calculations. The ‘Calculation of assets and their financial cover’ showed the need for a loan of 1 million CZK. The optimistic variant of sales is in the region of 4.8 million CZK; taking into account seasonal fluctuations, sales of 3.68 million CZK are predicted. The ‘Calculation of revenues, expenses and profit’ forecasts the company achieving a net profit of 760 752 CZK in the first year. In the third calculation, ‘Profit allocation and assessment of efficiency’, we first transferred net profit to undistributed funds (or net cash flow), as these represent the actual amount that will be available to business. The effect of entrepreneurship needs to be compared with alternative opportunities, or with opportunity costs [1]. They are lost wages and lost interest. The economic profit of 744 752 CZK is positive in this case and it's worth starting the business. The entrepreneur must then subjectively consider whether they are willing to undergo the difficulty and risk associated with the business for this much economic gain.

[1] Opportunity cost - represents lost revenue from the unrealized best alternative opportunity.

Summary

The aim of this chapter is to summarize the most important aspects of management for entrepreneurs starting small and medium-sized businesses. For entrepreneurs who have not previously dealt with budgets and calculations, this is an area that is very difficult and requires perspective, ‘common sense’ and prudence. Most small entrepreneurs use the principles of outsourcing to implement activities related to accounting records and tax documents, including the preparation of tax obligations. The reason for this is that these are activities that do not bring any direct added value to the business. That is, unless the company’s business is accountancy 😊.

Questions:
1. What are the basic parts included in the economic mini-plan (founding budget) when starting a business?
2. What is depreciation? What is the difference between accounting and tax depreciation?
3. **Who** has the right to depreciate tangible or intangible property?
4. What are the **methods of tax depreciation**?
5. What are the possible **sources of funding for a business** (at least five)?
6. What is the **asset structure of a company** and what does it depend on?
7. What is **capital breakdown**?
8. Explain the term **balance sheet**.
9. What is the **pricing policy** of a business based on?
10. What are the main **types** (methods) of pricing?

**Questions with answers (sample)**

Specify indicators of cost efficiency, turnover, total capital and equity. Answer:

- Return on costs = profit / cost;
- Return on sales = profit / turnover;
- Return on total capital = profit / total capital;
- Return on equity = profit / equity (e.g. return on equity should be higher than the interest on a term deposit at the bank).
5. Enterprise in the EU

To start up a business in the EU it is necessary to respect both EU law and the national law. Article 49 of the Treaty on the functioning of the EU (the freedom of establishment principle) allows entrepreneurs to set up a company in any EU country. Although this topic can be analysed in many different ways, this chapter focuses mainly on principles of:

- Internal European Market;
- Free movement of goods, capital, persons and services;
- Single European currency (Euro);
- EU external trade policy;
- Starting up a business in any EU country.

Guide to the chapter

The contents of each chapter are shown on a mind-map:

Key words:
Internal European Market; Euro; EU Trade policy; starting up a business; free movement of goods, capital, people and services.
5.1 **Internal European Market**

The internal European Market is a single market where European citizens are free to live, work, study and do business. The role of the Internal European Market was proposed in 1992 to protect the business of each citizen of EU member states. It should guarantee the EU's four freedoms - the free movement of goods, capital, services, and persons — within the EU's 27 member states.

Another important step in the integration process was the creation of the **Schengen Area**, which abolished physical barriers across the internal market by incorporation within the competences of the EU. It also helped the transfer of goods and people between most member states; it introduced common rules on visas and police and judicial cooperation.

### 5.1.1 Free movement of goods

The free movement of goods was established and first introduced in principle by the customs union among the six original member states. It ensures the elimination of tariff barriers (e.g. customs duties and equivalent restrictions, the physical and technical differences between products and goods in each EU country). In case there arise any complications connected with the incorrect application of legislation, there is a European network centre SOLVIT to help consumers and entrepreneurs to solve these problems.

**Example:**

EU countries removed tariffs on trade between them; they also unified their tariffs on goods imported from outside. This means, for example, that products are subject to the same tariff whether they enter the EU via the ports of Genoa or Hamburg. As a result, a car from Japan, on which import duty is paid on arrival in Germany, can be shipped to Belgium or Poland and sold there in the same way as a German car. No further duty is charged.

### 5.1.2 Free movement of capital

Capital within the EU may be transferred in any amount from one country to another. The free movement of capital includes free movement of payments for imported and exported goods or money transfers of migrating workers. Also included are all direct investments abroad, investments into real estate properties, loans and credits or operations on the financial markets. All intra-EU transfers in euros are considered as domestic payments and bear the corresponding domestic transfer costs.
5.1.3 Free movement of services
Services account for more than 70% of the economic activity of the EU Member States, and a similar proportion of employment. The free movement of services means that a provider of a service (sole entrepreneur, trader, company) can carry on its activity in any other member state according to the same conditions valid for subjects in this state. It is important and mainly used for cross-border services.

5.1.4 Free movement of people
The free movement of people means that EU citizens can move freely between member states to live, work, study or retire in another country. In connection with EU enlargement in 2004, original member states could apply temporary measures – a seven-year moratorium on full integration for new members to protect their labour market. Some of them (like Austria and Germany) opened their labour market at the latest possible time, in 2011. Since 2011, workers have the right to move to any other Member State, to apply for any work and be employed under the same conditions as nationals of that State.

5.1.5 European Company
A European company has its own legislative framework according to the EU law. It is known under its Latin name Societas Europaea (abbreviation SE). This allow companies incorporated in different Member States to merge or form a holding company or joint subsidiary, while avoiding the legal and practical constraints arising from the existence of 27 different legal systems. It should also help to arrange an involvement of employees in the European company and recognize their place and role in the company. For more information see http://actrav.itcilo.org/actrav-english/telelearn/global/ilo/law/eucomp.htm.

5.2 EU External trade policy
The European Union is the world’s biggest trader, accounting for 20% of global imports and exports. Free trade among its members was started by the signing of the Rome Treaty fifty years ago. The main reasons for liberalising world trade in the EU are the benefits of rich and poor countries and the protection of EU producers and consumers. The EU trade policy includes many different tools of liberalisation of the market, such as duty-free or cut-rate access to its market for most of the imports from developing countries under its generalised system of preferences (GSP). For more information see http://europa.eu/pol/comm/index_en.htm.
The Internal Market is intended to be conducive to increased competition, increased specialisation, and larger economies of scale. It allows goods and production plants to move to the area where they are most valued, thus improving the efficiency of the allocation of resources. It is also intended to drive economic integration whereby the once separate economies of the member states become integrated within a single EU-wide economy.

5.3 Single European Currency (Euro)
The Euro is a single currency used currently in 17 EU member states. To use the euro makes business much easier in many respects. There is no need to work in different currencies, which decreases costs and risks connected with fluctuations in exchange rates. Other arguments in favour of the euro are better borrowing, better planning, more investment, better transparency of prices, and so on. On the other hand, if any member state of the monetary union has financial problems it is dangerous for the balance of the whole monetary union.

For more information see: www.eubusiness.com/topics/euro/business

5.4 Start up a business in the EU
The transnational development of businesses is a key component of the completion of a European single market. There are big differences among EU countries in the procedures for starting up a business. In many countries reforms of the last few years have improved conditions for starting a business with respect to time, costs, procedure and minimal capital requirement.

For example, reforms in Portugal in 2006 resulted in a reduction of time taken to start a business from 54 day to 5 days. In 2007 and 2008 new business registrations went up 60% compared with 2006. In ranking of the comparative ease of doing business based on 9 indicators for the period between June 2009 and June 2010, the Czech Republic came in 63rd position, behind most of EU countries. (2011 The International Bank for Reconstruction and Development / The World Bank). For more information see http://www.doingbusiness.org/~/media/FPDKM/Doing%20Business/Documents/Profile/Regional/DB2011/DB11-European-Union.pdf

5.4.1 Point of single contact
The aim of Points of single contact is primarily to make it simpler for entrepreneurs to start their business activities. It is for both Czech entrepreneurs who intend to provide their services in other member states of the European Union, and service providers from other member states who wish to expand their business in the Czech Republic.
The points are intermediary between the entrepreneur and the respective administrative bodies.

**Best practices**
The Czech Republic was recognized as the first and in fact the only country in the European Union to offer a unified advisory system for business in the home country and abroad. It includes Points of single contact, ProCoP (Product Contact Point) and SOLVIT, which until 2010 worked separately. Despite the fact that they have been working for only a short period, they have already helped more than 3000 clients a year. ProCoP helps producers that want to bring a new product to market with legislative requirements.

As mentioned above, the process of establishing a company differs significantly among EU member states. For example, the procedure for the most common legal form (not only in the Czech Republic) – limited liability company - differs in the number of steps necessary to establish the company, the minimum capital requirement, the costs of establishment and the length of the process, as shown in the table. The conditions for establishing ltd companies seem to be quite easy in Estonia, where the whole process takes 6 days and the minimum capital requirement and costs connected with establishment are low.

**Table 10 – Establishment of Limited Liability Company (Ltd.) in EU Countries**

<table>
<thead>
<tr>
<th>Country</th>
<th>Minimum of Capital (EUR)</th>
<th>Number of Steps</th>
<th>Length of the process in days</th>
<th>Costs (EUR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>6.200</td>
<td>3</td>
<td>4</td>
<td>1.400</td>
</tr>
<tr>
<td>Bulgaria a)</td>
<td>2.556</td>
<td>9</td>
<td>28</td>
<td>195</td>
</tr>
<tr>
<td>Denmark a)</td>
<td>16.760</td>
<td>4</td>
<td>6</td>
<td>0</td>
</tr>
<tr>
<td>Estonia a)</td>
<td>2.556</td>
<td>6</td>
<td>6</td>
<td>192</td>
</tr>
<tr>
<td>Finland</td>
<td>2.500</td>
<td>3</td>
<td>14</td>
<td>330</td>
</tr>
<tr>
<td>France – b)</td>
<td>–</td>
<td>5</td>
<td>7</td>
<td>310</td>
</tr>
<tr>
<td>Ireland – b)</td>
<td>–</td>
<td>4</td>
<td>8</td>
<td>100</td>
</tr>
<tr>
<td>Italy c)</td>
<td>10.000</td>
<td>9</td>
<td>13</td>
<td>4.690</td>
</tr>
<tr>
<td>Cyprus – b)</td>
<td>–</td>
<td>3</td>
<td>approx. 2 weeks</td>
<td>620</td>
</tr>
<tr>
<td>Lithuania a)</td>
<td>2.896</td>
<td>7</td>
<td>26</td>
<td>190</td>
</tr>
<tr>
<td>Latvia a)</td>
<td>2.845</td>
<td>5</td>
<td>16</td>
<td>195</td>
</tr>
<tr>
<td>Luxemburg c)</td>
<td>12.400</td>
<td>7</td>
<td></td>
<td>628</td>
</tr>
<tr>
<td>Hungary a)</td>
<td>2.108</td>
<td>6</td>
<td>20</td>
<td>1.850</td>
</tr>
<tr>
<td>Malta c)</td>
<td>1.165</td>
<td>5</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>25.000</td>
<td>9</td>
<td>16</td>
<td>250</td>
</tr>
<tr>
<td>Netherland</td>
<td>18.000</td>
<td>6</td>
<td>10</td>
<td>2.052</td>
</tr>
<tr>
<td>Poland a)</td>
<td>14.956</td>
<td>10</td>
<td>31</td>
<td>910</td>
</tr>
<tr>
<td>Portugal</td>
<td>5.000</td>
<td>7</td>
<td>5</td>
<td>530</td>
</tr>
<tr>
<td>Country</td>
<td>Capital (EUR)</td>
<td>Time to Register</td>
<td>Start-up Cost (EUR)</td>
<td></td>
</tr>
<tr>
<td>-----------------</td>
<td>---------------</td>
<td>------------------</td>
<td>---------------------</td>
<td></td>
</tr>
<tr>
<td>Austria</td>
<td>35,000</td>
<td>8</td>
<td>30</td>
<td>1,300</td>
</tr>
<tr>
<td>Romania a)</td>
<td>56,5</td>
<td>6</td>
<td>14</td>
<td>124</td>
</tr>
<tr>
<td>Greece</td>
<td>18,000</td>
<td>15</td>
<td>38</td>
<td>2,220</td>
</tr>
<tr>
<td>Slovakia a)</td>
<td>6,594</td>
<td>9</td>
<td>25</td>
<td>385</td>
</tr>
<tr>
<td>Slovenia</td>
<td>25,000</td>
<td>9</td>
<td>58</td>
<td>800</td>
</tr>
<tr>
<td>Spain</td>
<td>3,005</td>
<td>10</td>
<td>40</td>
<td>1,081</td>
</tr>
<tr>
<td>Sweden a)</td>
<td>10,690</td>
<td>3</td>
<td>15</td>
<td>213</td>
</tr>
<tr>
<td>Great Britain a) b)</td>
<td>6</td>
<td>12</td>
<td>216</td>
<td></td>
</tr>
<tr>
<td>Czech Republic a)</td>
<td>6,715</td>
<td>10</td>
<td>20</td>
<td>1,080</td>
</tr>
</tbody>
</table>


Notes:

a) For countries, which have not been Euro zone members, was used a conversion of national currencies to Euro based on the exchange at [http://www.xe.com](http://www.xe.com) to 15.8.2008.
b) Minimum of capital is not set, in case of Cyprus is a common basic capital je at least 1,000 EUR.
c) These countries (Cyprus, Luxemburg, Malta) were not included in a synthetic study of the World Bank – data are received from a different methodology.

**Summary**

Entrepreneurs and businesses in the EU have to respect legislation, both on the EU and the national level, which helps and protects both customers and suppliers. To make business between member states easier, the EU applies the system of a single European market based on four economic freedoms. Most of the EU members also participate in the Schengen area and in connection with non-EU states there are rules set by the internal European market policy. Starting up a business in any EU country is a process based on national legislation which differs a lot across the EU. Nevertheless, no matter how difficult or expensive starting up a business is, the tendency in the EU is to make the process easier and also to support and advise entrepreneurs, e.g. through the SOLVIT organisation.
Resources


OPRAVIT ZÁPIS!!!!!!!!!!!!!!!!!!!!

http://www.mpo.cz/dokument83159.html

Zákon 586/1992 Sb., o dani z příjmů ve znění pozdějších předpisů.
Zákon 588/1992 Sb., o dani z přidané hodnoty ve znění pozdějších předpisů.
Zákon č. 100/1988 Sb., o sociálním zabezpečení ve znění pozdějších předpisů.
Zákon č. 155/1995 Sb., o duchovění pojištění ve znění pozdějších předpisů.
Zákon č. 187/2006 Sb., o nemocenském pojištění ve znění pozdějších předpisů.
Zákon č. 592/1992 Sb., o pojistném na všeobecné zdravotní pojištění ve znění pozdějších předpisů.