



Legal update

June 2023

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Obsah

New legislation

Amendment to the Act on Conversions of Business Corporations and Cooperatives

Case Law

Legal consequences of the actions of a representative whose interests are in conflict with the interests of the represented party

The information contained in this bulletin is presented to the best of our knowledge and belief at the time of going to press. However, specific information related to the topics listed in this bulletin should be consulted before any decisions are made.

Banking, Finance & Insurance:

Daniel Weinhold, Václav Štraser, Ondřej Tejnský

Competition Law / EU Law:

Tomáš Čermák

Dispute Resolution:

Milan Polák, Zbyšek Kordač, Anna Bartůňková, Michaela Koblasová, Michal Švec

ESG – Environment, Social, (corporate) Governance

Daniel Weinhold, Tereza Hošková

Family Office:

Milan Polák, Zbyšek Kordač, Michaela Koblasová

Insolvency and Restructuring:

Zbyšek Kordač, Jakub Nedoma

IT, Media & Telecommunication:

Martin Lukáš, Jakub Nedoma, Michal Przczek

Labour Law:

Eva Procházková, Anna Bartůňková, Daša Aradská, Ondřej Tejnský

Mergers and Acquisitions:

Daniel Weinhold, Václav Štraser

Personal Data Protection

Martin Lukáš, Tereza Hošková, Daša Aradská

Public Procurement & Public Sector:

Martin Lukáš, Tereza Hošková, Monika Švaiřčková

Real Estate:

Pav Younis, Václav Štraser

Slovak Law:

Tomáš Čermák, Karin Konečná

Start-ups, Venture Capital and Cryptocurrency:

Pav Younis, Martin Lukáš, Jakub Nedoma, Michal Švec, Ondřej Tejnský

New legislation

Amendment to the Act on Conversions of Commercial Companies and Cooperatives

On 31 May 2023, the Government of the Czech Republic submitted to the Chamber of Deputies a bill amending Act No. 125/2008 Coll., on Transformations of Commercial Companies and Cooperatives, as amended, and other related acts (the "Amendment").

According to the Explanatory Memorandum, the primary objective of the Amendment is to transpose Directive (EU) 2019/2121 of the European Parliament and of the Council of 27 November 2019 amending Directive (EU) 2017/1132 as regards cross-border seat transfers, mergers and divisions (the "Directive"). In doing so, the Directive not only harmonises the rules for cross-border mergers, but also introduces EU regulation of cross-border divisions and cross-border seat transfers.

The amendment will bring changes in the following areas, among others:

Division of the company by spin-off

A new form of division of a company will be introduced in Czech law. Companies will thus be able to be divided not only by splitting up and spinning off, but also by demerger, in which the demerged part of the assets will be transferred in exchange for a share or shares either to one or more newly emerging companies (so-called demerger with the creation of a new company or companies) or to one or more existing companies (so-called demerger by merger). The amended law also provides for a combination of these forms and the company being divided will not be dissolved by the spin-off.

Creditor's rights and their regulation

The current wording of the Act provides that creditors of the persons participating in the conversion who register their outstanding claims within 6 months from the effective date of the registration of the conversion in the commercial registers against third parties may request the provision of sufficient security in the event of deterioration in the recoverability of their claims. The amendment reduces the time limit to 3 months. Moreover, the time limit will not run from the effective date of registration of the conversion in the Commercial Register against third parties, as under the current legislation, but will start running from the date of publication of the conversion project in the Collection of Deeds. In this context, the definition of claims whose security may be claimed by creditors has also changed. Currently, protection is limited only to outstanding claims that arose before the registration of the conversion in the Commercial Register. However, after the Amendment becomes effective, the Act will explicitly mention that it may also cover future or contingent claims arising from obligations incurred before the publication or disclosure of the conversion project.

Changes to the information obligation

Currently, the persons involved in the conversion, who are registered in the Commercial Register, are obliged to publish a notice of the deposit of the conversion project in the collection of documents and a notice to creditors of their rights at least 1 month before the date of approval of the conversion by the supreme body of the company. After the Amendment comes into force, publication of the specified documents will not be required. Thus, the persons involved in the conversion will only be obliged to deposit the conversion project and the notice in the collection of documents. However, the notice will no longer apply only to creditors, but also to representatives of employees, employees, partners or members of the company.



Legal update

June 2023

Weinhold Legal

New ground for refusal of cross-border conversion certificate

The amendment will expand the list of grounds for refusal by a notary to issue a certificate for a cross-border conversion. Failure to submit the prescribed or other documents required by the notary will thus be supplemented by the notary's finding that the cross-border conversions have an abusive or fraudulent purpose aimed at avoiding or circumventing national or EU regulations or at committing criminal activities

Waiver of appointment of an expert

Compared to the current legislation, the amendment also for the purposes of conversions of companies and cooperatives, the appointment of an expert by the court shall be waived.

Instead of being appointed by the court, the expert will now be selected by the person involved in the conversion from the list of experts.

Approval of the conversion of a joint stock company and a cooperative per rollam

Under the current legislation, per rollam voting on the approval of the conversion is expressly possible only in the case of a limited liability company. However, the amendment also introduces the explicit possibility of approving the conversion of a joint stock company and a cooperative per rollam, i.e. outside the general meeting, i.e. outside the members' meeting.

Demerger of listed companies with a majority shareholder

Significant changes discussed by the professional public will also affect the division of a listed company, i.e. a company whose shares are admitted to trading on a European regulated market. If a company has a majority shareholder, it will be possible to approve a demerger with an unequal share exchange ratio or a demerger by way of a spin-off with the termination of the participation of all other shareholders with the approval of at least 75 % of the votes of the shareholders present at the general meeting. In this case, a quorum will be present if shareholders holding shares with a value exceeding two-thirds of the share capital of the company are present.

At present, a defined distribution is governed by the general rules governing the distribution of a public limited company with an unequal exchange ratio and must therefore be approved by at least 90 % of the votes of all shareholders

Effectiveness of the Amendment

Since the Czech Republic has been in delay in fulfilling its obligation to transpose the Directive into its legal system since the expiry of the transposition deadline of 31 January 2022, the entry into force of the Amendment should occur relatively quickly, on the 30th day after its promulgation.

Case law

Legal consequences of unauthorised conduct by a representative whose interests conflict with those of the represented party

(Judgment of the Supreme Court of the Czech Republic Case No. 31 Cdo 1640/2022 of 5 October 2022)

The Grand Chamber of the Civil and Commercial Chamber of the Supreme Court, in its judgment of last October, dealt with the legal consequences of the actions of a representative whose interests conflict with those of the represented party.

The Supreme Court, in dealing with the defined consequences, came to the following conclusions:

Consequences of an unapproved representative acting in a conflict of interest with a person who is not acting in good faith

In the context of the possible consequences of unauthorized conduct in conflict of interest with a person who is not in good faith, the Supreme Court has addressed the absolute invalidity of the legal representative's conduct and the relative invalidity of the conduct as well as the unbinding nature of the represented person's conduct.

The Supreme Court expressly excluded absolute nullity as a consequence of the legal representative's actions in conflict of interest. It supported its exclusion by arguing that an interpretation according to which a legal act performed by a legal representative acting in a conflict of interest is absolutely invalid or even apparent contradicts not only the wording of Section 437(2) of Act No. 89/2012 Coll., the Civil Code (hereinafter "the Civil Code"), which provides that the represented party may invoke such an act, but also its meaning and purpose. As a consequence of the absolute invalidity of the representative's actions, the represented party would not be able to obtain to be bound by the representative's actions, even if such actions are beneficial for the represented party.

The Supreme Court also found incorrect the view of the majority of the doctrine according to which the consequence of violation of the prohibition of representation in a conflict of interest is the relative invalidity of the legal action taken by the representative. The Supreme Court states that this interpretation, without any reasonable justification, associates different legal consequences with the lack or excess of the representative's authority than that of other legal facts. Furthermore, according to the Supreme Court, that interpretation results in weaker protection than that which would be appropriate to the fairness of the relationship between the representative, the represented person and the third party who knew or should have known of the lack of the representative's authority. Despite the fact that such a third party is not acting in good faith, it is left to the activity of the represented party, in the application of the defined legal interpretation, to discharge the obligations arising from the legal act of the unauthorised representative by raising the plea of relative nullity. Thus, the represented party must act actively despite the fact that it is he who is protected by the law in the relationship between him, the representative and the third party.

In this context, the Supreme Court acknowledges that the language of the first sentence of Section 437(2) of the Civil Code, by referring to the "plea" of the represented party, suggests that the represented party must take active steps to ensure that the representative's actions in an unlawful conflict of interest do not bind him or her. However, the Supreme Court also points out that the language interpretation is only an initial approach to the legal norm. On the contrary, a systematic interpretation suggests that the represented party is not bound by the representative's conduct in an illicit conflict of interest with a person who was not acting in good faith. In fact, the represented party invokes the lack of the representative's authority against the third party by not subsequently approving the legal action taken by the unauthorised representative, thereby indicating to the third party that he does not wish to be bound by the action in question.

The argument that the consequence of the unapproved conduct of an agent whose interests conflict with a person who is not acting in good faith is not the invalidity of such conduct, but that such conduct does not bind the principal. The Supreme Court also reinforces the application of theological interpretation, which leads to the same conclusion as systematic interpretation. In the absence of good faith on the part of the third party that the agent was authorized to act for the represented party, the represented party is the only one to be protected in the given situation. In the Supreme Court's view, in such a situation, it is consistent



Legal update

June 2023

Weinhold Legal

with a fair arrangement of relations that the represented party should be able to remain passive, even though he does not want to be bound by the representative's conduct and should not be forced to take any active steps to extricate himself from the legal action taken.

Consequences of an unapproved representative acting in a conflict of interest with a person in good faith

The Grand Chamber of the Supreme Court also concluded in its judgment that, notwithstanding the above, the represented party is bound by the actions of a representative whose interests are in conflict with the interests of the represented party if the representative acts with a third party who has a good faith belief that the representative has the representative's authority and, therefore, there is no conflict between the representative's interests and the interests of the represented party, or the existing conflict does not limit the representative's authority.

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