

Legal Update

February 2017

Weinhold Legal

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The information in this newsletter is correct to the best of our knowledge and belief at the time of going to press. Specific advice should be sought, however, before investment or other decisions are made.

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Bills under discussion

Proposal of new Payment Systems Act

On 6 January 2017, the Ministry of Finance submitted to the Government a bill proposing a new Payment Systems Act and a bill amending some laws in connection with the adoption of the Payment Systems Act.

The reason for this proposal is to transpose Directive 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market. The new law aims to make it easier for consumers to understand offers from individual banks and to improve and strengthen the consumer's position. Given the extent of the changes, it is proposed that a new law be adopted to replace existing Act No. 284/2009 Coll. on payment systems rather than merely amending it. It is also proposed that an accompanying law be adopted to implement corresponding changes in other acts, e.g. the Act on Banks and Anti-Money Laundering Act. In compliance with the Payment Services Directive, the new law expands the category of persons authorized to render payment services to include holders of postal licenses and introduces a number of other changes.

The bill introduces what is known as strong user authentication, which will be required when a user enters a payment transaction online or via other electronic means. Strong authentication is authentication involving the use of at least 2 of the following authentication methods: entering details of known users, e.g. login details, using an item under the user's control, e.g. a mobile phone, or biometric data of the user, e.g. fingerprint. This also means a reduction in the user liability limit to EUR 50 (formerly EUR 150) in the event of unauthorized transactions using a lost, stolen or misused card.

The bill also introduces a prohibition on payment system operators or users blocking legal persons that render payment services from accessing a payment system by tying these persons' access to requirements that are discriminatory or unreasonable or restricting their payment system access to a greater degree than is necessary to hedge specific risks and protect the financial and operational stability of the payment system. This also enables the emergence of alternative payment services schemes or a new group of payment service providers - so-called payment account information administrators. Their activity will comprise the provision of services involving the disclosure of information on payment accounts by a provider other than the provider operating the given payment account. This will make it possible to run applications allowing the retrieval of information about several accounts at once. In this way, the bill aims, among other things, to facilitate family financial planning.

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Another of the new services is the indirect taxation of a payment order. The essence of the service is that the taxpayer does not submit the payment order to the provider operating its payment account directly, but via what's known as a third-party provider. In contrast to standard bank transfers, the recipient gets information about whether there are sufficient funds on account at the moment the payment order is submitted, as a result of which the recipient can expedite the goods or provide the service at this same moment, which should speed up commercial transactions. It provides an alternative to online card transactions.

Other new features include the possibility of payment cards tied to a zero balance payment account. Users make purchases with these cards and the funds are provided as a loan. The card issuer has the option of finding out from the provider maintaining the payment account for the same user whether or not the balance on the user's payment account covers payment card transactions. The card issuer then deducts the amount from the user's account maintained by the other provider.

Recent case law

Exercise of due diligence when deciding on an investment plan

(Czech Supreme Court Judgment No. 29 Cdo 5036/2015 of 26 October 2016)

In this judgment, the Supreme Court dealt with the case of a company, as an applicant for appellate review, which stated, among other assertions, that the amount of money spent by the executive on an investment was disproportionately high "given the company's financial position" if the circumstances indicated no expectation of a return on the investment. The Supreme Court ruled that the outcome of decisions adopted by an executive in the performance of his role are immaterial to a determination of whether the decisions comply with the due diligence requirement (despite the potential negative consequences for the company). Even if the executive's activity failed to yield the expected results, it could not be deduced from this that the executive had failed to act in accordance with the law. Only if it is first determined the executive of a limited liability company failed to make every effort commensurate with the exercise of due diligence, can we then consider whether that executive is obliged to compensate the company for damage incurred as a consequence of such conduct.

To meet the requirement of due diligence, an executive is obliged to act with the requisite knowledge when performing his role, i.e. in an informed manner, and when making particular decisions must use all reasonably available (factual and legal) information sources and, on their basis,

carefully weigh the potential benefits and disadvantages of all business decision alternatives. Fulfilment of this obligation must, of course, be assessed from the perspective of the facts of which the executive was or could and should have been aware while exercising due diligence (while availing himself of available sources of information) at the moment the respective business decision was made. In other words, an executive's decision cannot be assessed based on facts that first arose or came to light after the business decision under review was made, e.g. the subsequent outbreak of an economic crisis.

Damage incurred by breach of a pre-contractual obligation

(Czech Supreme Court Judgment No. 25 Cdo 337/2015 of 26 October 2016)

In the above case, the Supreme Court dealt with a situation in which the defendant had undertaken actions intended to lead to the execution of a contract of donation for a house, and entered into a contract with the applicants based on which they could begin renovation of the house. The defendant then changed its mind about gifting the house and drew up a will bequeathing the house to the applicants, though the will was later voided. This ended the negotiations over the execution of the contract of donation and the defendant also changed its position with respect to the transfer without consideration and the bequeathal, despite knowing that the applicants, with the defendant's agreement and in good faith in the future gifting or bequeathal, had incurred expense to renovate the house.

The law stipulates that every individual is liable for damage caused by breach of a legal obligation and is obliged to act so as to avoid damage to health, property, nature and the environment. The previous sentence refers to a general duty of prevention applying to all participants in civil relationships. This is a binding legal duty of all to adhere not only to obligations imposed by law and contractually assumed obligations, but also to act with sufficient prudence so as not by action or omission to cause damage to oneself or others.

The actions of one contracting party in the contract execution process may be considered a breach of the duty of prevention. While respecting the principles of freedom of contract and the equal status of participants, the conduct of one of the potential contractual partners may be designated as illegal if contract negotiations reach a stage where one of the parties was under the impression the contract would be executed as a result of the conduct of the other party acting in good faith, and the second party halted contract negotiations without having a legitimate reason despite knowing the other contractual partner incurred expenses in connection with the assumed con-

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tract execution. Breach of the duty of prevention shall entail liability for damage that demonstrably arises as a direct result of a breach of legal obligation.

In such cases, damage is most likely to comprise costs incurred in connection with pre-contractual negotiations or the preparation of conditions for contract execution (costs of legal representation, expert opinions, administrative and other fees, loan collateral etc.) or expenditure associated with the contract subject-matter. To whom such amounts were paid (whether they were obtained by a potential contractual party or a third party) is immaterial, from the perspective of the definition of actual damage, what is decisive is whether the unnecessary expenditure reduced the injured party's finances. Expenses of this nature may include costs of modifying a thing that is to be subject to transfer, where the assumed future owner performed the alteration in agreement with the present owner, as happened in the case under review here.

It can thus be deduced that the impact of the general duty of prevention is broader and pertains to the case at hand in which the execution of an offered donation contract was not set out in an agreement on a future contract, though given the circumstances of the case, the manner of conduct of the participants and the justified expectation that the other party would keep its word, the applicants could, as potential parties to the contract, have reasonably expected the contract would be executed and conducted themselves in accordance with this expectation.

Assessment of a pactum commissorium arrangement

(Czech Constitutional Court Finding No. II. ÚS 3646/13 of 3 January 2017)

The Constitutional Court here dealt with alleged circumvention of the prohibition against the establishment of a pactum commissorium (the automatic appropriation by the creditor of property pledged or mortgaged upon the failure of the debtor to pay the principal obligation) set out in § 169(e) of Act No. 40/1964 Coll., the Civil Code (the "CC"). The Constitutional Court, while stressing the importance of the existence of the prohibition against a pactum commissorium in the context of the protection of the right to own property, also holds that this prohibition cannot be applied indiscriminately such that on its basis judicial power can (must) declare the nullity of every legal act that in any way elicits an impression (even one that is misleading) of circumventing this prohibition.

Although judicial power is generally called on to protect the rights of owners that would be significantly infringed by the application of a pactum commissorium, this does not relieve the general courts of the duty to consider the purpose of the prohibition on a case-by-case basis; thus, when providing protection of property rights pursuant

to Art. 11(1) of the Charter, which would be adversely impacted by a violation of the prohibition against a pactum commissorium, they must at the same time bear in mind the principle of autonomy of the will of private law entities (and business entities, in particular) and give it precedence - where the circumstances of the case allow - over an interpretation that leads to a finding of the nullity of the given legal act.

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We hope you will find *Legal Update* to be a useful source of information. We are always interested in your opinion about our newsletter and any comments you may have regarding its content, format and frequency.

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