Legal Update

March 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 and other decisions are made.

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Bills under discussion

Insolvency Act Amendment

On 3 March 2017, a bill amending Act No. 182/2006 Coll. on bankruptcy and settlement (the Insolvency Act) was promulgated under number 64/2017 Coll. in Section 21 of the Collection of Laws.

Under the amendment, the insolvency administrator or registered associate of the insolvency administrator are obliged to perform their work at their registered address on specific days and during certain hours. Their work will be subject to stronger oversight by the Ministry, which will have the authority to revoke the license or special license of an insolvency administrator who has committed a gross or repeated breach of an obligation stipulated by this law, a control authority or the Insolvency Act.

The amendment introduces the obligation of the insolvency petitioner, when filing an insolvency petition against a commercial corporation, to remit a CZK 50,000 advance payment for insolvency proceeding costs, and a CZK 10,000 advance when filing a petition against a non-commercial corporation or natural person. This shall not apply if the insolvency petitioner is an employee of the debtor whose receivable consists of claims under labour law or a consumer whose receivable consists of a claim arising out of a consumer contract.

The Ministry is also publishing new forms for statutory filings, which enable remote access. An insolvency administrator will be obliged to electronically submit a final report, the particulars and format of which will be set out in an implementing regulation.

Where a creditor and debtor together form a holding or is a person close to the debtor, the creditor may not vote at a creditors' meeting.

The amendment also introduces stronger protections against vexatious insolvency petitions, specifically by means of the preliminary assessment of an insolvency petition submitted by a creditor. Should an insolvency court conclude that uncertainty exists in an insolvency petition filed against a debtor as to the abuse of the rights of the insolvency petitioner to the detriment of another competing entity in the position of debtor or as to another shortcoming in the insolvency petition, which is grounds for rejecting the insolvency petition filed by the creditor for clear frivolousness, it will be authorized to decide that neither this insolvency petition nor the other documents in the file, including the declaration providing notification of the commencement of insolvency proceedings, are to be published in the insolvency register. Moreover, at this stage of an insolvency proceeding, only the insolvency petitioner and the debtor will be able to view the contents of the file and make extracts and copies from it, as a result of which the group of persons with knowledge of the fact that an insolvency proceeding has been initiated will be narrowed to a minimum. This will eliminate any de facto "scaremongering" concerning the fact that a given competing entity is insolvent.

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The court can impose a fine of up to CZK 500,000 (as compared to the current limit of CZK 50,000) for cases of the rejection of an insolvency petition for clear frivolousness.

If an insolvency petition was rejected for clear frivolousness, the same petitioner may re-file no earlier than 6 months after the effective date of the rejection decision (except in cases of rejection for non-payment of the advance for insolvency proceeding costs).

The amendment comes into force on 1 June 2017.

Bill amending the Advocacy Act

On 7 February 2017, the Ministry of Justice submitted a bill amending Act No. 85/1996 Coll. on advocacy, as amended, to the Government.

The objective of the proposed amendment is to supplement and expand state-guaranteed legal aid. What is specifically proposed is a new treatment of the entitlement to legal advice and legal services.

The entitlement to legal advice will pertain to an applicant

- whose average monthly income for the 6-month calendar period preceding the application filing does not exceed three times the subsistence level;
- who does not have assets that would otherwise enable him to secure legal services;
- who is not represented by another representative in the case for which he is seeking the provision of legal advice.

Legal advice will be provided for individual periods of no less than 30 minutes up to a total of two hours for every calendar year.

The entitlement to legal services (representation) will pertain to an applicant:

- whose income and assets justify it; and
- who is not represented by another representative in the case for which he is seeking the provision of legal services.

In any given case, however, an attorney may only be appointed to an applicant once by the Bar Association.

An application will be submitted on a form provided by the Ministry of Justice. An attorney will only be entitled to reimbursement for loss of time and travel expenses in warranted cases. If the government is to pay the attorney a fee, the attorney is obliged to send the Bar Association an invoice within one month of service provision.

The proposed effective date is 1 July 2018.

Bill amending the Civil Procedure Code

On 17 February 2017, the Government submitted a bill amending Act No. 99/1963 Coll., the Civil Procedure Code, as amended, and some other laws to the Chamber of Deputies as Parliamentary Bulletin No. 1034.

The purpose of the bill is to ensure employee protection in situations where, based on credible facts, a criminal complaint is brought to a law enforcement authority and employees are hindered or disadvantaged in their work in connection with this notification. The protection comprises the shifting of the burden of proof to the employer, who is obliged to prove that the employee was in no way hindered or placed at a disadvantage as a result of the criminal complaint.

The proposed effective date is 1 January 2018.

Trades Licensing Act amendment

On 31 January 2017, the Government submitted a bill amending Act No. 455/1991 Coll. on trade licenses (The Trades Licensing Act), as amended, to the Chamber of Deputies as Parliamentary Bulletin No. 1014.

Now, an entrepreneur whose trade license was revoked pursuant to § 58(2) or (3) of the Trades Licensing Act (for a gross violation of conditions set out in a concession award decision, the Trades Licensing Act or special legislation, violation of the residency permit requirement for a foreign individual, payment arrears to the Social Security Administration), should not be excluded from carrying out a trade in a related field. The bill also proposes that the treatment of the length of time for which the carrying on of a trade may be banned be standardized at 3 years for all categories of persons to whom the ban on carrying out a trade set out in § 8(6) of the Trades Licensing Act pertains. The entrepreneur obligation to report identifying information for members of the statutory body of a corporate body and supervisors in a branch plant of a foreign person to the Trades Licensing Office has been removed.

The bill also caters to the requirements of the entrepreneur and non-entrepreneur public and introduces the issue of bulk files with publicly available current information about entrepreneurs based on a request from a member of the public. The file will always contain the identifying information of the entrepreneur as well as requested data that may include the subject of enterprise or location of an establishment. The applicant may only use the data provided in the file for his or her own needs (e.g. finding contact information for an entrepreneur for the purpose of entering into a business transaction) and shall not disclose or provide it to a third party. There should be a CZK 5 administrative fee for issuance of a file for the provision of data pertaining to one entrepreneur.

The proposed effective date is the fifteenth day after promulgation.

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Recent case law

An alternative arbitration clause with a choice between an arbitrator and general court, transparency of arbitrator selection, nominal appointment of arbitrators

(Czech Supreme Court Judgment No. 33 Cdo 1546/2016 of 23 November 2016)

In this judgment, the Supreme Court deals with a situation in which the court of first instance cancelled an arbitration award and rejected the applicants' petition to suspend the enforceability of the arbitration award. The reason for the cancellation was the arbitration contract, which appointed four arbitrators (individuals), each of whom was authorized independently to decide on a "dispute" of the parties; the sequence of the arbitrators was also determined. The arbitrators on whom the parties agreed were identified by name; their number was constant and unchanging for the duration of the parties' legal relationship. The clause also stipulated the applicants' option to choose either a general court or an arbitration court (an asymmetrical arbitration clause).

The appellate court upheld the judgment of the court of first instance, as it reached the same conclusion that the arbitration contract was invalid as concerns the arbitrator appointment owing to conflict with the law. It concluded that if the entity that is to decide on a case is not a permanent arbitral tribunal established by law, then the arbitrator's identity should be clearly stated. The mechanism for appointing an arbitrator under the assessed arbitration contract failed to stipulate transparent rules for arbitrator selection and the contractual arrangements on arbitrator appointment fail therefore to meet the requirements of clarity and transparency.

The Supreme Court reversed both judgments and returned the case to the court of first instance. It subsequently found the arrangement whereby the party to the arbitration contract who decides to file suit may choose between an arbitrator and a general court to be valid. It considers this arbitration clause as an alternative that affords the claimant the choice of initiating a proceeding before an arbitration court or a general court. The appellate court had thus evaluated the matter incorrectly, if we conclude that the provision § 2(1) of the Act on Arbitration Proceedings gives rise to an obligation clearly to determine the competence of the arbitral tribunal in addition to the general court.
It also concluded that the arbitration contract in which the parties clearly agreed that a property dispute shall be decided by one of the four nominally appointed arbitrators constitutes a valid legal act, as the manner in which the arbitrator(s) is/are appointed complies with the provision of § 7(1) of Act No. 216/1994 Coll. and is thus not an arrangement having the nature of an unreasonable and abusive clause.

Arbitration clause in disputes between entrepreneurs

(Czech Supreme Court Ruling No. 23 Cdo 1098/2016 of 8 November 2016)

In contrast to the foregoing judgment, here the Supreme Court opined on the invalidity of an arbitration clause. In this case, it had been agreed in a framework purchase agreement that all disputes arising based on the agreement should be resolved in an arbitration proceeding before a sole arbitrator. Arbitrator selection in any given dispute would be left to the petitioner.

The court of first instance concluded that the agreed arbitration clause was imprecise and thus invalid in compliance with the Civil Code in effect until 31 December 2013.

The appellate court upheld the decision of the court of first instance and concluded that only an arbitrator selection on which both parties to a proceeding agree may be considered an acceptable manner of arbitrator appointment. Thus, the selection of an arbitrator cannot be left solely to one party to a proceeding, as such an approach would give rise to an imbalance in the rights and obligations ensuing directly from the arbitration clause. Nothing alters this conclusion, not even the fact that the parties freely signed the framework purchase agreement that included the arbitration clause and thus expressed unreserved agreement with its content.

In its ruling, the Supreme Court first cited a Constitutional Court ruling dated 1 November 2011, case no. II. ÚS 2164/10, and found that its conclusions pertaining to the limits of contractual autonomy may also be applied to an arbitration proceeding in which neither party is a consumer. An arbitration contract, even one to which a consumer is not party, is invalid if the manner in which the arbitrator is appointed has been agreed such that the selection is left to the discretion of one of the parties.

The manner in which arbitrators are appointed or designated should always comply with the principle of equality of the parties, as an underlying procedural principle of legal and arbitrations proceedings. From this perspective, it is undesirable that arbitrators be chosen entirely or in large part by one party. The same rule shall also apply where a sole arbitrator is appointed. As regards the facts of this case in which arbitrator selection was to have been left at the sole discretion of only one of the parties, such arrangement in an arbitration contract cannot be deemed valid owing to conflict with § 39 of the Civil Code for its violation of the principle of the equality of the parties in proceedings.

If the manner in which the parties agree on arbitrator appointment in an arbitration contract is invalid, then the arbitration contract is invalid.

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Petition of a former executive seeking a declaration of invalidity of a General Meeting resolution

(Czech Supreme Court Ruling No. 29 Cdo 5352/2015 of 22 November 2016)

In this decision, the Supreme Court dealt with a situation in which a former executive of an LLC sought a declaration of the invalidity of the General Meeting decision recalling him from his position.

The Supreme Court ruled that an executive has a fundamental legal interest in having any General Meeting resolution recalling him from his position declared invalid (and where he was recalled more than once, all such resolutions). If the court finds in a proceeding pursuant to § 131 of the Commercial Code that a General Meeting resolution recalling an executive is in violation of legislation or the Memorandum of Association, and for this reason pronounces such resolution to be invalid, then the respective executive shall not be recalled from his position (through recall by the contested resolution). In other words, the declaration of invalidity of a General Meeting resolution directly affects the rights and obligations of the recalled executive. This is true even where the General Meeting again recalls the executive (in another, later adopted resolution); even here, the executive has a legal interest in the General Meeting resolution being declared invalid, as its potential invalidity affects the date at which the position of executive (and the rights and obligations of the executive ensuing from performance of the role) terminate. If a General Meeting resolution recalling an executive is found by a court to be invalid, then as a rule (taking into account the number of executives agreed in the Memorandum of Association), the related resolution appointing a person to replace that executive will also be invalid.

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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