Legal Update

April 2018

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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Legislative amendments

Amendment of the Business Corporations Act

On 23 February 2018, the Ministry of Justice submitted a bill to the Government amending Act No. 90/2012 Coll. on business corporations and cooperatives (the "**BCA**") as amended by Act No. 458/2016 Coll. and certain other laws (the "**Bill**").

The Bill's presentation report states that the proposed changes to the BCA are primarily designed to eliminate legislative-technical and terminological errors and inaccuracies, reduce the regulatory burden on entrepreneurs, ensure greater transparency in the organisational structures of capital companies and cooperatives, remove shortcomings in the transposition of some provisions of EU directives and assure greater protections for the rights of company members (as well as third parties) and strengthen their legal certainty. In the view of the Ministry of Justice, the Bill should thus remove shortcomings arising in the practical application of the BCA.

Key changes proposed by this extensive Bill include the possibility of transferring business shares in general partnerships, establishing a cooperative without an establishment meeting, introducing the pre-emption right of company members in the event of the sale of their own contribution to a limited liability company, the possibility of invoking the invalidity of a resolution of the supreme body of private companies or the obligation to immediately authorize one natural person to represent a legal entity as a member of an elected body of a capital company or cooperative.

Another major change introduced by the Bill is the new treatment of the monistic system of joint-stock company corporate governance. The Czech monistic system was often criticized for its mandatory establishment of two bodies (an administrative board and statutory director) because the unclear definition of their positions and powers created practical difficulties. For this reason, the Bill abolishes the position of statutory director and establishes a (three-member) administrative board as a joint-stock company's sole statutory body. According to the Bill, this body is tasked with deciding on the primary focus of business management and with oversight of company activity.

The Bill's proposed effective date is 1 January 2020. However, given the extensive nature of the proposed changes and their current topicality in public discussion, we can expect the final version of the Bill to look quite different from the current one. It is worth mentioning that at the time of writing, the Bill was in an interdepartmental discussion procedure whose outcome had not yet been publicized.

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Recent case law

A business company's knowledge of a certain (legally material) fact

(Czech Supreme Court Judgment No. 29 Cdo 4554/2015 of 15 November 2017)

In the above decision, the Supreme Court dealt with a petition to pronounce a legal act invalid pursuant to § 42a(1) and (2) of Act No. 40/1964 Coll., the Civil Code (the "**CivCo**").

The petitioner in this case sought a ruling that a purchase agreement executed between a bankrupt, as seller, and the respondent, as buyer, was not binding for the "petitioner" due to the respondent's knowledge of the bankrupt's intention to impair the satisfaction of the petitioner. The district court and court of first appeal were both of the opinion that for the petitioner to win the dispute, it would have to show that, at the time the purchase agreement was executed, members of the Board of Directors of the respondent were aware of the debts of the bankrupt and of its intention to short-change the petitioner.

The petitioner sought an appellate review of the findings of the courts of lower instance, arguing that a company's knowledge need not be consonant with its Board of Directors' knowledge, as internal company relations such as those between a statutory body and a director or holder of procuration, give rise to the will of the company. Citing the provision of § 14 of Act No. 513/1991 Coll., the Commercial Code (the "**ComCo**"), the appellant concluded that if the company's director or holder of procuration knew about the debts, then the company, as such, will be deemed to have known about them, too.

The Supreme Court found the petition for appellate review to be well-founded and opined in the rationale of its ruling that a legal entity's knowledge of a certain fact depends not only on the knowledge of the members of the statutory body, but also of their representatives, if they represented the legal entity in the performance of the legal act in question. Where this involves persons authorized by the management of a legal entity who are entrusted with extensive decision-making powers as well as broad authorization for representation, then it is the view of the Supreme Court that knowledge of a certain legally significant fact is fundamentally attributable to the legal entity, even where these individuals did not represent it in the legal act in question, though they could have (in compliance with § 15 of the ComCo).

In the given case, the holder of procuration – who was at the same time the company director – knew of the bankrupt's debts and its intention to short-change the creditor. In the view of the Supreme Court, then, this knowledge could be attributed to the sued company. The Supreme Court therefore vacated the decision and returned the case to the appeals court for further proceedings.

Procedural succession in the event of revocation of indirect representation

(Constitutional Court Ruling No. IV. ÚS 3359/17 of 6 March 2018)

The Constitutional Court dealt here with the issue of procedural succession. The factual elements pertained to a situation in which the complainant (represented by this firm) was assigned a receivable under an agreement in which the complainant also authorized the assignor to indirectly represent her in receivable recovery proceedings pursuant to § 530 of the Civil Code, which the assignor subsequently did via a legal action.

During the claim proceedings, the complainant revoked the assignor's contractual authorization to claim the receivable and filed a petition to join the proceedings herself pursuant to § 107a of Act No. 99/1963 Coll., the Civil Procedure Code (the "**CPC**"). However, neither the district court nor the appellate court granted the petition, as in their view the assignment of the receivable could not be taken into consideration as a result of the concentration of proceedings pursuant to § 118a(1) of the CPC. Given the unwillingness of the general courts to recognize the complainant as a party to the proceedings (the complainant eventually invoked, inter alia, a procedure pursuant to § 107[3] of the CPC), the complainant filed a constitutional complaint against the lower courts' decisions.

The Constitutional Court deemed the constitutional complaint to be well-founded and stressed that § 530 of the CivCo provides for indirect representation of a creditor in the recovery of a receivable. Hence, if the complainant was seeking the receivable in place of the assignor, then the general courts should have allowed the complainant to join the proceedings after the revocation of authorization pursuant to § 107a of the CPC. In the view of the Constitutional Court, the general courts were obligated to avoid the denial of justice and to interpret procedural legislation in the manner most accommodating to the complainant, who had repeatedly and rightly sought to join the proceedings.

Thus, due to a violation of the complainant's right to due process guaranteed by Art. 36(1) of the Charter of Fundamental Rights and Freedoms, the Constitutional Court overruled the contested general court decisions.

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