CZECH REPUBLIC DEVELOPMENTS 2005/2006

Rent Regulation and Landlord Tenant Relationships

Year 2006 brought the principal changes to landlord tenant relationships by the substantial modification of rent control (Rent Regulation Act no.107/2006 Coll amending Civil Code. no.40/1964 Coll.) and by the new rules of Civil Code concerning the termination of the lease of the residential space by landlord.

According to the mentioned legislation substantial increase of regulated rents will be achieved between years 2007 - 2010. During this period landlords are entitled to one-sided annual rise of the regulated rent by the amount stipulated in governmental decrees. Annual increase is differentiated by particular locations. The most rapid increase is expected in big cities, mainly in Prague, where it can reach app. 20 % increase annually during next 4 years. Aim is to achieve within the of period o 5 years the stabilization of price level both at the non regulated and regulated rents and to minimize the black market and illegal speculation with the flats.

Legal position of landlord was substantially improved by the 2006 amendment to the civil code (Act No. 40/1964) modifying the procedure of termination of the lease of the residential space. Until 2006 all the termination of the lease of the apartments were subject to compulsory court approval, which was necessary to obtain before the actual termination of the lease. 2006 legislation provided for the cases, where this lengthy and costly procedure could be avoided. In the cases of

- Nonpayment of the rent or services for the period of more than 3 month
- Gross and repeating violation of the rules of conduct by tenant
- Tenant having two or more flats
- Tenant not using the flat properly or at all.

In such cases landlord may terminate the lease contract without prior court approval and tenant could only claim invalidity of the termination at the regular civil proceeding within 60 days after delivery of the termination. He is entitled to claim both the material and formal failures of the termination and for the time of the proceedings and he is, however, not bound by the duty to vacant the apartment till the executable judgement is passed in the case.

Important new rule also applies in above-mentioned cases, when landlord is not obliged to provide for the tenant provisional flat anymore. Tenant could be provided by “shelter” only, which in regular court interpretation could also dormitory, hostel or any other facility providing the temporary residential services, at the costs of tenant of course.

Lease concluded for the definite period of time is automatically expiring by this time frame. No automatic prolongation in the case landlord not filing the action at the court within the 30 days after such expiry is possible in new legislation.

Change to the Legal Regime of the Lease and Sublease of the Non-residential Premises

On October 2005, Act No. 360/2005 Coll. shall enter into force, by the means of which the Act No. 116/1990 Coll., on lease and sublease of non-residential premises, as amended, was amended. By the mentioned amendment legal regulation of lease and sublease of non-residential premises has been materially altered and made more precise. For example, the amendment newly determines the essentials of the contract on lease of non-residential premises.

It is newly established that, unless agreed otherwise, the Lessor shall be obligated to hand over the non-residential premises to the Lessee in condition fitting to the agreed purpose of the lease, to maintain the premises in such condition at his own costs, secure the proper providing of services to be provided with the lease of the non-residential premises, and to enable to the Lessee full and undisturbed exercise of his rights arising out of the lease. On the other hand, it was removed from the act, that the Lessee should be obligated to pay the costs of the ordinary maintenance.

Newly, unless agreed otherwise, the rent and the refund of costs of services provided with the lease shall be paid monthly in advance, always as of the first day of the relevant calendar month.

It is newly expressly permitted to the parties to agree on other reasons for termination of the lease of non-residential premises concluded for the indefinite time period, than those specified by the law.

Apparently crucial in practice will probably be the provision, according to which in case there is any change to the ownership of the building, in which the leased non-residential premises are located, or of the leased non-residential premises in ownership pursuant to a special Act, neither the Lessee nor the Lessor shall for this reason be entitled to terminate the lease, if not agreed otherwise.

The new legal regulation will affect also the contracts on lease of non-residential premises that have already been entered into. The legal relationships incepted before October 19, 2005 shall be governed by this amendment; however, the inception of these legal relationships and the rights and obligations arising thereof prior to the day of effectiveness of this amendment shall be judged in accordance with the existing legislation.

Business Law - Change to the Squeeze out Legislation

On September 29, 2005 an amendment to the commercial code came into effect, which, brought along a change in the regulation of compulsory purchase of shares possessed by minority shareholders to the majority shareholder.

Still effective remains that the entity possessing any security papers in a company, (i) the aggregate nominal value of which amounts to at least 90 % of the company's registered capital, or (ii) which substitute security papers, the aggregate nominal value of which amounts to at least 90 % of the company's registered capital, or (iii) which represent at least a 90% share of the voting rights in the company, is entitled to require the Board of Directors to summon a General Meeting, which shall decide on legal transfer of all other company's security papers to the respective majority shareholder.

The new enactments provide that to adopt the resolution of the General Meeting on legal transfer of all other company's security papers to the majority shareholder, a prior consent of the Securities Commission is required, which shall be issued no sooner than 3 months prior to the respective decision, otherwise the respective decision shall be null and void. It is also provided that the Securities Commission shall always expertise whether the amount of the remuneration is adequate to the value of the security papers, whereas upon the expertise of the adequacy of the remuneration it shall take into consideration especially the fact that the possessor of the security papers shall be deprived of the possibility to decide whether and when he wants to transfer his security papers to the majority shareholder. In doubts the Securities Commission shall take into consideration the interests of the security papers possessors.

The title of the minority shareholders for payment of adequate remuneration is newly secured, as the majority shareholder shall be obligated to hand over the financial assets in the amount necessary for the payment of the remuneration to a securities dealer or to a bank prior to the respective General Meeting session and also to document this fact to the General Meeting. The payment of the remuneration shall be executed by the bank or by the securities dealer.

Legal Professions

Act no 79/2006 Coll amending the Advocacy Act no.85/1996 Coll. finally implemented to Czech system of legal professions new position of “Employed Attorney”. According to the new law Attorney could be employed by another Attorney of by the Law Company and remain formally member of the Bar. In such cases liability of Employed Attorney is limited by the applicable labor legislation to 3.5 of the monthly salary of Employed Attorney.

According to new rules Law Firms could also exist in the form of Limited Liability Company or Limited Partnership (form of company combining limited and general partners) company in other forms with the limited liability of partners. In such a case limitation of liability must be balanced by the increased compulsory insurance coverage. Mandatory minimum coverage for such a company must be at least 50.mil czk (app EUR 1.8 Mil) and minimum coverage for one attorney must be 10.mil CZK (app EUR 350. 000)

Insolvency Act

Transparency of Bankruptcy proceedings in Czech Republic was widely criticized by the international bodies, many criminal charges was recently launched against the whole big groups of people involved in bankruptcy proceedings including judges, attorneys and politics. Modification of the bankruptcy rules was therefore important part of improvement of otherwise unbearable situation.

Insolvency Act (no.182/2006 Coll.) is replacing the obsolete and nonsystematic Bankruptcy act and providing for the comprehensive Insolvency Act is introducing to the Czech bankruptcy legislation new legal instruments, which will make the bankruptcy proceedings quicker and more effective. For the improvement of so far extremely lengthy bankruptcy proceedings new legislation providing for binding time periods for passing some decisions or other acts by bankruptcy administrator and state organs involved.

Until now in fact the prevailing and in practice almost only existing form of the solution of the bankruptcy situation was liquidation of the enterprise. Following the new rules the new form of Reorganization will be applicable for many bankruptcy cases. Creditors will be motivated to accept the safeguarding Reorganization plan of the enterprise enabling to continue in the business activities and generate the profit. Important role in reorganization will play Creditors Committee, which is granted by large scope of powers and closely cooperating with the Bankruptcy Administration, leading the enterprise in Reorganization.

Also another form of solution of insolvency situation – Sell of the Enterprise – is newly and more precisely regulated, providing more transparency and speeding up the procedure. In the case of Sell of Enterprise the seller is now bound by duty to buy the enterprise in full including all receivables and duties.

For the smaller enterprises and also the natural person the new form of solution of insolvency was introduced – Discharge of debts (Personal Bankruptcy). If agreement between debtor and creditors is reached concerning the proportion of satisfied claims (i.e.70 %), than the remaining part of the debts will expire and become no executable. This system will be widely used for the consumer landings, therefore there exist reasonable expectations that this new system will be used by banks in large extend.

In order to improve the transparency of bankruptcy procedures the Insolvency register was also created, being the publicly accessible source of important economic data in electronic form.

As a reaction to the mafia-like conspiracy criminal cases among certain bankruptcy judges, the new legislation gives also more power to the Creditors Committee, mainly the right to appoint and the control Bankruptcy Administrators.

In order to minimize the willfully claimed invalid claims Insolvency Act is providing for financial penalties for such a behavior of creditors, which so far was not punishable.

Labor Law

2006 amendment to Labor Code (Act. no 65/1965 Coll) introduced new fundamental liberal principles to the so far rigid post communist legislation not respecting the private law principles. After decades of theoretical and practical confusion new legislation introduced back the idea of subsidiary of the Civil Code to Labor Code as the part of the Labor legislation. This will ensure more consistency in interpretation and especially at the labor court decision-making.

New labor act is therefore built on the explicate private law principle stating that "*what is not prohibited expressis verbis, is possible and valid*". This general rule is opening the wide possibilities especially in

- the individual approach in entering to the labor contracts reflecting the specifics of particular labor relationship and its parties.
- as a result of this the form of the labor contracts also the *contracust innominatus* considered as a valid and applicable form. This flexibility must however respect not only the mandatory rules of Czech labor legislation but also the international treaties and other rules.
- the strict rules concerning the working time were modified giving more flexibility in creating so called " working time account" particular setup of which is fully subject of agreement of the parties of the Labor contract. Working time accounts will be especially used in the areas of seasonal work as the building industry, agriculture and similar areas with the variable work load
- more flexibility in termination of the labor contract by abolishment of duties of employer to provide some groups of employees (single parents, etc) mandatory offer of the alternate employment position.
- In the case of termination of employment by employee for the health reasons right to special severance payment was abolished.
- Employees are obliged to work only up to 50 hours overtime upon instruction of employer (existing legislation provided for 150 hours overtime duty).
- In the case of death of employer (natural person) all duties will not be passed to heirs and labor relationship is terminated as such.

New Labor Code is also reflecting important **Changes in social security legislation** which introduced the new system of sick leave compensations, when, according to new rules first 14 days of the employees sick leave compensation will now be paid not by state but by employer. This rule is widely criticized and will be most probably subject to constitutional court claim by right wing MP parties.

The bill of the **Labour Inspection Act** was for the third time passed at the meeting of the Chamber of Deputies on June 14, 2005. The entry of this act into force on July 1, 2005 shall probably have far reaching implications for businesses. Until now labour inspection has been relatively disintegrated. Supervision over the observance of the obligations arising out of the labour law regulations, the state's professional supervision over the labour safety protection and technological facilities and over the observance of the stipulated work conditions have been distributed among a number of institutions.

The basic aim of the new Labour Inspection Act is to concentrate supervision over the labour law regulations compliance, from which arise employees' rights or obligations in labour law relations, supervision over the compliance with labour law regulations, which set working hours and the time for resting, supervision over the labour law regulations guaranteeing the labour safety protection and technological facilities and supervision over the other respective legal regulations.

It is newly stipulated that the Inspection Authorities shall also supervise the observance of the collective agreements in those respects, which stipulate the individual employees' rights in relation to the labour law regulations more advantageously. The act now includes the authority of the Inspection Authorities to invite to the inspection also other professionals in addition to the inspectors. The supervisory authority of the Employment Offices according to the Employment Act and Employee's Protection against the Employers Insolvency Act will remain to be regulated by the existing legal regulations and shall not be affected by the proposed legal regulations. Also the supervisory authority of trade unions shall not be affected by the proposed legal regulations.

Doubts about the new act are caused especially by the penalisation provisions. The act introduces substantial fines for offences and infringement of governmental committed by the legal entities constituted by breaches of the labour law regulations. For example a fine up to **CZK 200.000** for an infringement of governmental committed by the legal entity, which breaches the labour law rules concerning the duration of holiday leave period, use of holiday leave or if the legal entity will not set the holiday's draw-down. The legal entities which commit an infringement of governmental constituted by breach of work time regulations, will be penalized by a fine of up to **CZK 2.000.000**. A legal entity will be penalized for an infringement of governmental constituted by breach of the remuneration regulations by a fine of up to **CZK 2.000.000** as well.

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Registered Partnership of Person of the Same Sex

Registered Partnership of Person of the Same Sex Act (Act no 115/2006) was adopted after more than 10 years of public debate and numerous unsuccessful legislative proposals and even against the very final presidential veto. Registered partnership is mainly focused on the property matters as inheritance, alimony, transfer of the lease of the apartments in the cease of death of the partner, right to represent each other in normal course of business. These areas are in fact equalizing the legal status of the Registered partners of the same sex to tradition marriages. The new legislation will not allow registered couples to adopt the child. Registered partnership of person of same sex could only be concluded between major (more than 18 years of age) and non-married or already non-registered person. Registered partnership could be terminated during the lifetime of partners by court only.