



Legal update

December 2019

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

Definition of family business and the family business support program

The Czech Government approved a regulation defining a family business, and this definition will enable the introduction of some form of support for family businesses. A family business can be either a family business corporation or a trade license-based family business.

A family business corporation is a business corporation in which more than half of the members are members of one family and at least one member of the family is its statutory body, or in which members of one family directly or indirectly exercise most of the voting rights and at least one member of the family is a member of the statutory body of this business corporation. A family business corporation is also deemed to be a business corporation in which a majority of voting rights is exercised for the benefit of one family by a foundation or trust fund trustee, provided at least one member of the family is also a member of the statutory body of the foundation, or a trustee of the trust fund.

A trade license-based family business is a business in which at least two members of one family participate via their work or assets and at least one of the family members holds a trade or other similar license or is authorized to do business for another reason.

A key initiative in the field of family business law is the creation of the "Czech National Company" label. As a rule, companies whose formation and activities are largely shared by more than one family member will be entitled to use this state-sponsored label. An essential condition for granting the certificate will be the obligation to observe a Family Business Code of Ethics. Other requirements for granting the certificate are not at present clear. However, the Ministry of Industry and Trade should make every effort to minimize the administrative burden. It is expected that family businesses will be able to start using the new label in the first half of next year.

Recent Case Law

Approval for a statutory body member to exceed a representative's authorization

(Supreme Court Judgment No. 27 Cdo 4593/2017 of 23 July 2019)

In this commercial dispute, the Supreme Court dealt with the exceeding of a representative's authorization by a statutory body member, and its subsequent later approval (ratihabition). The applicant (a limited liability company) sought payment of a sum from the respondents as unjust enrichment, which the respondents had received from the applicant as performance under a contract on a future contract. The contract was signed on behalf of the applicant by only one statutory representative, even though authorization for such act required two statutory representatives to be acting jointly. On that basis, the applicant claimed the contract had never been established.

The Court of First Instance dismissed the action, and the Court of Appeal upheld the decision, affirming the judgment. Upon ascertaining who was authorized to act on behalf of the company, and the fact that the applicant rendered performance to the respondents under the contract, the courts concluded there had been no unjust enrichment to the detriment of the applicant. The Court of Appeal endorsed the ruling of the Court of First Instance whereby the provisions of the Act may be applied in this case, and the represented person is bound by a legal act that he has



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approved without undue delay. The decisive factor, according to the Court of Appeal, was that the applicant had rendered performance under the contract, thereby implicitly approving the contract and remedying the breach of the statutory representative's power.

In its ruling on appeal, the Supreme Court decided that the general provisions governing representation should be applied to members of a statutory body as representatives of a legal entity – insofar as a special regulation governing bodies of legal persons does not specify otherwise. Members of a statutory body may only represent a legal entity in a manner in accordance with the method of representation of a legal entity determined by the founding legal act and entered in a public register.

The Supreme Court stated that a legal entity may subsequently approve an act undertaken by an unauthorized representative. In principle, any individual who would be entitled to represent that legal entity in the (legal) act in question may manifest the will to be bound by acts made by an unauthorized representative.

The good faith of a third party in the representative's authorization is not a condition for its approval. However, it is a prerequisite for the possible binding of the unauthorized representative himself by the (not subsequently approved) legal act. If it is clear from the manner of representation of a legal entity by members of the statutory body registered in the public register of legal entities that only two or more members of the statutory body jointly represent the legal entity, the person being dealt with will generally not (in light of the principle of formal and material public register disclosure) be in good faith that only one member of the statutory body of a legal entity may represent such legal entity. Lack of good faith of a third party results in a legal act that is not subsequently approved binding neither the represented legal entity nor the unauthorized representative.

The Supreme Court reflected these conclusions in the present case and decided to set aside the judgment of the Court of Appeal. In particular, the Court of Appeal erred in not considering whether the appellant had been represented by a person entitled to express the will to subsequently approve the contract in the asserted implied conduct consisting in remitting part of the price under the contract. In the given situation, it was not possible (thus far) to conclude that the appellant (the company) had expressed the will to be bound by the concluded contract.

Additionally, the Court of Appeal ruling under which, in the absence of additional approval, the statutory representative would himself be bound by the contract was, at the very least, premature (having regard to the absence of an assessment as to whether the respondents, in good faith in the representative's power of attorney, were acting in breach of the Commercial Register entry).

Statutory representative's liability for damage caused by him/her through misappropriation of company property

(Supreme Court Resolution No. 27 Cdo 844/2018 of 18 September 2019)

In this resolution, the Supreme Court dealt with the liability of a statutory representative failing sufficiently to control another statutory representative who misappropriated company assets. Together with the other statutory representative (M.K.), the respondent was obliged – in accordance with lower court decisions – jointly and severally to repay sums that statutory representative M.K. had misappropriated from the applicant (the insolvency trustee of the debtor).

In the present case, the courts found that the appellant (statutory representative) had breached his obligations in the performance of his duties in that capacity, as he left the management of the company entirely to director M.K., who later became the second statutory representative (although they did not have a division of responsibilities), and by virtue of his failing to set up any control mechanisms or to control how the company was being run and managed, thereby enabling M.K. to withdraw funds from the company's bank account and use these for his own needs. The Supreme Court is in line with the conclusions of the courts of both instances, according to which such conduct contradicts the requirement of due managerial care.

The Supreme Court further states that if a statutory representative is acting only formally, i.e. he does not in fact perform the function and leaves fulfilment of the duties of the statutory body to another statutory representative or to company employees, and fails also to control how the company is being run and how its affairs are being handled, it can as a rule only be concluded that he has not acted with due managerial care.

In assessing the case, the appellant emphasized – without legal significance – the fact that it was he who ultimately uncovered the crime committed by M.K. and filed a criminal complaint. Similarly, the objection that the appellant did not understand bookkeeping and therefore had engaged qualified "staff" is irrelevant. Preventing or detecting embezzlement in a timely way did not require knowledge of accounting, but, at the very least, a minimal interest in the corporate governance from the appellant.

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We firmly believe you will find *Legal Update* a useful source of information and we would value your feedback on this newsletter, in particular its content, format and frequency.

Please e-mail any comments to jakub.kolda@weinholdlegal.com or fax them care of Jakub Kolda to +420 225 385 444, or contact your usual partner or manager.