

Capital Punishment for Corporations

After a number of unsuccessful attempts to introduce the criminal liability of corporations into Czech law, a new Act on Criminal Liability of Corporations was finally adopted by the Czech Parliament recently when the Lower House overrode the President's veto. The Act will come into effect as of 1 January 2012 and is likely to transform the legal landscape in which Czech businesses operate. The Act was passed to meet the Czech Republic's international commitments and also as part of the Czech government's anti-corruption strategy.

The criminal liability of corporations

The Act introduces approximately 80 criminal offences, most notably offences related to money laundering, corruption, interference with justice, fraud, fraudulent accounting, rigging of tenders, pollution or other degradation of the environment, organised crime, human trafficking, computer crimes and tax related offences.

A legal person (including all forms of corporations, other than the State and its territorial units, but including the Czech National Bank, state-owned companies and enterprises and entities such as hospitals and schools) will be held criminally liable if the criminal offence is committed on its behalf, in its interests or as part of its activities and the offence is committed by (i) its statutory body or *other* persons acting on its behalf; (ii) persons performing managerial or supervisory activities within the corporation; (iii) persons exercising decisive influence over the management of the corporation; or (iv) its employees while carrying out their

tasks, subject to further qualifications set out in the Act, e.g. where due supervision was not exercised.

A corporation (including a foreign corporation) can be held liable under the Act if it is registered in the Czech Republic, conducts its business in the Czech Republic through an enterprise or branch or otherwise, or has assets in the Czech Republic. Czech corporations can also be punished under the Act for criminal offences committed abroad.

A corporation will be held liable even if the individual offender (as specified above) cannot be identified. Criminal liability of corporations will be without prejudice to and independent of the criminal liability of the individual offenders themselves. Corporations that have used other corporations or individuals to commit criminal offences may also be classed as offenders.

Unlike in the case of criminal liability of individuals, under the Act, the criminal liability of corporations will pass to each of its legal successors. This is to prevent the evasion of

Key issues

- Criminal liability of corporations
- Penalties
- Criminal records for corporations
- Implications of new regulation
- Compliance required
- Impact on insolvency

liability through the deliberate transformation of a corporation.

Penalties can be severe

The Act outlines eight penalties and a single "protective measure" (in Czech: *ochranné opatření*) which can be imposed. The most severe penalty will be the dissolution of the corporation. This penalty can only be imposed against legal entities with a seat in the Czech Republic and only if the activities of such legal entities wholly or predominantly consist in the commission of criminal offences.

The other possible sanctions are:

- **Forfeiture of property (wholly or partly);**
- **Monetary penalties;**
- **Forfeiture of a thing or other property value;**
- **Prohibition of activity (for up to 20 years);**
- **Prohibition of performance under public procurement contracts, participation in concession procedures or public tenders (for up to 20 years);**
- **Prohibition on accepting grants and subsidies (for up to 20 years);**
- **Publication of judgments.**

As regards the protective measure, the court will be able to order the seizure of a thing or other property value.

Corporations to have criminal records

Similarly to the crimes committed by individuals, criminal offences committed by corporations will also be registered in the Criminal Records Register (in Czech: *Rejstřík trestů*). Unlike in the case of individuals, the data in the Criminal Records Register in respect of corporations will be publicly accessible. In addition, the fact that criminal proceedings against a corporation have been initiated/terminated will be reported to the Commercial Register and/or other relevant registers.

Interconnection with the Czech Criminal Code and Code of Criminal Procedure

The Act constitutes an entirely separate act but foresees the default

application of the Czech Criminal Code and the Czech Code of Criminal Procedure where the Act does not provide specific rules and the nature of the matter permits.

Implications of the new legal regulation

The Act will enable the punishment of criminal conduct that currently cannot be sanctioned due to the fact that it is often impossible to identify the responsible individual where the collective body of a corporation adopts a decision. It can also help prevent situations where an individual is identified and held criminally liable but the corporation continues its criminal conduct. The penalties contemplated under the Act can severely affect the continued operation and profitability of corporations. However, it is difficult to judge at this point whether the Act will prove an effective deterrent to corporate crime. It still remains to be seen what the impact of the Act will be on corporate crime and the criminal liability of corporations in practice.

Practical implications

The introduction of criminal liability of legal persons will influence both the day-to-day operation of companies and also less common events such as acquisitions or insolvency proceedings.

Compliance required

Every corporation can be held criminally liable for offences committed by a wide range of persons. Besides the actions of members of its statutory body, corporations can also be held accountable for actions performed by persons acting on the basis of a power of attorney (including advisers), members of the supervisory board, members of the

audit committee, persons acting on behalf of a corporation on the basis of Section 15 of the Czech Commercial Code, parent companies acting as shadow directors, etc.

A corporation will also be criminally liable for offences committed by its employees (widely defined) if they were following the instructions of their superiors or when they commit a criminal offence as a result of a lack of certain measures which are required by law or can be reasonably required (supervision). A corporation cannot be criminally liable for actions constituting an independent excess on the part of the employee, i.e. if the corporation did all that could be reasonably expected of it to prevent the employee's conduct leading to an offence.

It is clear that compliance will now be key for any corporation, covering a range of areas from the rules for issuing powers of attorney to the proper supervision of employees. In this respect it is highly advisable to identify the main areas of risk and amend internal regulations setting out internal policies, procedures and the corporation's risk-mapping, and to train people accordingly. Otherwise corporations may face tough measures such as the forfeiture of property or disqualification from public tenders.

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Examination of the criminal liability of legal persons is bound to become a regular part of due diligence exercises and will also have to be reflected in contractual documentation (e.g. warranties, withdrawal or special indemnities).

No transformation of a corporation will be possible after the commencement of criminal prosecution or during execution proceedings, unless approved by the court. It is worth

mentioning that the Act might create room for abuse by third parties who may wilfully initiate criminal proceedings to complicate acquisitions and mergers.

Banks and similar regulated entities

The Act also covers criminal offences committed by banks, insurance houses, reinsurance houses, investment companies, investment funds, securities brokers, savings and credit cooperatives, the central depository, electronic money institutions, payment institutions, settlement system operators and organisers of the investment instruments market. In the case of these entities the imposition of certain penalties will be subject to the opinion of the Czech National Bank.

Criminal penalties levied on corporations and insolvency

Under Czech insolvency law, the opening of insolvency proceedings does not result in a stay of criminal proceedings conducted against the debtor, including proceedings under the new Act. Thus, criminal

proceedings may be continued or even commenced irrespective of whether the defendant corporation is also subject to insolvency proceedings.

Nonetheless, Czech insolvency law contains a rule under which non-contractual sanctions levied over the debtor's assets (other than certain penalties accruing on tax arrears) may not be satisfied in insolvency proceedings. Therefore, the three potentially most potent penalties meted out under the Act (forfeiture of property (wholly or partly), monetary penalties, or forfeiture of a thing or other property value) should not become a threat to the satisfaction of the corporate defendant's creditors.

It remains to be seen how insolvency courts will react when they are first faced with reorganization proposals that, as the result of the rule cited above, would ultimately result in the discharge of a criminal penalty imposed under the Act.

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