

LEX COVID 2.0: FURTHER EMERGENCY AMENDMENTS TO CZECH INSOLVENCY LAW

In the spring of 2020, Act No. 191/2020 Sb. (also referred to as "*Lex Covid*") was quite understandably enacted in the form of emergency legislation as an improvised legislative response to the Covid-19 outbreak. Yet the proposal to amend Act, tabled by the Czech government in the Chamber of Deputies as Bill 1060 in late October, gives rise to certain concerns both over its contents and over the fact that the government drafted and tabled the bill without subjecting it to any public consultation, despite having had six months in which to do so. On 10 November 2020, the amendment was passed into law by the Chamber of Deputies – once again in the form of emergency legislation – despite partial objections raised by the Senate. This publication briefly outlines these amendments, mainly from the perspective of lending and other financial markets.

SUSPENSION OF THE DUTY TO FILE AND THE RELATED LIABILITY

The original *Lex Covid* suspended, for the duration of the emergency anti-Covid measures and for six months thereafter, though not beyond the end of 2020, the debtors' duty to file for insolvency proceedings under Section 98 of the Czech Insolvency Act, and the associated personal liability of directors under Section 99 of the Insolvency Act. Additionally, it suspended the right of creditors to file insolvency petitions up to the end of August 2020.

The amendments in no way affect the creditors' right – renewed since September 2020 – to file insolvency petitions. But they once again suspend the debtors' duty to file for insolvency, this time up to the end of June 2021.

In addition, substantial changes to the rules governing the liability of directors Czech corporations are on the way not only under the *Lex Covid* amendments, but also under impending amendments to the Business Corporations Act (the "**BCA**"). From 1 January 2021, an entirely new provision (Section 66 of the BCA) will apply to the liability of directors of companies threatened with insolvency, enacting a rule more lenient towards directors than the existing provisions of Section 68 of the BCA which will be repealed on 31 December 2020. Viewed from a creditor's perspective, the situation is naturally the opposite – the protections provided to them by Section 68 of the BCA throughout the period of suspension of the debtor's duty to file under the original *Lex Covid* will be weakened from 1 January 2021.

IS THE EXTRAORDINARY MORATORIUM STILL "EXTRAORDINARY"?

Lex Covid introduced the new extraordinary moratorium provisions (Section 127a) into the Insolvency Act as a time-limited emergency tool to protect Czech debtors who were not insolvent at the outbreak of the epidemic. Debtors could have utilised the extraordinary moratorium only if they applied for it by the end of August 2020.

Despite a lack of any systematic analysis of the experiences with the extraordinary moratorium, and despite the failure to remove the shortcomings in the original wording of Section 127a committed during the improvised drafting

exercise in the spring of 2020, the amendments to *Lex Covid* merely extend the availability of the extraordinary moratorium up to the end of June 2021. Apart from this, and despite floor amendments to the contrary tabled both in the Chamber of Deputies and in the Senate, a new rule has been introduced whereby an extraordinary moratorium ordered on the basis of an application filed before the end of August 2020 may be extended by a court without the consent of the creditors. This change retroactively interferes with creditors' rights, infringes on their legitimate expectations arising out of the original wording of *Lex Covid* and, moreover, it discriminates among debtors based on the moment when they applied for the extraordinary moratorium (creditors' consent to extensions will still be required in moratoriums ordered after the amendments enter into force). These outcomes are so controversial that, in our view, one cannot rule out the possibility that they will become subject to judicial review as regards their constitutionality.

As regards the contents of the amended rules, the extraordinary moratorium provisions have not changed much in practical terms, except that the solvency of the debtor applying for the extraordinary moratorium will be tested against circumstances in place as of October 2020, not March, and that the extraordinary moratorium will not be available to debtors who have already been granted one in the past.

As in the original *Lex Covid*, an extraordinary moratorium will not only prevent the commencement of insolvency proceedings, but will also stay the enforcement of charges and other forms of unilateral debt collection. The extraordinary moratorium will also not prevent debtors from utilising any state aid provided in connection with the Covid-19 outbreak. In addition, under the conditions set out by the law, it will continue to enable debtors to prioritise the payment of liabilities which are directly related to the operations of the debtor's business and which have arisen since the extraordinary moratorium was declared, over liabilities which were due and payable earlier. The extraordinary moratorium will also protect debtors from having certain long-term contracts terminated by their counterparties, similar to the protection provided under the "ordinary" moratorium pursuant to Section 115 and the following of the Insolvency Act.

Just as under the original wording of Section 127a of the Insolvency Act, debtors who utilise the extraordinary moratorium will have a duty to use their best efforts to provide the best possible outcome for creditors and to prioritise their creditors' interests over their own interests or the interests of other parties. As in the "ordinary" moratorium, directors will be personally liable for any loss caused by a breach of the debtor's obligations during the moratorium or in connection with the application for it. Unlike with the "ordinary" moratorium, set-off will not be prohibited under the extraordinary moratorium. In derivative and other financial transactions, extraordinary moratoriums will not affect (similarly to the "ordinary" moratorium) financial collateral or close-out netting provisions. Since extraordinary moratoriums will continue not to be notified as proceedings under the European Insolvency Regulation 2015/848, their protective effects will not apply outside the Czech Republic.

Extraordinary moratoriums ordered under the amendments will terminate once the period for which they were ordered has expired, unless the majority of the debtor's creditors consent to their extension. Extraordinary moratoriums will also terminate if the debtor files an insolvency petition or if the court orders an "ordinary" moratorium following a subsequent application by the debtor.

On the whole, we find it rather unfortunate that the entirely improvised legislative solution arrived at in the spring of 2020 will remain a part of Czech insolvency law for more than a year. We can only hope that these "temporary" measures will not be extended again by emergency legislation after June 2021.

SUSPENSION OF THE CLAW-BACK PERIODS

Just as under the original wording of *Lex Covid*, the amendments also contain a rule whereby, for as long as the debtors' obligation to file for insolvency proceedings is suspended, the running of claw-back periods relevant to actions for the avoidance of antecedent transactions will also be suspended.

EFFECTIVE DATE

The amendments will take effect immediately upon publication in the Collection of Laws.

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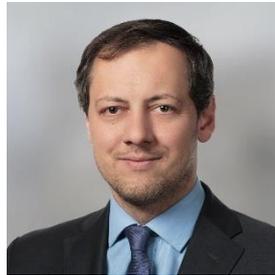
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