

Opportunities for entrepreneurs in times of economic crisis

Overview of potential measures

Against the backdrop of the worsening economic conditions, company management are often faced with the decision whether certain business activities should be terminated or if different measures should be taken with respect to cost reduction. In this article, we will examine various measures that can be taken within a given context. At the same time focus will be placed upon the circumstances in respect of individual cases. Concurrently, it is nevertheless always advisable to carry out a detailed and extensive analysis of the economic, tax and legal aspects in regard to the circumstances surrounding the given case.

Measures concerning termination of business activities

Where it concerns terminating production and trade activities, **cessation of operations** or **liquidation** of the company are specific terms which come into account. In this connection, it is also necessary to mention the term bankruptcy as well.

Cessation of operations, i.e. termination of business activities without winding up the company does not have any direct consequences in light of Company Law. However, if the company is not wound up nor deleted from the Commercial Register, some obligations arising from the Commercial Code or accounting and tax provisions ("*corporate maintenance*") may continue to persist for the company. If operations cease, in most cases employees are dismissed. In general, the employment relationship is primarily terminated by giving notice or by an agreement. The termination of business activities and the eventual winding up of the company falls under legal grounds for providing notice (so-called organizational changes). In such cases a statutory two-month notice period is set. In addition, companies can give rise to one-off costs, e.g. severance payment pertaining to employees under law or on the basis of a collective agreement (amounting to at minimum three average monthly wages of the employee). If at the moment of ceasing operations the company has more than 20 employees, it is necessary to uphold stricter statutory conditions for collective dismissals (notification duty towards trade-union organizations / works' councils / employees, notification and submission of a situational report to the competent labour office, etc.). In addition to labour-law consequences, costs may give rise in connection with the termination of long-term contracts, e.g. lease or supplier contracts, or as consequence of a below cost sale of the company's property, etc.

In the event of liquidation, the company is wound up by decision of the General Meeting. The company enters into liquidation on a particular date at which time a liquidator is appointed thereby taking over the competence of the statutory body of the company regarding all acts leading up to liquidation of the company. The registration of the liquidation and liquidator with the Commercial Register has only declaratory effects. The liquidator is obligated to inform all known creditors of the fact that the company has entered into liquidation and at least on two occasions must also make public the resolution or ruling on the winding up of the company, thus inviting the company's creditors to submit any outstanding debts. The creditors have a fixed period set by the liquidator, which is not shorter than 3 months, within which they may submit their claims. Such claims must be settled by the company. Once all obligations of the company have been paid, the liquidator will distribute the resulting yield from the liquidation proceeds amongst the shareholders. After approval has been granted by the tax authority to

the deletion of the company from the Commercial Register, the liquidator must file a petition for the company to be stricken from the Commercial Register. Based on previous experience, the entire liquidation process in the Czech Republic takes anywhere from five to six months. However, the given period can be substantially prolonged as a result of lengthy negotiations with the creditors regarding finalization of existing statutory relations.

A company that is bankrupt, *i.e.* that is insolvent, over-indebted or the threat of bankruptcy is imminent, according to the Czech Insolvency Act such company is obligated to file a petition initiating **insolvency proceedings** with the competent court without undue delay. Infringement of this duty could result in the responsibility of liable persons to compensate for damages (towards the creditors of the company while in bankruptcy), more specifically, responsibility on the part of the statutory body of the company. In addition, criminal liability can be placed upon such individuals breaching such fiduciary duty on filing a petition to initiate insolvency proceedings. On January 1, 2008 a new Insolvency Act became effective which, in addition to traditional bankruptcy with proportional distribution of the bankruptcy assets and customary subsequent liquidation of the company, also enables so-called reorganization within the company, thus allowing for continued operations which in turn provides more effective and transparent satisfaction to the creditors; however, reorganization can only be implemented by larger companies (with a turnover in excess of CZK 100 million over the last accounting period and more than 100 employees). Such recovery of the company is carried out according to a reorganizational plan that must be approved by an insolvency court and a meeting of the creditors.

Cost reduction and optimization measures

The Czech Labour Act is acquainted with various instruments on how to reduce labour costs such as e.g. establishing so-called **account of working hours, partial unemployment** or when necessary, also reduction in the number of employees on the basis of **collective dismissals**.

In the case of an **account of working hours**, work is provided to the employees over the course of a settlement period according to the reduced needs of the employer, eventually to a greater extent than by the average weekly working hours. The employee shall always receive, at least 80% of his monthly average wage. The account of working hours can only be included in a relevant collective agreement or in the company's internal regulations. However, the settlement period may not typically exceed 26 consecutive weeks, and only the relevant collective agreement may change this period of up to a maximum of 52 weeks.

Partial unemployment represents an impediment to work on the side of the employer in which an employer is unable to provide an employee with any work due to a temporary drop in the employer's product sales or demand. Under these circumstances, an individual employee must be paid a compensatory wage at least 60% of his average monthly earnings. In this regard, it is necessary to conclude an agreement between the employer and the trade union organization, and eventually a decision from the competent labour office must be issued regarding the reasons justifying payment of compensatory wages at a lower level. In addition, it is also possible to conclude an agreement with the employee regarding part-time work and a lower respective wage (**part-time work**). If conditions necessary for **collective dismissals** are satisfied by an employer, *i.e.* termination of a specific number of employment relationships within a period of 30 calendar days on the basis of organizational changes, prior to the first given notice legal obligations arise to the employer towards trade union organizations / works' councils, eventually to an individual employee (prior written notice, consultation, etc.) and towards the respective labour office (written notice, report, etc.). In general, a collective dismissal is usually implemented within a time-period of 3 to 4 months.

Cost reduction can also potentially be attained by measures taken within the sphere of Commercial Law as well as through corporate modifications. In particular, the purpose of these measures is to consolidate and rationalize the concerned business activities, which in turn will result in the synergy and reduction of statutory and tax obligations. Here it is also noteworthy to mention e.g. the **transfer of enterprise or its part**, when the seller as a legal subject remains to exist; a **merger, de-merger** or **transfer of business assets** upon a shareholder whereat the company typically ceases to exist at the moment the entry is made into the Commercial Register.

With regard to the new Act of Transformations, which became effective on July 1, 2008, allowing for cross-border mergers, restructuring can also include groups of foreign companies. Aside from synergizing effects, it is also possible to attain a significant savings with concern to a permanent secession of corporate management.



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