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New Insolvency Rules Resulting from the COVID-19 Pandemic

The current unusual situation caused by the COVID-19 pandemic will undoubtedly have substantial consequences for the economy of the Czech Republic. It can be expected that the amount of debts will rise sharply not only on the side of the state, but also on the side of citizens and business entities. Subsequently, many of these debts are not going to be repaid. Therefore, such debts will be claimed before the courts and other competent authorities sooner or later and subsequently enforced (either individually through enforcement proceedings or collectively through insolvency proceedings).

The current emergency may thus lead to the bankruptcy of many entrepreneurs, both in the form of insolvency and in the form of over-indebtedness. **In spite of the current extraordinary situation, entrepreneurs are still obliged to file an insolvency petition without undue delay after they have learned of their insolvency or should have learned about it exercising due care.** This obligation is also not affected by the fact that the insolvency could have been caused by the current emergency and it could be expected that the debtor will be able to recover from the inability to pay its debts in the near future (the so-called temporary insolvency). **This puts many entrepreneurs at considerable risk, as their personal property may also be at stake. Failure to file the insolvency petition creates the liability of these persons (including members of the statutory body) for damages.**

On March 31, 2020, the Government of the Czech Republic tried to mitigate the negative consequences of the COVID-19 pandemic on the economic situation of citizens and entrepreneurs by passing a bill (adopting draft legislation) to amend, inter alia, the Insolvency Act and the Act on Private Enforcement Procedure (hereinafter referred to as the "**Amendment**"). The Czech Republic thus follows the countries such as Germany or Spain which have already adopted certain changes to their enforcement or insolvency regulations.

The most important proposed changes to the Czech insolvency law can be summarized as follows:

- 1. Limitation of the obligation of entrepreneurs to file debtor insolvency petitions:** A new rule is introduced for entrepreneurs not being obliged to file a debtor insolvency petition within the period from the effective date of the Amendment until 6 months from the termination or cancellation of an emergency anti-epidemic measures (but no later than by December 31, 2020). An exception to this rule exists when (i) the insolvency occurred even before an emergency anti-epidemic measure was adopted, or (ii) the insolvency was not mostly caused by the emergency anti-epidemic measure that would make it impossible or substantially difficult for the debtor to fulfil its payment obligations.
- 2. Limitation of creditor insolvency petitions:** Creditor insolvency petitions filed from the effective date of the Amendment till August 31, 2020 will not be taken into account. Thus, there is a legal fiction that no such insolvency petition will have been filed. Therefore, such filing will not even be published in the insolvency register. The purpose of this measure is, inter alia, to prevent the debtor from spending money to defend against a creditor's insolvency petition. However, the creditors will still be entitled to exercise their civil-law rights (e.g. by offsetting or enforcing a collateral), in court proceedings or out of court. [1] This measure - unlike the limitation of the obligation of entrepreneurs to file debtor's insolvency petitions - affects all debtors (i.e. not only entrepreneurs) and regardless of why and when the insolvency occurred.
- 3. Introducing an extraordinary moratorium:** The Amendment establishes the rule that a debtor who is an entrepreneur and who has not been in bankruptcy at the date of March 12, 2020 can file a request for a so-called extraordinary moratorium by August 31, 2020. The effect of the moratorium is that: (i) the debtor cannot be declared insolvent for the duration of the moratorium, (ii) the debts required to maintain the debtor's enterprise that arise after the extraordinary moratorium is introduced can be paid by the debtor during the moratorium preferentially, before previously due liabilities are met and (iii) the time limits for exercising rights against the debtor for the duration of the extraordinary moratorium neither commence nor continue to run. The debtor may file a motion for a moratorium order even before the filing of an insolvency petition and the commencement of the insolvency proceedings. In addition, unlike the current "normal" moratorium, the proposal for an extraordinary moratorium does not need to be approved by the majority of the debtor's creditors.
- 4. Suspension of performance of a reorganization plan:** A debtor whose reorganization plan has been legitimately (finally) approved as of March 12, 2020 at the latest is entitled to propose to the insolvency court to state that the debtor is entitled to temporarily suspend performance of the reorganization plan (provided that the plan has not yet been fully fulfilled). The performance of the reorganization plan may be interrupted for the period of time during which the obligation of entrepreneurs to file debtor's insolvency petitions is to be limited (see section 2 above). During the said period, it will not be possible to convert reorganization into bankruptcy (i.e. the liquidating way of the bankruptcy solution). However, the insolvency trustee and the creditor committee must comment on the debtor's proposal to suspend the reorganization plan.

5. Discontinuation of time limits for relative ineffectiveness of legal acts: During the period of limitation of the obligation of entrepreneurs to file debtor's insolvency petitions (see section 2 above), time limits for objections to relative ineffectiveness of legal acts should be suspended. By claiming ineffectiveness of a legal act, creditors can defend themselves within the statutory time limit against legal acts of the debtor that jeopardize the payment of their enforceable claim. When the measures described above provide special protection to the debtor, it is equally fair, during the period of such emergency measures, to discontinue the time limits for creditors within which they can defend themselves against the debtor's prejudicing acts. Nevertheless, it is recommended that creditors should, even during the state of emergency, carefully monitor changes in the structure of their debtors' assets (e.g. in the land registry) so that they can effectively defend themselves against any prejudicing disposal of the debtor's assets.

The Government proposes that the Amendment is to be discussed by both chambers of the Parliament of the Czech Republic in an abbreviated procedure. Therefore, it can be expected that the Amendment may be passed in a few days. However, before the described changes to insolvency law become effective, entrepreneurs still have the obligation (i) to perform the so-called insolvency test and (ii) to file a debtor's insolvency petition without delay after the defined prerequisites of insolvency are met. **Failure to comply with this obligation may have far-reaching consequences not only for the legal entity, but also for the members of its statutory body, consisting mainly in incurring liability for damage caused thereby.**

We would like to assure you that we have extensive practical experience with insolvency law, from the point of creditors and debtors (and their statutory bodies). We also continuously monitor the current changes in Czech insolvency law. Please feel free to contact us if you have any questions regarding the above.

At the same time, we are ready to provide you with comprehensive legal advice on imminent or already existing bankruptcy situation (if any) and solutions thereto under insolvency law, including protection against personal liability of members of statutory bodies of legal entities. Such advice can be provided in connection with your (imminent) bankruptcy situation, but also in the case of bankruptcy of your contractual partners (either suppliers or customers). Should you decide to enforce your receivables in a different manner than by insolvency, we will be happy to propose the best solution for you and to provide you with comprehensive legal representation. If you are in danger of bankruptcy as a result of the crisis-related measures of the Government of the Czech Republic, we are ready to provide you with comprehensive legal advice regarding claiming damages towards the state. [2]

At the same time, insolvency can be an opportunity to expand your business activities, for example by buying a debtor's enterprise. We also have considerable experience with insolvency acquisitions and, therefore, we can provide you with the necessary assistance in this regard.

[1] For out-of-court dispute resolution options at the time of the coronavirus epidemic, see the ŘANDA HAVEL LEGAL newsletter called "Impact of the COVID-19 Epidemic on Dispute Resolution" that is available [here](#)

[2] For the possibility of claiming compensation from the State for crisis measures, see the ŘANDA HAVEL LEGAL newsletter on "Recent Developments in the Matter of State Liability for Damage in Connection with Measures in Crisis" that is available [here](#)

