



→ **Security Transfer of Rights – Effective Security**

Ownership of property acquired with a security transfer of rights can be automatically transferred to someone else.

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→ **Should Exchange Rate Differences be Entered in the Tax Base?**

In its decision the Supreme Administrative Court overturns previous practice.

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→ **New Civil Code Provides New Rules Regarding the Statute of Limitations**

Parties may as of 1 January 2014 effectively agree to shorten or extend limitation periods.

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## → Security Transfer of Rights – Effective Security

When entering into commercial contracts the entitled party is always interested in reasonably securing the due fulfilment of obligations or the payment of claims by the liable party. Typical security instruments include establishment of a lien on property or the entitled party's claims, a bank guarantee or the issue of a bill of exchange. Less common is the establishment of security through the security transfer of rights based on the principle that the liable party will transfer its right (usually an ownership right but it could also, for example, involve the assignment of a claim) to the entitled party and after the secured obligation has been met the original state will be renewed. The fulfilment of the secured obligation therefore represents a resolutive condition for the transfer of rights in question.

The use of the security transfer of rights is very practical in securing the due fulfilment of a liability to pay loan obligations. In view of the fact that the entitled party can dispose of the property that is subject to the security transfer of rights as the owner if the liable party does not fulfil its obligations, the security transfer of a title to real property, for example, is considered to be more practical than the standard application of a lien.

Recently, however, legal practice addressed the question of whether a property that is subject to the security transfer of rights can be transferred to somebody else without the secured obligation becoming due and the liable party therefore not being in default of fulfilling its obligation at the time of the transfer and whether in this situation the Land Registry Office is required to register the title in favour of the new assignee or whether it is entitled to reject such a proposal. The Supreme Court recently dealt with such a situation and in its verdict file ref. Cdo 3766/2010 of 8th September 2011 it came to the conclusion that “whoever has acquired ownership of real property based on a security transfer of rights is entitled to automatically transfer the acquired ownership to someone else” and it also stated that “in proceedings concerning the entry of a title in the property register the Land Registry Office does not deal, even as a

preliminary issue, with whether the resolutive condition for the security transfer of rights has been met.”

In the dispute in question the beneficiary of the secured obligation had transferred its title to real property (a residential unit), which it had conditionally acquired on the basis of the security transfer of rights from the liable party, to a third party and had demanded that the Land Registry Office enter the relevant title in the property register. The Land Registry Office had, however, rejected the proposal stating that the resolutive condition had been met and the entitled party no longer had the title at the time the proposal for the entry was made. This conclusion was contested by the entitled party in court on the grounds that the debt had not been paid.

After examining the entire case the Supreme Court came to the conclusion that there was nothing to prevent a creditor that had acquired the title to real property on the basis of a security transfer of rights from being able to transfer this title to a third party. Any resolutive condition (unless it has already occurred), however, shall pass to the new assignee on the transfer of ownership. So if the obligation were fulfilled, the debtor would again have the title to the property. In its decision the Supreme Court also stated the opinion that in the proceedings concerning the entry of a title in the property register the Land Registry Office does not have the right to examine whether the resolutive condition has been met or not because it is not entitled to do so according to the explicitly defined conditions regarding the entry of a right under Section 5, paragraph 1e) of Act No 265/1992 Coll., on the registration of titles and rights in rem to real property.

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## ▶ Should Exchange Rate Differences be Entered in the Tax Base?

In a case heard before the Supreme Administrative Court under file ref. 5 Afs 45/2011 the question of whether foreign exchange revenue from the revaluation of long-term liabilities in a foreign currency on the



financial statements date are real taxable income was addressed.

In the dispute in question the complainant had used long-term loans which had been provided by foreign entities in a foreign currency to finance the construction of a hotel in Prague. When compiling its financial statements the complainant had converted its liabilities in the foreign currency into Czech crowns. It incurred exchange rate gains from the conversion of the foreign currency liabilities which, according to current practice, are entered into the income tax base. However, the complainant requested that these unrealised exchange rate differences be excluded from the tax base. It argued that the unrealised exchange rate differences reflected a situation that had not yet happened and is only simulated for accounting for reporting purposes. Any real enrichment will only occur on payment of the loan instalment. (note: In practice a situation often occurs where companies initially finance their investment loans from foreign investors in a foreign currency and despite the fact that to begin with they do not actually generate any profits from their business activities, they incur relatively high exchange rate gains and as a result also a considerable tax liability due to exchange rate fluctuations).

When deciding the dispute the Supreme Administrative Court in its verdict of 19th April 2012 broke the current procedure regarding the taxation of exchange rate differences as it decided that unrealised exchange rate gains are only a fictitious income because the taxpayer's property does not increase on the balance sheet date when a foreign currency is converted. For this reason the income from unrealised exchange rate differences is not part of the tax base.

On this particular issue the Supreme Administrative Court relies on the definition of income in previous jurisprudence. The court also refers to Sections 18 and 23 of the Income Tax Act. According to Section 18, paragraph 1 of the Income Tax Act income (revenue) from all activities and the management of all property is subject to tax, unless stated otherwise elsewhere in the Income Tax Act. In the court's opinion a change in the exchange rate alone does not meet this definition and in the other provisions of the Income Tax Act

there is no specific mention of unrealised exchange rate differences. The interpretation of Section 23 of the income Tax Act also supported its argument. It states that the trading income is used to determine the tax base, not that the trading income is the tax base.

After the ruling was published the professional community, the Czech Chamber of Tax Advisors and financial administration were in doubt because it was not clear whether to begin proceeding according to this ruling or to continue under the existing, established practice. Therefore the General Financial Directorate subsequently gave a statement on 6th June 2012 stating that it considers this ruling to be a decision in a specific case and so due to its unique nature the decision does not represent established jurisprudence and therefore the established application procedures that have been used up until now shall be maintained by the tax administration.

In view of the above information given by the General Financial Directorate, in general a more conservative approach and respect for this statement is, of course, recommended. Nevertheless in certain cases it may seem tempting to taxpayers to use the Supreme Administrative Court's opinion for their benefit even though such a procedure involves the risk that they will have to defend it in a court case.

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### ► **New Civil Code Provides New Rules Regarding the Statute of Limitations**

Once the new Civil Code (act No. 89/2012 Coll.) comes into force, it will introduce certain changes with respect to the statute of limitations. The following article takes a closer look at the most prominent of these changes.

In the Civil Code as is in force today (act No. 40/1964 Coll.), limitation (or "prescription") is strictly governed by mandatory provisions, i.e., the parties to a legal relationship or transaction may not elect to deviate from the statutory arrangement, even if they are in mutual

consent. The new Civil Code will to some extent break with this mandatory character of the statute of limitations.

The limitation period remains three years also under the new Civil Code (Sec. 629); this will newly also apply to commercial relationships (for which the limitation period has previously been four years according to today's Commercial Code). The commencement of the limitation period is newly tied to that moment in which the beneficiary learns of the circumstances which are relevant for the statute of limitations (or in which the beneficiary should and could have learned of them – Sec. 619).

According to the new Civil Code, the parties may agree on a shorter or longer limitation period in deviation from the statutory arrangement, which is calculated as of the day on which the pertinent right could have been invoked for the first time (Sec. 630). In this manner, parties may agree on a limitation period of at least one year and no more than fifteen years. Shortening the limitation period is not possible, however, with respect to claims for performance arising from loss or harm of freedom or life and limb, and from an intentional breach of obligations, nor will arrangements be taken into account which extend or shorten the limitation period at the expense of the weaker of the two parties. The provisions concerning the beginning, suspension, and lapse of the limitation period remain mandatory (i.e., non-optional) also in the new Civil Code.

The new rules also respond to the frequent case of debtors who willfully protract out-of-court negotiations by making promises of future performance - on which they then renege once the limitation period has lapsed, invoking the statute of limitations. For this reason, the lawmaker newly prescribes that the limitation period will not begin if the debtor and creditor have entered into an agreement on out-of-court negotiations regarding the right which may become subject to limitation (Sec. 647) or, as the case may be, will be suspended for as long as the negotiations last (if the limitation period had already commenced). In these cases, the limitation period commences only after the debtor or the creditor expressly refused to partake in further negotiations. The new Civil Code does not specify what exactly is meant by the "agreement on out-of-court negotiations", but it

is perfectly safe to assume that a mediation agreement pursuant to the Mediation Act (act No. 202/2012 Coll.) would suffice, as would an agreement in which the creditor and the debtor unambiguously declare their desire to resolve their dispute out of court.

Also, the limitation period will newly be stayed for as long as the creditor was prevented from asserting their right due to threats, and for as long as the creditor did not assert their right due to having been misled by the debtor (or a person close to the debtor - Sec. 650). Nor does the statute of limitations apply during the presence of force majeure, if such a state prevented the creditor from asserting their right during the past six months of the limitation period (Sec. 651).

While the new Civil Code largely adopts and preserves current law when it comes to the statute of limitations, it also introduces a number of interesting novelties, the most appealing of which appears to us to be the optional character of the limitation period's duration, which adds to the parties' freedom of contract.

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## Legal News in Brief

- The Chamber of Deputies will debate a bill (chamber document no. 740) which should enshrine a **contracts register** in Czech law as a publicly accessible list of mandatorily disclosed contracts or the identification data on designated entities' contracts (for example state authorities and local self-government units). Mandatorily disclosed contracts should come into force on the day after they are published unless the parties to them arrange a later date. The law should come into effect on the first day of the second calendar month after its date of publication.
- The Chamber of Deputies will debate a bill which should **terminate certificated bearer shares** (chamber document no. 742). According to the bill, if a company did not convene a general meeting which would decide on a change of manner (i.e. to certificated registered shares) or form (i.e. to uncertificated bearer shares) by 30.6.2013, then a fiction would be used that on 30.6.2013 the general meeting decided to change the manner from certificated bearer shares to certificated registered shares. The main aim is to ensure greater transparency of the ownership structure of joint stock companies. It is proposed that the act will come into effect 15 days after publication. The bill should be submitted alongside a bill on certain measures to increase the transparency of joint stock companies (chamber document no. 715) which will also make certificated bearer shares no longer permissible (unless they are immobilised).
- The Chamber of Deputies has also received the **new Cadastral Act** (chamber document no. 778) which should respect the adjustment to the new Civil Code effective from 1st January 2014.
- The Chamber of Deputies will also address an amendment to the Commercial Code **limiting the period for the payment of invoices** (chamber document no. 711). The basic maturity period should become 30 days, including for public authorities. By mutual agreement it will be possible to extend the period to 60 days for deliveries of goods or services to a public authority which in the case of state administrative authorities must be justified by the nature of the obligation. Private entities can extend the maturity period to more than 60 days but this must not be grossly unfair to the creditor. The law shall come into effect on 1st March 2013.
- The government has approved the analysis of ways of adjusting the commercial register in the new **Registry Act**. The bill provides, inter alia, a partial modification of the existing administration model used by the registry courts, by enshrining the option for notaries to make direct entries in the commercial register in clearly defined cases or to register associations. The government has also instructed the minister of justice, in cooperation with the minister of interior, to draft a bill on the public registry of legal entities.

## → Current Events at bnt Prague

**SAVE THE DATE: For the fourth time already, bnt | attorneys-at-law invites you cordially to the EXPO REAL**

**The International Trade Fair for Commercial Property and Investment takes place in Munich from 8 October to 10 October 2012. Please come to Hall C1 – booth No. 031 – to visit the stand of bnt!**

Following a dear tradition, Munich will again be hosting the International Trade Fair for Commercial Property and Investment, one of the largest B2B trade fairs of its kind. Almost 1,600 exhibitors from all corners of the world present their real estate portfolio on altogether 64,000 square meters of exhibition space within the halls of the München Messe fairground. The list of participants reads like a cross-section of the industry and is testimony to the great variety of the field: project developers and managers, investors, financial advisors, consultants, architects, planners, construction companies, and representatives of municipalities and regions. The three-day event, which takes place in the wake of the Oktoberfest, is enriched by a variety of individually programmed conferences, forums, and panel discussions on the latest trends and innovations in real estate, investments, and financial markets.



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Visitors with a valid ticket to the trade fair have free entry to all these accompanying events. For more information, please visit the organizers' website: [www.exporeal.com](http://www.exporeal.com).

Throughout the trade fair, the stand of bnt | attorneys-at-law will be staffed by partners and lawyers from the various offices within the bnt network in order to accommodate visitors' wishes and requests. Aside from expert advice, those who alight at our stand will also be treated to two very special industry surveys: the ATLASSES FOR INVESTORS evaluate the legal environment across Central and Eastern Europe and provide a nifty, intuitive comparison between the individual countries in which bnt maintains a presence. Our unique survey from 2011/2012 allowed us to create region-wide guides to the areas of real estate and real-estate financing. These publications are available in an English and a German version.

Would you like to arrange for a personal meeting with a specific lawyer of bnt | attorneys-at-law? Just drop us a line, at [eliska.fucikova@bnt.eu](mailto:eliska.fucikova@bnt.eu).

We are looking forward to meeting you in person, on the floor of the communication platform that is this year's EXPO REAL!

### **Announcing our symposium on the recodification of Czech private law – only two months left until the event**

Following years of arduous efforts by the Ministry of Justice, the Czech lawmaker, and the legal community, the new Civil Code is finally taking concrete shape. In tandem with the new Act on Corporations and on Private International Law, it provides a modern legislative framework for our times within which private-law relations play out. The principal virtues of the new Czech private law include the greater stress which will now be put on personality rights and the principle of freedom of choice, and the uniform design of the law of obligations.



bnt | attorneys-at-law and the Institute for International Research have cooperated to organize a symposium for you, „**The Recodification of Law**“, which will take place on **6–7 November 2012** at the Park Inn Hotel in Prague. Join us to find out, among other things, how the legal standing of private individuals (natural persons) and legal entities has changed or what the new concept of corporate holdings entails. Would you like to find out in advance about the fundamental changes with which joint-stock companies will be confronted, and how limited liability companies will be affected by the new law? What are the differences between the monist and dualist model of corporate governance? Don't wait until you are caught off-guard by the surprises which the changes of terminology in contract law hold in store for you, but prepare even now for future amendments in this field! Make room in your planner and make use of the opportunity to meet the architects of new Czech private law in the flesh and exchange thoughts and ideas with them.

You also do not want to miss our workshop „**Incorporation and governance of companies under the new Civil Code**“, scheduled for 8 November 2012, in which you'll learn all the essentials regarding the business operations of limited liability companies and joint-stock companies pursuant to the new civil law.

While you are at it, maybe pencil in the dates for these subsequent expert seminars as well:

**Joint-Stock Companies after the Recodification:** 4–5 December 2012

**Contractual Law after the Recodification:** 11–12 December 2012

We are looking forward to meeting you in person! For additional information, please visit <http://www.konference.cz/akce/detail-2597-Rekodifikace-prava/>.



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