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LEGAL UPDATE

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An End to Bearer Share Certificates in the Czech Republic

The information in this newsletter is correct to the best of our knowledge and belief at the time of going to press. Specific advice should be sought, however, before investment and other decisions are made.

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NEW LEGISLATION

AN END TO BEARER SHARE CERTIFICATES IN THE CZECH REPUBLIC

On 31 May, 2013, Act No. 134/2013 Coll. **on certain measures to increase the transparency of joint stock companies** and on the amending of other laws entered into force. The regulation will become effective on 20 June.

The aim of the Act is to ensure shareholder traceability by banning the issue of bearer shares. The Act also lays down the procedure and deadlines for transforming existing bearer share certificates.

According to the explanatory report, the proposed amendment will apply to some 80% of joint stock companies, i.e. roughly 13,000 JSCs that have issued bearer shares.

WHAT ARE BEARER SHARES?

In contrast to registered shares, bearer share certificates, often called "anonymous shares", do not include the name of their owner. At the same time, this owner, in contrast to book-entry bearer shares, is not entered in any public register. Moreover, bearer share certificates may be transferred by mere physical conveyance from hand to hand with no need to record such transfer and thus enable the traceability of these shares' owners, as is necessary in the case of book-entry bearer shares.

CHANGES UNDER THE NEW LEGISLATION

A key innovation is that a company wishing to maintain its bearer shares will have to choose one of the following options:

- have the shares book-entered (registration with the Central Depository) or immobilised (kept at a bank), or

- cease to have bearer shares and switch to registered shares.

Companies that have issued bearer share certificates will have to choose one of these options **by 31 December, 2013**.

The bearer share certificates of companies that fail to make this choice will (without exception) become registered shares at 1 January, 2014; the corresponding change in the company Articles of Association will also occur at this date.

The Act sets the following deadlines in connection with the ban on the issue of bearer share certificates:

- **by 30 March, 2014**, a company is obliged to invite shareholders to exchange shares,
- **by 30 June, 2014**, shareholders are obliged to surrender bearer shares for exchange and
- **by 30 June, 2014**, the Board of Directors is obliged to effect a change in the share form entered in the Commercial Register.

The penalty for failure to fulfil the shareholder obligation to submit shares to a company to be furnished with the relevant changes or for exchange is **loss of all rights attached to these shares** for the period of the delay in submitting the shares. In such a case, these shareholders may not vote at the General Meeting, cannot be paid dividends, do not have the right to a share in a liquidation balance and, in the case of minority shareholders, cannot exercise special protected minority rights, e.g. to request the convocation of an extraordinary General Meeting or request a review of the Board of Directors' performance.



RELATED AMENDMENTS

The new legislation is associated with related Commercial Code, Securities Act and Capital Market Act amendments.

- Of particular note among the *Commercial Code* changes are the mandatory Commercial Register entry of specific information about the financial institution at which bearer shares are suspended and the related restriction of the issue of shares to just three types: immobilised bearer share certificates, book-entry bearer shares or registered shares.

Information on share suspension will become an essential requirement in the Articles of Association.

If a company has issued registered share certificates, the list of shareholders shall have to include the shareholders' bank accounts to which the company pays any dividends or other sums arising out of the shareholders' participation in the company.

Another new provision allows a shareholder of a company that has not yet issued shares to transfer its interest in the company under an agreement on the transfer of an equity investment. A joint stock company that has not yet issued shares is newly obliged to keep a list of shareholders.

Transitional provisions provide an obligation of shareholders of existing companies with registered share certificates to provide joint stock companies with a bank account

number for payment sums that may be due to such shareholders. The deadline by which such shareholders must act is the date of the first General Meeting to take place after the Act becomes effective.

Shareholders shall be informed of this obligation in the General Meeting invitation. In the meantime, payments of sums due to shareholders will be effected under existing regulations.

- A key *Securities Act* change is an amendment concerning collective share certificates, adopted in order to facilitate suspension by replacing an entire share issue with one collective share certificate. Another related change is the requirement to keep a separate register for the custody of suspended shares.
- Changes to the *Capital Markets Act* pertain to the suspension of already issued shares. At the same time, a rule is imposed explicitly stating that if a General Meeting decides to change bearer share certificates to book-entry, but an owner of shares fails to provide the number of the account on which the shares are to be recorded, such shares will be deemed as undelivered.

RELATIONSHIP BETWEEN THE NEW TRANSPARENCY ACT AND THE BUSINESS CORPORATIONS ACT

An amendment of Act No. 90/2012 Coll. on business corporations (the "BCA") that enters into force on 1 January, 2014 must be borne in mind in connection with the

Transparency Act. The BCA assumes the only shares in certificated form that joint stock companies will be able to have are registered shares. If they decide to have bearer shares, the Act imposes the obligation to suspend them or have them book-entered at the Central Depository.

The reason for the adoption of a separate Act (on certain measures to increase the transparency of joint stock companies) is primarily the fact that the legislation will in this way be independent of the rules set out in the BCA. The Act has been drafted so as to be applicable both in the case of BCA effectiveness and in the event the BCA, for any reason, does not enter into effect at 1 January, 2014.

The date at which bearer share certificates will be deemed registered share certificates in the Transparency Act is fixed at 1 January, 2014, i.e. the effective date of the BCA. Joint stock companies can make the relevant changes to their Articles of Association after this date, and these changes can thus be connected with the changes required of joint stock companies in the transitional provisions of § 777(2) of the BCA.

Finally, another reason for addressing the ban on bearer share certificates, which is set out in the explanatory report accompanying the Transparency Act, is the opinion put forward by its submitter that the transformation of joint stock companies with bearer share certificates cannot be implemented based on the BCA alone, as the law lacks explicit rules for changing shares and for how to proceed if shareholders fail to submit their bearer share certificates.

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