



**HAVEL & PARTNERS**

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# **A BRIEF GUIDE ON**

THE OFFICE OF A MEMBER OF THE STATUTORY  
BODY OF A BUSINESS CORPORATION  
| EXECUTIVE DIRECTOR



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# INTRODUCTION

Dear Executive Directors, Clients, and Business Partners,

In our many years of experience in the legal profession, we understand that regardless of the size or line of business of a company, all executive directors face a range of duties and corresponding responsibilities.

Our team specialising in corporate law has been partnering with statutory bodies for more than twenty years. In addition to day-to-day assistance with the preparation of all types of corporate documents and analyses of related duties, we have long provided practical training and other consultancy advice to clearly explain the functioning of statutory bodies.

It is precisely because of the considerable complexity and comprehensiveness of the regulation of the duties of statutory body members that we have decided to prepare this brief guide. Its aim is to provide a clear and one-stop overview of the functioning of statutory bodies, the duty of due managerial care, control mechanisms, concerns, profit distribution and other basic attributes that every executive director encounters. Finally, we add a very simple calendar of corporate obligations that statutory body members face each year.

Whether you are a newly elected or an experienced member of a statutory body, we hope this guide will make it easier for you to perform your office.

On behalf of the whole team, we wish you the most successful period while performing your office!

**David Neveselý & Ondřej Florián**

*partners responsible for the corporate law team*

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# COMMENCEMENT AND TERMINATION OF OFFICE

The office of an executive director is commenced upon election, i.e., upon the effectiveness of a resolution of (typically) the general meeting or the sole shareholder. However, the resolution may also determine a later date of the commencement of the office. Thus, the office is not commenced by an act of the entry into the Commercial Register.

In a limited liability company, the statutory body consists of one or more executive directors. The memorandum of association may state that they shall form a collective body if the company has more than one executive director. Implications of this situation will be discussed in more detail below.

The office of the executive director may be terminated in several ways. An executive director may resign from his/her office on his/her initiative. In such a case, the office terminates on the date on which the resignation is discussed by the body that elected the executive director unless otherwise provided in the memorandum of association. An executive director may also be expelled by the court (see p. 14 for more details).

Last but not least, an executive director may also be recalled by the supreme body (the general meeting or the sole shareholder) or by another body that appointed him/her to the office. In this case, too, the removal becomes effective upon the adoption of the resolution. As in the case of commencement of the office, the resolution to recall the executive director from the office may also determine a later effective date.

Executive directors do not have a statutory term of the office upon expiry of which their office would terminate. Nevertheless, we recommend executive directors check whether their term of office is stated in the memorandum of association or in their agreements on performance of the office.



# CHANGE IN THE TERM OF OFFICE

If the term of office of the executive director is determined in the memorandum of association (as its length is not determined by law) and it is changed by a decision of the supreme body, such change may also affect the term of office of the current executive director.

If the change introduces a longer term of office, the term of office of the serving executive director will also be extended; however, the executive director must consent to this as well as at the time of their election, otherwise the extension of the term of office does not apply to them. No specific form is needed for the consent; hence, implied consent is sufficient.

Analogically, if the term of office is shortened, the current term of office will also be shortened. However, if the term of office is shortened to such an extent that the period for which the executive director has already served precedes it, the decision will result in the recall of the executive director from their office. In case of such shortening, the executive director will be recalled from the office upon the date of effect of the decision at the earliest. The office of an executive director may not be terminated retroactively.

When changing the term of office of executive directors, it is therefore always necessary to consider the impact of the change on the current situation and, if necessary, to take into account the term of office of the current executive directors in the decision to change the memorandum of association.

# ACTIVITIES OF THE STATUTORY BODY

## Business management

The statutory body is responsible for the business management of the company. However, the law does not provide for a definition of the term “business management”. The answer to the question of what is meant by business management has been provided only by the Supreme Court's decision-making practice. The Supreme Court has concluded that business management means the organisation and management of the company's day-to-day business activities, in particular decisions on the operation of the company's business and related internal affairs of the company. According to the Supreme Court, it is irrelevant whether the business activities are carried out by executive directors as a collective body or an independent executive director, or by a third party authorised by the statutory body.

Simply put, business management is the day-to-day decision-making about the performance of the company's business activities.

It is essential that business management is the exclusive scope of the powers of an executive director. No one may give instructions to the executive director regarding business management (i.e., not even the general meeting or the sole shareholding) and the executive director should not comply with such instructions without his/her discretion. The exceptions are the formal request for giving an instruction sent by the statutory body to the general meeting (or the sole shareholder) and the so-called concern instructions.

**NO ONE MAY GIVE  
INSTRUCTIONS TO THE  
EXECUTIVE DIRECTOR  
REGARDING BUSINESS  
MANAGEMENT.**

A formal request for an instruction on the business management does not fully discharge a statutory body member of his/her duty to act with due managerial care in its entirety. The concern instructions are discussed in detail on p. 19. By law, executive directors decide on business management by a majority, even in cases where they do not form a collective body.

## Representation of the company

The process of representation of the company can be divided into two basic phases, namely (i) the phase in which the will of the company is formed, and (ii) the phase in which such will materializes into a specific act on behalf of the company.

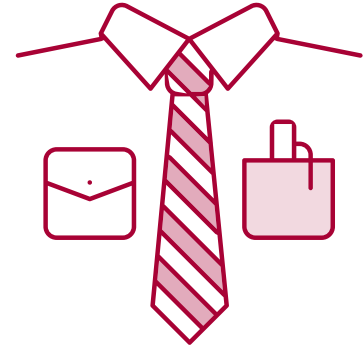
## Formation of will

The will as to how to act on behalf of the company is formed within the statutory body. The act itself is, in principle, only the implementation of the decision of the statutory body. In business management matters, executive directors decide by a majority regardless of whether they form a collective body (of course, if there is more than one of them in the company). Executive directors should keep thorough records of their decisions and archive them. In case their potential liability for damage is assessed, the archiving of relevant records may typically be the very thing that will enable executive directors to demonstrate that they have acted with due managerial care.

As a rule, it will be an executive director in the position of a defendant who will bear the burden of proof. Thorough archiving may thus save executive directors from being held liable for the damage caused, as they might not otherwise be able to prove that their actions were correct.

**“**  
**IN BUSINESS  
MANAGEMENT  
MATTERS, EXECUTIVE  
DIRECTORS DECIDE  
BY A MAJORITY  
REGARDLESS OF  
WHETHER THEY FORM  
A COLLECTIVE BODY.**

“**THOROUGH ARCHIVING  
OF DECISIONS OF  
EXECUTIVE DIRECTORS  
MAY SAVE THEM FROM  
A POTENTIAL OBLIGATION  
TO COMPENSATE FOR  
DAMAGE.**”



## Acting on behalf of the company

Acting on behalf of the company means the acting of authorised persons on behalf and for the account of the company in legal relations with third parties – acting vis-a-vis third parties. The basic rule of acting on behalf of the company is that each executive director is authorized to represent the company individually.

However, the specific manner of acting must always be in accordance with the manner of acting entered in the Commercial Register.

The memorandum of association may provide for the manner of representation of the company in different ways. One such option may be, for example, the two-man rule, when at least two executive directors must act jointly on behalf of the company.

In some cases, the manner of representation of the company is provided directly by law. For example, in civil court proceedings, the company is represented by one executive director.





## Acting contrary to the above

What is relevant is whether there has been an act contrary to the will-forming process or contrary to the rules of acting on behalf of the company. If an executive director has acted on behalf of the company without a prior decision of the statutory body, this may constitute a breach of the duty of due managerial care.

However, if an executive director acts in a manner contrary to the manner of acting on behalf of the company, it is possible that he/she will be bound by such an action instead of the company. The company will thus not be bound at all and will not, for example, be obliged to perform under the contract. However, the company may also approve such an action without undue delay (typically by correcting the originally incorrect manner of its representation).

**FOR THESE REASONS,  
OUR CLIENTS USE OUR  
SERVICES, WHICH  
CONSIST NOT ONLY  
OF THE CORRECT AND  
COMPLETE PREPARATION  
OF DOCUMENTS BUT ALSO  
OF ARCHIVING THEM AND  
MAINTAINING A FILE OF  
DECISIONS OF EXECUTIVE  
DIRECTORS, WHETHER  
IN PHYSICAL OR SECURE  
ELECTRONIC FORM.**

**WE OFFER A COMBINATION OF COMPREHENSIVE CONSULTING IN WHICH WE WILL PREPARE YOU FOR THE GENERAL MEETING, COMPLETELY ORGANISE IT FROM THE PREPARATION STAGE, THROUGH THE DRAFTING OF THE INVITATION TO THE ACTUAL IMPLEMENTATION OF THE GENERAL MEETING AND, IF NECESSARY, DEFEND AND JUSTIFY THE GENERAL MEETING IN COURT. WE INCORPORATE MODERN TECHNOLOGY AND THE STATE-OF-THE-ART PROCEDURES IN CONDUCTING GENERAL MEETINGS – BE IT VARIOUS TECHNICAL TOOLS, DIGITISATION OF THE ENTIRE GENERAL MEETING AND DECISION-MAKING OUTSIDE THE GENERAL MEETING (ESPECIALLY IN THE FORM OF PER ROLLAM), ALL UNDER THE GUIDANCE OF AN EXPERIENCED ATTORNEY.**

## **ORGANISATION OF GENERAL MEETINGS**

Every company has to hold a general meeting at least once a year. The general meeting can, however, become an easy tool used to abuse rights by anyone who has been given the opportunity through undue organisation and conduct of the general meeting. Only a duly organised and conducted general meeting will allow for proper “corporate life” and will also be able to succeed in a judicial review should any shareholder wish to apply for one.

The proper convocation and organisation of the general meeting is part of the executive director’s duty to act with due managerial care. We recommend not to underestimate the drafting of the invitation, the decision on the choice of the right venue and time for the general meeting, and the decision on the presence of persons at the general meeting to ensure its due course.

# AGREEMENT ON PERFORMANCE OF OFFICE, REMUNERATION

All performance by a limited liability company for the benefit of an executive director for the performance of his/her office must be provided under an agreement on the performance of the office concluded between the company and the executive director and with the consent of the general meeting or the sole shareholder.

## Agreement on performance of office

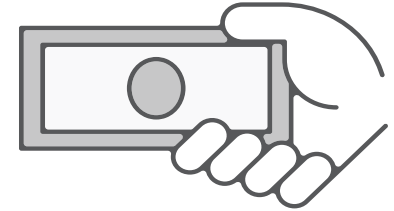
An agreement on the performance of the office is a contractual relationship between the company and an executive director. It provides for the rights and obligations of the parties. Primarily, it may serve to specify certain obligations of an executive director, the manner of performance of his/her office, but also to provide for the manner and amount of remuneration of the executive director for the performance of his/her office.

It is not an employment agreement and the conclusion of the agreement on the performance of the office does not establish an employment relationship. Therefore, the employment law principles do not automatically apply here. However, certain rules typical for the employment relationship may be expressly provided (e.g., severance pay, certain benefits, etc.).

The agreement on the performance of the office must be in writing. It is approved by the company's supreme body. If not approved, the performance of the office is for no consideration. The agreement on the performance of the office may be approved both before and after its conclusion. However, until approval, an executive director is not legally entitled to remuneration.

“  
**ALL REMUNERATION  
PAYMENTS SHOULD  
BE SPECIFIED IN THE  
APPROVED AGREEMENT  
ON THE PERFORMANCE  
OF THE OFFICE.  
OTHERWISE, THIS  
COULD CONSTITUTE THE  
UNJUST ENRICHMENT  
OF AN EXECUTIVE  
DIRECTOR.**

**CLIENTS ARE ADVISED TO NOT UNDERESTIMATE THE AREA OF REMUNERATION AND CONCURRENCE OF FUNCTIONS. THE AGREEMENT ON THE PERFORMANCE OF THE OFFICE IS A KEY DOCUMENT WITH MANY BENEFITS FOR THE BODY MEMBER. OUR MANY YEARS OF EXPERIENCE ENABLE US TO THOROUGHLY AND CORRECTLY SET UP THE MUTUAL RELATIONS BETWEEN THE COMPANY AND AN EXECUTIVE DIRECTOR OR TO THOROUGHLY REVISE THE ALREADY SET RELATIONS. THIS PROVIDES SUFFICIENT LEGAL CERTAINTY FOR BOTH PARTIES, WHO THUS AVOID THE RISK OF LATER LITIGATION, E.G., OVER THE SCOPE OF BENEFITS DRAWN OR THE SCOPE OF THE DUTIES OF A MEMBER OF THE ELECTED BODY.**



## Remuneration

Any remuneration payments that an executive director receives from the company for the performance of his/her office should be specified in the approved agreement on the performance of the office or, at the very least, should be approved by the body approving the agreement on the performance of the office. Otherwise, this could constitute the unjust enrichment of an executive director. The company could (and, according to law, must) then enforce such payments back from the executive director.

For these purposes, remuneration is considered to be any benefit, whether monetary or non-monetary, received by an executive director from the company in connection with the performance of his/her office. This may be a fixed monthly remuneration payment (similar to a wage or salary), but also the provision of a company car or telephone for private purposes, various types of insurance and supplementary insurance, a possible share in the company, e.g., through a managerial programme, a profit share, participation securities or enabling their acquisition by an executive director or a person close to him/her, etc.

## ESOP as another remuneration option

One of the alternatives and a possible addition to the remuneration of an executive director in a company is the introduction of a management incentive plan (ESOP, i.e. Employee Stock Option Plan).

The creation of an appropriately set management programme provides increased motivation for executive directors in an effort to steadily increase the performance of the entire company. With the right ESOP setup, an executive director is primarily motivated to ensure that in the long run, the company achieves good and steady results, as opposed to unsustainable short-term growth that can, on the contrary, deplete the company.

A management programme can take various forms, from the provision of a management bonus set on the basis of the fulfilment of given criteria under the service agreement, through the issue of innominate securities ensuring, for example, the possibility of obtaining a share in the company's profits, to the option of acquiring an ownership interest in the company if predefined conditions are met.

There are many different approaches to implementing a management programme and the specific approach is always selected based on the individual case. Nowadays, management programmes have definitely become a standard part of managing the executive directors, as well as their expectations and their remuneration.

**BY PROPERLY SETTING UP A MANAGEMENT INCENTIVE PLAN, MANAGERS ARE MOTIVATED IN A WAY THAT LEADS TO ENHANCED PERFORMANCE OF THE ENTIRE COMPANY. THIS IS SUCH A CRUCIAL STEP IN THE LIFE OF A CORPORATION THAT SIMPLE BOILERPLATE SOLUTIONS CANNOT BE APPLIED. WE TEND TO LOOK FOR TAILOR-MADE SOLUTIONS FOR OUR CLIENTS, WHICH WE HAVE TESTED IN OVER 20 YEARS OF OUR PRACTICE, NOT ONLY IN COOPERATION WITH OUR CLIENTS, BUT ALSO ON OURSELVES.**

“**THAT THE OFFICE IS FOR NO CONSIDERATION DOES NOT EXHAUST THE RISKS. CASE LAW HAS ALSO DEALT WITH CASES WHERE UPON ELECTION TO THE STATUTORY BODY THE CONCURRENT EMPLOYMENT AGREEMENT WAS IMPLICITLY TERMINATED, ITS EFFECTIVENESS WAS INTERRUPTED, ETC. IT IS, THEREFORE, NECESSARY TO EXAMINE EACH CASE INDIVIDUALLY.**”

## Concurrence of functions

When performing the office of an executive director, care must be taken to avoid the so-called prohibited concurrence of functions. This means a situation where an executive director has concluded an employment agreement for a position which job description overlaps with the description of the office of the executive director.

Typically, this situation can arise in positions such as sales director, CEO or CFO, etc. However, the specific job description of the position must always be assessed.

Such a situation is undesirable. The office of an executive director cannot be performed under an employment relationship. In addition, as the employment agreement will generally not be approved by the general meeting or the sole shareholder in these cases, the performance of the office will often be for no consideration.

That the office is for no consideration does not exhaust the risks. Case law has also dealt with cases where upon election to the statutory body the concurrent employment agreement was implicitly terminated, its effectiveness was interrupted, etc. Difficulties may also arise with the correct determination of health and social insurance premiums. It is, therefore, necessary to examine each case individually.

However, it is not excluded that a member of the statutory body has concluded an agreement on performance of the office and at the same time an employment agreement for performance of his/her work activities which will not overlap with the office of an executive director in terms of content.

Therefore, we recommend that upon election to the office of a member of the statutory body, an agreement on performance of the office be concluded, and the existing employment relationship (if any) be appropriately modified according to the will of both parties.

# DUTIES OF A MEMBER OF THE STATUTORY BODY

When performing his/her office, an executive director has many various duties, but the most specific of these, and probably the most important for the executive director, is the duty to act with due managerial care.

## Duty to act with due managerial care

Due managerial care means that a member of the statutory body must act with the necessary loyalty and care and always act on an informed basis and in the defensible interests of the company when taking business decisions.

In this regime, an executive director is not evaluated for the outcome but for the effort. It, therefore, depends on whether he/she has acted loyally, diligently, on an informed basis, and in the interests of the company. If the answer is positive (and, as the case may be, the executive director can prove that these criteria are met in court), he/she will not be liable for the damage caused.

Due managerial care is a comprehensive concept that cannot be fully explained in a short paragraph. In general, however, concerning loyalty, an executive director should always put the interests of the company before those of the shareholders or even his/her interests. As far as expertise, in general, is concerned, an executive director does not have to be an expert in every conceivable field, but he/she must make the right judgment as to when it is appropriate to call for expert assistance.

**“AN EXECUTIVE DIRECTOR DOES NOT HAVE TO BE AN EXPERT IN EVERY CONCEIVABLE FIELD, BUT HE/SHE MUST MAKE THE RIGHT JUDGMENT AS TO WHEN IT IS APPROPRIATE TO CALL FOR EXPERT ASSISTANCE.”**

**DUE MANAGERIAL CARE IS A VERY COMPREHENSIVE AND DIFFICULT TOPIC, BUT ONE THAT IS ABSOLUTELY ESSENTIAL TO THE PERFORMANCE OF THE OFFICE OF AN ELECTED BODY. TO THIS END, WE ORGANISE SEMINARS FOR CLIENTS TO EXPLAIN THE PRACTICAL ASPECTS OF THEIR DUTIES AND HOW TO DEAL WITH THE RISKS ARISING FROM THEIR OFFICE.**

## **Sanctioning mechanisms related to due managerial care**

If an executive director breaches the duty of due managerial care, he/she must return to the company the benefit he/she has received thereby. If he/she causes any damage to the company by this breach of duty, he/she is obliged to compensate for it. If he/she fails to compensate for the damage caused, he/she may even be liable to the company's creditors for debts that they fail to recover from the company to the extent that the executive director has not compensated for the damage. Thus, persons outside the company may also claim certain performance from him/her.

The court may also prohibit a member of the statutory body from performing the office of a member of the statutory body for up to three years if he/she repeatedly or materially breaches his/her duties.

If a member of the statutory body contributes to the company's insolvency by breaching his/her duty, the court may order him/her to return the benefits received under the agreement on the performance of the office for up to two years in arrears and, in an extreme case, to pay debts up to the amount for which the company's existing assets are insufficient.

Similarly, the remuneration of an executive director may be reduced if he/she has contributed to the unfavourable profit or loss of the company by performing his/her office.

This basic list of consequences can then also be extended in the agreement on the performance of the office.



## Conflict of interest

When performing his/her office, an executive director may have a conflict between his/her interests and the company's interests. In general, the company's interests should prevail.

However, if he/she complies with the conflict-of-interest rules, he/she may, under certain conditions, also promote his/her interest at the expense of the company.

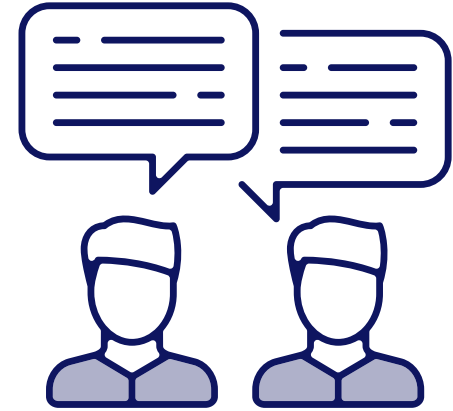
An executive director has a direct conflict of interest if he/she plans to enter into a contract with the company. In such a case, he/she is obliged to inform the other executive directors and the supervisory board, if any, otherwise the general meeting (the sole shareholder) in advance. The general meeting (the sole shareholder) may prohibit the conclusion of the agreement.

In other cases where there is not a direct conflict of interest, but an executive director has an indirect conflict of interest or becomes aware that a conflict of interest is imminent, he/she is also obliged to inform the other executive directors and the supervisory board, if any, otherwise the general meeting (the sole shareholder). The supervisory board is then obliged to inform the general meeting (the sole shareholder) about the conflict of interest of the executive director.

In response to a conflict of interest, the supervisory board or the general meeting (the sole shareholder) may in some cases suspend an executive director from performing his/her office or prohibit the conduct in question. Acts taken in a conflict of interest without meeting these conditions may be ineffective or bind the executive director himself/herself instead of the company.

**“IN GENERAL, AN EXECUTIVE DIRECTOR SHOULD PUT THE COMPANY'S INTERESTS FIRST. HOWEVER, IF HE/SHE COMPLIES WITH THE CONFLICT-OF-INTEREST RULES, HE/SHE MAY ALSO PROMOTE HIS/HER INTEREST TO**

**“AN EXECUTIVE DIRECTOR MAY REFUSE TO DISCLOSE INFORMATION ONLY IF SUCH INFORMATION IS CLASSIFIED OR PUBLICLY AVAILABLE (AND ALSO IN THE CASE OF AN ABUSIVE EXERCISE OF THAT RIGHT BY A SHAREHOLDER).”**



## **Obligations related to the shareholders' right to information**

When performing the office of a member of the statutory body, it must be taken into account that shareholders have certain rights to information, which are modified depending on the legal form of a company.

A shareholder of a limited liability company has the right to request information about the company, inspect documents, and check the data contained therein and other information specified in the memorandum of association. An executive director may refuse to disclose such information only if such information is classified or publicly available (also in the case of an abusive exercise of that right by a shareholder).

# BUSINESS GROUPS

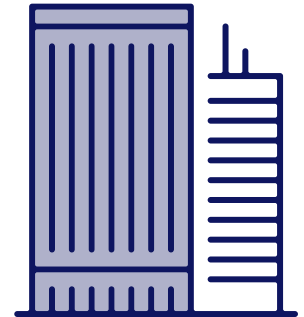
The issue of business groups is an integral part of the world of business corporations. It is important for an executive director to recognize whether and at what level of a group the corporation is. From this assessment, the executive director must normally draw the consequences for himself/herself and his/her duties. However, for all levels, the executive director is obliged to act with due managerial care.

The level of intensity of integration into a business group can be expressed as follows:

**NO  
GROUP**



**COMPLETE  
GROUP**



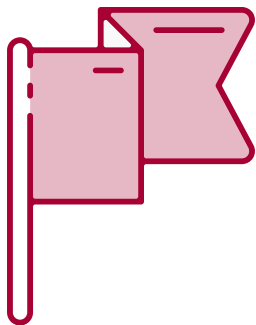
## Influence

In the first level of business groups, a distinction is made between influential and influenced entities. Both natural and legal persons may become influential entities. Only a business corporation may be an influenced entity. In this case, the main focus is the influence of the influenced entity in a decisive and significant manner. As the terms themselves suggest, this will often be a one-off influence. The hallmark of influence is factual completion, i.e., that the influence has already occurred. If the influence causes damage to the influenced entity, the influential entity is obliged to compensate the influenced entity for the damage. The influential entity may be exempted from this obligation under certain conditions, but on the other hand, it may also be liable to creditors for the damage caused.

The influential entity may be an entity with a direct share in voting rights, a beneficiary under shareholder agreements, but also, for example, a significant creditor, business partner, etc.

## Control

In the second level of business groups, the law distinguishes between controlling entities, which may be both natural and legal persons, and controlled entities, which may only be business corporations. A controlling entity is an entity that may exercise decisive influence in the company, e.g., a majority shareholder. Unlike influence, the mere potentiality of such a state is sufficient to fulfil the characteristics of control. That is, the controlling entity may directly or indirectly exercise decisive influence in the business corporation. The statutory body of the controlled entity must prepare, inter alia, a report on relations in which the control is specifically described.



## Concern

A concern does not have a legal personality and therefore cannot have rights and obligations under Czech law. Also, in this case, there are two types of entities, namely, dependant entities and dominant entities. A concern is established where the dependant entity (or more than one such entity) is subject to single management by the dominant entity or entities.

The advantage of the existence of a concern is the potential to discharge oneself of the obligation to compensate for damage caused by an executive director and the possibility of the dominant entity to give instructions to the executive director regarding business management (and, within those instructions, to discharge itself of liability for damage).

## Discharging itself of the obligation to compensate for damage

In order for the dominant entity to discharge itself of the obligation to compensate the dependant entity for damage, the following formal requirements must be met:

- concern affiliation is published on the website;
- the damage has occurred in the interest of the concern;
- the damage has been or will be adequately compensated within the concern within a reasonable period of time;
- no insolvency of the dependant entity will occur as a result of the actions of the dominant entity toward the dependant entity.

**CLIENTS ARE ADVISED TO FAMILIARISE THEMSELVES THOROUGHLY WITH THE CONCERN LAW REGULATION. THE ASSESSMENT OF THE POSSIBILITY TO CARRY OUT AN INSTRUCTION AND THE POTENTIAL LIABILITY FOR CARRYING IT OUT MAY HAVE SIGNIFICANT CONSEQUENCES FOR AN EXECUTIVE DIRECTOR.**

**ALTHOUGH AN EXECUTIVE DIRECTOR OF THE CONTROLLED ENTITY IS OBLIGED TO PREPARE A REPORT ON RELATIONS WITHIN THREE MONTHS, OUR PRACTICAL EXPERIENCE IS THAT EXECUTIVE DIRECTORS OF MANY COMPANIES NEGLECT THIS OBLIGATION.**

## **Instructions regarding business management within the concern**

The body of the dominant entity may give instructions regarding business management to the bodies of the dependant entity if such instructions are in the interest of the concern. However, such an instruction regarding business management does not discharge a member of the statutory body of the obligation to act with due managerial care.

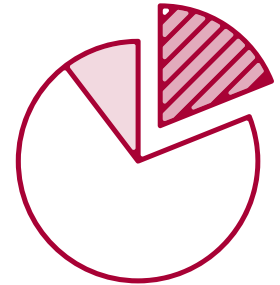
However, an executive director of the dependant entity may discharge himself/herself of liability for damage if he/she proves that the requirements for giving a concern instruction have been met and at the same time that he/she could have reasonably foreseen that any damage to the dependant entity resulting from the instruction would be settled within the concern. In doing so, there must be circumstances for which the executive director reasonably believes that the damage will be settled with adequate consideration and within a reasonable period of time.

## **Report on relations**

An executive director of a limited liability company that is the controlled entity is legally obliged to prepare a written report on relations within three months of the end of an accounting period.

The report on relations will include, as a minimum, the structure of the relations between the controlling entity and the controlled entity, the role of the controlled entity within those relations, the manner and means of control, an overview of the acts taken in the last accounting period in which the controlling entity was involved, an overview of the contracts concluded between the controlled entity and the controlling entity, and an assessment of the advantages and disadvantages of control. If the company prepares an annual report, the report on relations is part of it and is subject to audit.

# DISTRIBUTION OF THE COMPANY'S PROFIT



Making a profit is usually the primary objective of establishing a limited liability company. However, there are rules for its distribution that an executive director should know and follow. This is primarily because it is ultimately the executive director who decides on the actual payment of a profit share to shareholders.

## Determination of the amount to be distributed

The law imposes the obligation to deposit in the Collection of Deeds the proposals of an executive director on the disposal of the company's profit or loss. This should be submitted by executive directors to the general meeting (the shareholder), and as early as at this stage executive directors should already know what amount of the profit or loss they can dispose of and how.

To that end, the law prescribes the obligation to draw up financial statements, which must be submitted to the general meeting for approval within six months of the end of the accounting period. Furthermore, the law contains several "capital tests", which should be applied by an executive director to determine the maximum amount he/she can propose to be distributed as a profit share.

## Non-distribution of profits to shareholders and earmarked funds

Although the right to a dividend is one of the fundamental rights of shareholders, shareholders are not automatically entitled to it. Especially in a limited liability company, it does not necessarily follow that the company must, in principle, distribute the generated profit among its shareholders. A limited liability company as a legal form of a capital company thus allows a slightly more benevolent approach in this respect than a joint-stock company.

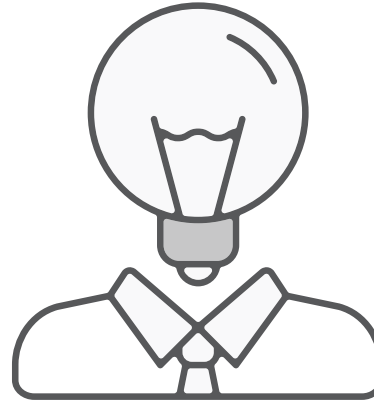
A limited liability company does not have an “obligation to distribute profits”. In case profit is not distributed, however, the company must ensure that voting rights are not abused to the detriment of the whole (in the case of joint stock companies, the shareholder’s right to a dividend is much stronger, i.e. joint-stock companies must distribute profits unless there are particular reasons for not doing so, or other special rules, typically laid down in the articles of association or in a special law).

The actual distribution of profits may be laid down in various ways in the memorandum of association. One possibility may be the distribution of profits or part thereof into an earmarked capital fund established by the memorandum of association. This is another situation where the profit (or its part) is not distributed to the shareholders while their right to profit has not been violated.

The provisions of the memorandum of association on the allocation of profits to the earmarked funds comply with the statutory conditions based on which the executive director may allocate profits to the earmarked fund only if the memorandum of association lays down the amount of money to be allocated to the earmarked fund, or specify the part of profits to be allocated to it, as well as the purpose for which the fund is established. Unless the memorandum of association contains the above rules, no profit may be allocated to such earmarked fund. Similarly, the memorandum of association must contain the rules for the allocation of profits to the fund and may not leave the decision up to the executive director.

The executive director should therefore always make sure whether the memorandum of association provides for the allocation of profits or part thereof to earmarked funds and how (if at all) this arrangement will affect the distribution of profits and other own resources to shareholders.





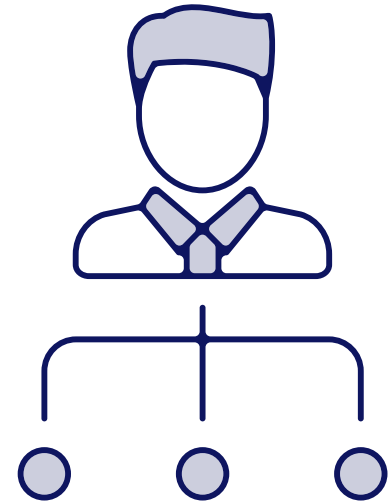
## Obligations before profit payment

As mentioned above, following the resolution of the general meeting (the shareholder) on profit distribution, it is up to the statutory body to assess whether to pay out the profit. Even within this decision, the statutory body must exercise a certain degree of discretion. First, an insolvency test must be prepared, and the company must not pay out a profit share if this would cause it to become insolvent.

As part of this phase, the statutory body should also consider whether it will pay out the profit less the withholding tax to each shareholder, and where and when it will send the relevant amounts. Even if the general meeting (the shareholder) has decided on the distribution of the profit, the statutory body is responsible for its final correct payment.

**SINCE THE FINAL  
PAYMENT OF PROFIT IS  
THE RESPONSIBILITY OF  
AN EXECUTIVE DIRECTOR,  
CLIENTS OFTEN USE OUR  
PROFESSIONAL SERVICES  
TO ENSURE THAT THE  
PAYMENT OF PROFIT IS IN  
COMPLIANCE WITH THE  
LAW.**

## REGISTER OF BENEFICIAL OWNERS



In particular, we would like to point out that the statutory body should also take care throughout the existence of the company to ensure that a correctly identified beneficial owner is entered in the Register of Beneficial Owners pursuant to the relevant statutory provisions.

In addition to various public law penalties that may also result from an incorrect entry in the Register of Beneficial Owners, the consequence is also a prohibition on the company to pay out a profit share to a person who should be registered as a beneficial owner or to a person who has not registered its beneficial owner. Such persons may not even exercise voting rights in the company.

“THE CONSEQUENCE OF AN INCORRECT ENTRY IN THE REGISTER OF BENEFICIAL OWNERS IS ALSO A PROHIBITION ON THE COMPANY TO PAY OUT A PROFIT SHARE

# CALENDAR OF CORPORATE OBLIGATIONS

OBLIGATION	EXPLANATION	FREQUENCY / NOTE	DEADLINE
<b>Preparation of financial statements</b>	The company is obliged to prepare a formal record of the financial activities carried out in the previous accounting period. The bodies are obliged to draw up the relevant business reports.	Once a year.	
<b>Filing a corporate income tax return</b>	Obligation to the tax office. Please note that the company may have multiple tax obligations.	Once a year.	3 months after the end of the tax period. 6 months in the case of the obligation to have the financial statements audited.
<b>Preparation of the report on relations</b>	The statutory body of the controlled entity will prepare a written report on relations.	Once a year.	3 months after the end of the accounting period.
<b>Convening a general meeting</b>	The statutory body is obliged to convene a general meeting at least once a year (to discuss the financial statements, see below).	At least once a year. However, the obligation to convene a general meeting may arise more frequently.	So that the financial statements can be discussed no later than 6 months after the end of the accounting period.
<b>Discussion of the annual financial statements</b>	The general meeting is obliged to discuss the financial statements.	Once a year.	6 months after the end of the accounting period.
<b>Disposal of the profit or loss</b>	The statutory body should annually propose how the profit or loss will be disposed of.	Once a year.	Depending on whether a general meeting is convened.

OBLIGATION	EXPLANATION	FREQUENCY / NOTE	DEADLINE
<b>Obligation to publish relevant corporate documentation</b>	The company is obliged to deposit the following documents in the Collection of Deeds:		Without undue delay.
	a) financial statements, unless they are part of the annual report;		Within 30 days of (i) the auditor's verification and upon (ii) approval of financial statements and of annual report by the relevant body.
	b) auditor's report on verification of financial statements;	Under the terms of the Accounting Act.	
	c) annual report;	Companies that are obliged to have their financial statements audited.	
	d) proposal for distribution of profit or other own resources or settlement of loss, and its final form, if not already included in the financial statements;		
	e) report on relations.	If the company is a controlled entity.	

OBLIGATION	EXPLANATION	FREQUENCY / NOTE	DEADLINE
	f) articles of association, any amendments thereto (each time a new consolidated version);	On a continuous basis.	
	g) decision on the appointment and removal of an executive director;		
	h) other documents which must be deposited in special cases.		
<b>Record keeping</b>	The statutory body is responsible to the company for the proper keeping and storage of accounting records. The company keeps the following records:		
	a) financial statements and annual report for 10 years;		
	b) accounting documents, ledgers, amortisation schedules, inventory lists, chart of accounts for a period of 5 years;		

OBLIGATION	EXPLANATION	FREQUENCY / NOTE	DEADLINE
	c) accounting records by which accounting units document the keeping of accounts, for a period of 5 years;		
	d) employee records;		
	e) tax records for a period of 3 years;		
	f) list of shareholders;		
	g) minutes of the sessions of the supreme body, including all annexes, for the entire period of its existence (+ after dissolution, if applicable);		
	h) other corporate records.		

# NOTICE

We hope that this guide has provided you with a useful basic overview of the selected rights, obligations, and rules that are relevant to the performance of the office of an executive director. Due to the complexity and comprehensiveness of the issue of the performance of the office of an executive director, we have limited ourselves to a very brief explanation of some related selected issues. The calendar of corporate obligations in this guide is just a basic list of all obligations. In fact, there will be many more obligations depending on the company's scope of business, its size, and other factors. This guide is not and cannot be a comprehensive legal opinion on the matter or legal advice on any of the areas discussed.

The areas described are only a brief summary of the issues involved. Nor can this guide be a substitute for legal advice on any particular matter covered in it. Moreover, each case must normally be assessed individually. We, therefore, recommend that you seek specific legal advice from a specialist in the relevant field. We are ready to assist you in this respect at any time.

This guide does not cover the business, technical, financial, or tax aspects of performing the office of a member of the statutory body.

This guide does not address the issue of the intertemporal aspects of individual obligations, risks, and claims. This guide has been prepared under Czech law and does not take into account the law of any other jurisdiction. If any issue indicated in this guide relates to any jurisdiction other than the Czech Republic, a qualified lawyer from the relevant jurisdiction should be consulted for specific advice. This guide is up-to-date reflecting the legal status effective as of 1 March 2024.

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