

Allen & Overy (Czech Republic) LLP,  
organizační složka

## CLIENT BRIEF

To ISDA CEE/SEE/CIS Committee

From Allen & Overy (Czech Republic) LLP, organizační složka

Our ref KLOCAL-0000143 KNO1: 59566.1

Date 3 April 2020

Subject **COVID-19 Update (Czech Republic) – Business as Usual for Derivatives and Similar Financial Transactions Following the Latest Legislative Proposals?**

The Czech government has approved and submitted to the Czech Parliament a set of new draft bills that are likely to affect a myriad of financing transactions on the Czech market. These legislative proposals have been scheduled for debate in the Czech Parliament on 7 April 2020 and can therefore become laws fairly quickly. We have prepared a summary of the most relevant upcoming changes relating to derivatives and similar financial transactions entered into with Czech counterparties under ISDA Master Agreements.

### 1. EXTRAORDINARY MORATORIUM AND RELATED AMENDMENTS TO CZECH INSOLVENCY LAWS

The Czech government has submitted to the Czech Parliament a draft bill containing temporary changes to the Czech insolvency regime aiming to mitigate the impact of various measures adopted in response to the COVID-19 pandemic.

In this context, the draft bill provides that any insolvency petitions filed by creditors of a Czech debtor until 31 August 2020 should be disregarded. Any such filings made until the end of August would have to be made again in September this year in order to effectively commence insolvency proceedings. This restriction applies to all creditors, including foreign creditors, of a Czech debtor (i.e., a debtor with its COMI in the Czech Republic).

#### 1.1 Extraordinary Moratorium

The draft bill creates a brand new and bespoke regime for Czech debtors. Until 31 August 2020, a Czech debtor, which was not insolvent as of 12 March 2020, can apply for an extraordinary moratorium for an initial period of three months. To that end, the Czech debtor will have to file a simple application form with, *inter alia*, an attached affidavit representing that:

- (a) the Czech debtor files the application due to impacts of the COVID-19 Extraordinary Measures\*;

Allen & Overy (Czech Republic) LLP is a limited liability partnership registered in England and Wales with registered number OC341967 and its registered office at One Bishops Square, London, E1 6AD, United Kingdom of Great Britain and Northern Ireland. A list of the members of Allen & Overy (Czech Republic) LLP is open to inspection at its registered office. Allen & Overy (Czech Republic) LLP je přidružená k Allen & Overy LLP, právnické osobě s ručením omezeným, zapsaná v Anglii a ve Walesu. Allen & Overy (Czech Republic) LLP je právnická osoba s ručením omezeným zapsaná v Anglii a ve Walesu pod registračním číslem OC341967 a se sídlem na adrese One Bishops Square, Londýn E1 6AD, Spojené království Velké Británie a Severního Irsku. Seznam společníků Allen & Overy (Czech Republic) LLP je k nahlédnutí v sídle společnosti.

Allen & Overy (Czech Republic) LLP, organizační složka is registered in the Commercial Register administered by the Municipal Court in Prague, Section A, File no. 64194, Identification no. 28507436. Allen & Overy (Czech Republic) LLP, organizační složka, je zapsána v obchodním rejstříku vedeném Městským soudem v Praze, oddíl A, vložka 64194, IČ 28507436. Allen & Overy LLP or an affiliated undertaking has an office in each of: Abu Dhabi, Amsterdam, Antwerp, Bangkok, Barcelona, Beijing, Belfast, Bratislava, Brussels, Budapest, Casablanca, Dubai, Düsseldorf, Frankfurt, Hamburg, Hanoi, Ho Chi Minh City, Hong Kong, Istanbul, Jakarta (associated office), Johannesburg, London, Luxembourg, Madrid, Milan, Moscow, Munich, New York, Paris, Perth, Prague, Riyadh (cooperation office), Rome, São Paulo, Seoul, Shanghai, Singapore, Sydney, Tokyo, Warsaw, Washington, D.C. and Yangon.

- (b) the Czech debtor was not insolvent as of 12 March 2020; and
- (c) the Czech debtor had not paid out any extraordinary funds to its shareholders, members of its bodies or its group members, unless such extraordinary payments were returned.

\*The draft bill defines the **COVID-19 Extraordinary Measures** rather broadly. It covers any measure declared by the Czech government or a measure declared by the Czech Ministry of Health or by a Czech Regional Public Health Station in the Czech Republic relating to public health protection and COVID-19 spread limitation.

It will be possible to extend the extraordinary moratorium for an additional three months, subject to the prior consent of the majority of creditors based on the amount of their due receivables.

The main effects of the extraordinary moratorium would be that:

- limitation periods that would otherwise affect creditors' rights and their enforcement against the Czech debtor are fully and automatically suspended;
- the Czech debtor could be sued but judgments could not be enforced against it;
- significant asset disposals would generally be prohibited, except in the usual course of business;
- the Czech debtor could prioritize payment of debts incurred while the extraordinary moratorium is in place (these debts would have priority ranking in any subsequent insolvency proceedings); and
- the Czech debtor's counterparties would not be entitled to terminate or refuse to perform certain essential pre-existing contracts for as long as the debtor continues to meet at least its obligations arising during the moratorium.

However, the extraordinary moratorium generally does not affect ordinary set-off.

Since the extraordinary moratorium is not notified as an eligible proceeding under Regulation (EU) 2015/848 of the European Parliament and of the Council dated 20 May 2015 on insolvency proceedings (recast), its protective effect does not extend to proceedings carried out outside of the Czech Republic. This also means that various specific rights relating to ordinary set-off or security enforcement, which are otherwise granted and available under the Insolvency Regulation, will not be available.

## **1.2 Certain Other Changes contained in the Draft Bill**

The draft bill would suspend obligations of Czech debtors (and their directors) to file for insolvency when normally required by law. This suspension should last until the end of a six-month period starting from cancellation of the COVID-19 Extraordinary Measures, but not extending beyond the end of 2020.

The draft bill would also automatically suspend all suspect periods in connection with transfers at undervalue, preferences and fraudulent transfers for the period of applicability of the COVID-19 Extraordinary Measures (i.e., for the same period as the obligation to file for insolvency would be suspended).

## **1.3 Impacts on Transactions under ISDA Master Agreements**

We confirm that none of the changes introduced by the draft bill affect the ability of a counterparty under derivative and similar financial transactions to perform close-out netting in respect of such transactions under an eligible close-out netting arrangement. Nor will the changes proposed in the draft bill affect validity or enforceability of financial collateral arrangements, if these are made in line with the relevant documentation and in accordance with other applicable Czech laws.

### ***Applicability of Bankruptcy Event of Default***

The commencement of an extraordinary moratorium does not evidence the Czech debtor's inability to pay its debts but serves primarily as a protective measure. Accordingly, a counterparty to derivative and other financial transactions under ISDA Master Agreements with a Czech counterparty should bear in mind that the filing for and commencement of the extraordinary moratorium does not, in our view, in and of itself trigger the relevant Bankruptcy Event of Default under the 1992 ISDA Master Agreement.

The analysis seems to be different under the 2002 ISDA Master Agreement, where the Bankruptcy Event of Default also covers a situation where a party “*has instituted against it a proceeding seeking a judgment of insolvency or bankruptcy or any other relief under any bankruptcy or insolvency law [...] affecting creditors' rights [...] and [...] is not dismissed, discharged, stayed or restrained in each case within 15 days of the institution or presentation thereof*”. However, any final assessment as to the applicability of the relevant Bankruptcy Event of Default in the event of the extraordinary moratorium will have to be made on a case-by-case basis taking into account all circumstances of the specific contractual relationship.

### ***Applicability of Failure to Pay or Deliver Event of Default***

If the Czech debtor fails to pay or deliver contrary to the 1992 or 2002 ISDA Master Agreement, then, regardless of certain effects of the extraordinary moratorium preventing the Czech debtor's suppliers to terminate or refuse to perform certain contracts, the ISDA Master Agreement counterparty will not be affected by such a limitation and will generally be able to trigger the Failure to Pay or Deliver Event of Default.

Neither the Czech insolvency laws nor the effects of the extraordinary moratorium affect the right to trigger the Failure to Pay or Deliver Event of Default as eligible close-out netting arrangements (including the contractual trigger events) remain protected under Czech insolvency laws.

## **2. SUSPENSION OF PAYMENTS UNDER CREDIT FACILITIES, LOANS AND SIMILAR FINANCING AGREEMENTS**

The Czech government has also approved and submitted to the Czech Parliament a draft bill, which would ultimately result in suspension of certain payment obligations under, and some temporary changes to, credit facilities, loans and similar financing agreements agreed and utilised and, in some cases, agreed but not utilised, before 26 March 2020, if the Czech borrower opts-in for such protection.

This draft bill grants rights to Czech borrowers, including corporations, to ask their lenders for suspension of payments under credit facilities, loans and similar financing agreements up until 31 October 2020 (if so selected by the borrower). As far as Czech corporations are concerned, this protective period will not affect their duty to make interest payments; however, such Czech borrowers may stop paying amortized payments of the principal.

The draft bill expressly excludes from its scope, *inter alia*, (i) financial instruments within the meaning of Annex I Section C of MiFID 2; (ii) obligations the subject matter of which is such a financial instrument; (iii) obligations giving rise to receivables of financial nature secured by a financial collateral arrangement<sup>1</sup>; or (iv) margin loans. Therefore, it should not directly adversely affect rights of counterparties of such in-scope Czech counterparties to require payments under derivatives or similar financial transactions entered into under ISDA Master Agreements.

Unfortunately, the draft bill may, in some instances, cause asymmetry between payments and deliveries under any currency hedging transactions and repayments of the loan, if the Czech borrower requests an extension of the term of the loan, effectively changing the agreed term sheet.

---

<sup>1</sup> For a detailed discussion of the scope of receivables of financial nature and financial collateral arrangements, please see p. 18 *et seq.* of the Industry Netting Opinion (*Enforceability under Czech Law of Close-out Netting of Privately Negotiated Derivatives Transactions under the 1992 ISDA Master Agreements and the 2002 ISDA Master Agreements*) dated 2 August 2019.

## Contacts

---



**Petr Vybíral**

Counsel - Czech Republic - Prague  
Tel +420 222 107 173  
Mob +420 724 064 044  
petr.vybiral@allenoverly.com



**Tomáš Kirner**

Associate - Czech Republic - Prague  
Tel +420 222 107 118  
Mob +420 734 178 454  
tomas.kirner@allenoverly.com



**David Mikyska**

Junior Lawyer - Czech Republic - Prague  
Tel +420 222 107 112  
Mob +420 607 863 693  
david.mikyska@allenoverly.com