

Interpretation of what constitutes providing financial services in the Czech Republic

- Regulations
- Act No. 21/1992 Coll., on banks, as amended (the “**AoB**”)
 - Act No. 256/2004 Coll., on capital market undertakings, as amended (the “**AoCMU**”)
 - Act No. 240/2013 Coll., Act on Management Companies and Investment Funds (the “**AoMCIF**”)
 - Act No. 277/2009 Coll., on insurance, as amended (the “**AoI**”)
 - Act No. 284/2009 Coll., on payments, as amended (the “**AoP**”)

- Provisions
- Article 1(1) and (3) of the AoB
 - Article 328 and following of the AoMCIF
 - Article 5 of the AoCMU
 - Article 4(1) and (2) of the AoI
 - Articles 4 and 9 of the AoP
 - and others

Question

When is a financial service regarded as provided in the Czech Republic?

Answer

1. Introduction

Under the legal regulations governing the activities of legal entities subject to supervision by the Czech National Bank, the provision of financial services in the Czech Republic is conditional on obtaining authorisation under public law.¹ Such authorisation may take the form of a permit, a licence or registration (“authorisation”) for Czech entities and for non-Czech entities that do not enjoy the benefits of single authorisation valid throughout the European Economic Area. Non-Czech entities from member states of the European Economic Area that do enjoy the benefits of the single licence are authorised to provide financial services in the Czech Republic on the basis of notification.

Doubts about whether a financial service is being provided in the Czech Republic arise in situations where the provider and beneficiary of the financial service are from different countries. Anyone providing financial services without the relevant authorisation risks administrative or criminal prosecution and may face consequences in private law.

The regulations for assessing where a financial service is provided are harmonised to only a very limited extent by European Union law and by the standards and recommendations of international organisations of supervisory authorities, financial service providers and similar entities. The financial market supervisory authorities of other countries may therefore have different interpretations. Where possible, this interpretation is based on EU and international documents in this area.²

The answer given below relates only to the location of where the service is provided. It does not deal with the issues of whether the provision of services constitutes business activity, when it is necessary to establish a branch to provide services, or whether the provision of services is permanent or temporary.

All the criteria given below should be considered when assessing specific cases.

¹ The entities subject to supervision by the Czech National Bank are listed in Article 44(1) of Act No. 6/1993 Coll., on the Czech National Bank, as amended. For the definition of “financial service”, see, for example, Article 54a(1) of Act No. 40/1964 Coll., the Civic Code, as amended.

² Commission Interpretative Communication “Freedom to provide services and the interest of the general good in the Second Banking Directive” (SEC(97) 1193 final), Commission Interpretative Communication “Freedom to provide services and the general good in the insurance sector (2000/C 43/03)”, IOSCO “Securities Activity on the Internet” (approved on 13 September 1998), Communication from the Commission “The application of conduct of business rules under Article 11 of the Investment Services Directive (93/22/EEC)” (COM/2000/0722 final) and “What constitutes providing payment services in another Member State”, PSDTG Working Paper, 8 October 2008.

Where a service provider has doubts about whether it is providing services in another country, it is prudent to obtain the necessary authorisation.

2. Criteria for assessing a service as being provided in the Czech Republic

The key criterion for deciding whether a service is provided in the Czech Republic is the place of provision of the characteristic performance of the financial service, i.e. the place where the customer receives contractual performance for which payment is due.³ This general criterion implies the following:

Where the financial service is provided in the simultaneous physical presence of the two contracting parties or their representatives, it is provided in that location (usually the place of business of the provider with the customer present).

The place of business of a financial provider in another country constitutes the place of characteristic performance also if

- the performance is provided at a distance, but the beneficiary of the service actively sought out the foreign service provider in the other country, or
- the contract was entered into in the other country and it must have been clear to the customer that Czech law would not apply (the legal regime of the contract is irrelevant).

The following situations do not constitute active seeking out of a foreign service provider in another country by the beneficiary:

- a) where a financial service provider offers its services in a targeted manner in the Czech Republic, or
- b) where contracts are signed in the Czech Republic.

In the case of distance financial services, the service is provided where it is “offered in a targeted manner” and where it can simultaneously be used. The targeted offering of services in the Czech Republic includes promotional activity within the territory of the Czech Republic directed at the provision of a financial service, for example in the form of advertisements in the Czech media or offers through the internet under the conditions set out below. The targeted offering of a service in the Czech Republic also includes canvassing potential beneficiaries of that service and offering it to them by means of letters, e-mails, telephone calls or visits from sales representatives within the territory of the Czech Republic.⁴

However, the place of supply can also be the place where the customer is currently staying, for example in the case of a service that is specifically linked with a particular place in another country.

3. Physical presence of a service provider in the Czech Republic

For the purposes of regulation of business in the financial market, a financial service is always provided within the territory of the Czech Republic when it is provided in the Czech Republic through a person located in the Czech Republic, be it an employee or a person operating on the basis of some other contractual relationship (such as an introducing broker). If a foreign service provider only has certain support activities located in the Czech Republic (such as an IT unit or call centre) and does not provide financial services in the Czech Republic, it does not need authorisation to carry on business in the financial market even if it has an

³ See the Commission Interpretative Communication for the banking area cited in footnote 1. Performance means property benefit, the possibility of gaining control of a securities account and so on.

⁴ This includes cases where such activities are performed by an entity authorised to broker financial services in the Czech Republic (for example, an investment intermediary on the basis of a contract to perform activities for a foreign investment firm).

⁵ Judgment of the European Court C-452/04 (Fidium Finanz).

⁶ This list is taken essentially from the IOSCO document “Securities Activity on the Internet” approved on 13 September 1998.

⁷ “Eligible financial institution” is defined in Article 5e(1) of the AoB.

organisational unit (branch) located in the Czech Republic.

The provision of the characteristic performance of a service by sending an employee or representative to the Czech Republic in order to provide the service constitutes provision of the service in the Czech Republic.

4. Clarification of the term financial service

Not every activity connected with a financial service in itself constitutes provision of the financial service in the sense of the characteristic performance of that service (e.g. sending account statements to the Czech Republic, enabling credit cards issued in another country to be used in the Czech Republic, checking the value of collateral provided in the form of property within the territory of the Czech Republic). Activities preceding or following the provision of a financial service do not in themselves constitute provision of the service within the territory of a given country, hence authorisation to do business in the financial market is not necessary.

5. Specific regulation in the area of insurance

The insurance sector is a specific case regulated explicitly in European Union law. Article 13(9) of Directive 2009/138/EC on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II) regulates the Member State in which life and non-life insurance services are provided. The deciding factor is the location of the risk in the case of non-life insurance and the location of the commitment in the case of life insurance.

According to Article 13(13) of the Solvency II directive, the risk is situated in

- the Member State in which the insured property is situated, where the insurance relates to buildings and their contents,
- the Member State of registration, where the insurance relates to vehicles,
- the Member State where the policy holder took out the policy in the case of policies of a duration of 4 months or less covering travel or holiday risks,
- in other cases, the Member State in which the habitual residence or establishment of the policy holder is situated.

According to Article 13(14) of the Solvency II directive, the location of the commitment is the Member State in which the habitual residence of the policy holder or the establishment to which the contract relates is situated.

6. Application of the criteria in section 2 in the case of the internet

The use of the internet to offer a financial service and for communicating between the beneficiary and provider of a financial service has no bearing on the assessment of where the service is provided. The internet serves as a means of communication and does not alter the nature of the financial service provided. The provision of distance financial services may constitute provision of services within the territory of the customer's country.⁵

To assess whether a financial service is provided through the internet in the Czech Republic, the following factors are important:⁶

- a) whether the financial service is offered in the Czech Republic (through the internet, newspaper advertisements, billboards, financial advisers, etc.),
- b) whether an interactive means of communication between the beneficiary and the provider of the service on a website is used,
- c) whether the offer of the service represents a legally binding draft contract and the customer can enter into this contract from his or her place of residence

- through the internet or by post,
- d) whether the service provider accepts money from natural persons resident within the territory of the Czech Republic or from legal entities established within the territory of the Czech Republic,
 - e) whether there is a large number of contacts from service beneficiaries from the Czech Republic,
 - f) whether there is a specific website targeted at persons from the Czech Republic,
 - g) whether the website and the communications between the service provider and service beneficiaries are in the Czech language,
 - h) whether the Czech Republic is listed among the countries to which the offer is directed, or whether the Czech Republic is not listed among the countries to which the offer is not directed,
 - i) whether there are no technical measures preventing the service from being provided to natural persons resident within the territory of the Czech Republic or to legal entities established within the territory of the Czech Republic.

The factors listed above should be assessed in context, taking into account the nature and frequency of the activities.

By contrast, the location of the server used to provide a financial service is irrelevant as regards the place of provision of the service.

7. Advertising and offers of financial services

Promoting and advertising a financial service does not in itself constitute providing the service. It is not usually necessary to obtain authorisation or give notification in order to promote financial services in the Czech Republic. The need to obtain authorisation or give notification depends on the intention of the service provider to provide financial services in the Czech Republic as per section 2. Only if the financial service provider intends to provide services in the Czech Republic is it necessary to obtain the relevant authorisation or give notification for the financial service concerned.

The right of banks and eligible financial institutions⁷ to advertise their services freely is laid down in Article 5m of the AoB. Similarly, insurance companies from other Member States and insurance companies from third countries are authorised under Article 135 of the Aol to use all available means of communication to advertise their services. Offers in such cases are subject only to general regulations in the areas of advertising, consumer protection, competition, etc. It should be said, however, that the related service provision will very often constitute supply in the Czech Republic and the financial service provider must obtain authorisation to do business in the Czech Republic before starting to provide the characteristic performance.

In some sectors of the financial market (investment services, collective investment and money changing) authorisation to do business is explicitly required even to offer a financial service. However, the only offers that are regulated are for services to be provided – even if only at a distance – within the territory of the Czech Republic in accordance with the criterion described in section 2 (for example, authorisation is needed to offer investment services in respect of which customers issue instructions from home, but is not needed to advertise foreign bureaux de change advertising at Czech airports that it is cheap to change money at their premises in another country). In the said areas it is an administrative offence even to offer provision of financial services in the Czech Republic without the relevant authorisation. It is therefore necessary to obtain authorisation before offering the service, unlike in other cases, where it is necessary to obtain authorisation before providing the service for the first time.

8. Additional information

Examples of the application of the aforementioned regulations to various types of financial services are given in the annex to this standpoint. These examples are provided only for illustration; it is always necessary to assess the specific situation.

A financial institution is entitled to undergo the notification procedure relating to the single European licence regardless of whether the supervisory authority believes it is providing services on the relevant territory or not.

This answer concerns the location of service provision from the perspective of regulation of entities subject to supervision by the Czech National Bank. It cannot be applied to service providers that are not subject to Czech National Bank supervision.

The application of private law is an entirely separate issue. This interpretation is also without prejudice to the location of the place of supply pursuant to the Act on Value Added Tax and the assessment of payments for financial services as income from sources within the territory of the Czech Republic from the income tax perspective.

This answer expresses the opinion of Czech National Bank staff. The courts and the Bank Board of the Czech National Bank may take a different view. However, when performing supervision of the financial market, the Czech National Bank will consider the approach set out in this answer to be legally compliant unless the context indicates that the answer is not applicable to the case in question.

Further information for the users of the answer:

The answer reflects views of the Czech National Bank staff. A court, or possibly the Board of the Czech National Bank, may take a different view. However, Czech National Bank will in the course of financial supervision consider a practice that adheres to the answer, within the limits of the answer and its assumptions, to comply with legal regulations, unless it follows otherwise from circumstances of the case.

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Annex: Examples of practical application of the criteria for assessing a service as being provided in the Czech Republic to individual financial services

A) Accepting deposits

During a visit to Austria, a Czech citizen buys a registered deposit certificate of an Austrian bank with a maturity of one year.

Solution: The Austrian bank does not need authorisation to provide services in the Czech Republic, i.e. it does not have to give notification of the acceptance of deposits, because the acceptance, repayment (including interest) and any other handling of the deposit is taking place in another country in the simultaneous presence of both parties. The characteristic performance will take place in another country. Any advertising by the Austrian bank in the Czech Republic is irrelevant.

B) Providing loans

A Czech citizen buys a holiday home in France which she will partially finance using a mortgage obtained from a French-based bank that she sought out herself in another country after seeing an advertisement placed in a local newspaper in that country. For this purpose, she has opened an account with the bank through which the loan will be drawn and repaid. To do so, she has communicated in French from the Czech Republic over the internet.

Solution: In this case, the French bank does not need authorisation to provide services in the Czech Republic, because the Czech citizen sought out the service provider herself in another country without the service being offered in the Czech Republic.

C) Account maintenance

An Irish bank advertises in Czech on the internet that it is offering Czech citizens above-average interest rates on deposits and cheap payments in euros. To set up an account, all that is needed is to have an electronic signature and send certified copies of two documents in writing to the bank's address. After filling in a questionnaire, the customer is sent a draft electronic agreement for electronic signature. After signing the contract he is immediately sent the account information and log-in information for electronic banking, which is the only possible way of managing the account.

Solution: In this case, the Irish bank needs authorisation to provide services in the Czech Republic, i.e. it must give notification of the relevant activities pursuant to the AoB, because the offer as well as all contacts and the handling of customer affairs are going on within the territory of the Czech Republic. The account maintenance agreement is effective in the Czech Republic, because it is there that the deals are executed. It should be emphasised that the bank itself canvassed potential customers in the Czech Republic with a view to concluding an agreement, albeit in a non-individualised manner.

D) Insurance activity

The criteria for locating where the services of an insurance company are provided are laid down directly in Articles 9, 13 and 14 of Directive 2009/138/EC on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II) (the country in which the risk or commitment is situated) and no interpretation problems arise in this case.

Example: A Czech citizen owns a property in Germany and wants to ensure it against flooding. A German insurance company contacts him on the advice of the property manager. The Czech citizen takes out this policy at a distance, from the Czech Republic.

Solution: The German insurance company provides services in Germany, because the service is provided in the Member State where the risk is situated, which is the country where the property is located.

E) Reinsurance activity

Example a): A Swiss reinsurance company sends representatives to the Czech Republic. These representatives contact individual insurance companies to offer them services, discuss reinsurance options, etc. On the basis of this information, the final draft agreement, including the reinsurance calculation, is prepared at the Swiss headquarters.

Solution: The Swiss reinsurance company needs authorisation to provide services in the Czech Republic (as an entity from a third country it must have a branch in the Czech Republic pursuant to Article 47 of the AoI unless an international treaty or an agreement between the supervisory authorities pursuant to Article 48(3) of the AoI provides otherwise), because the purpose of reinsurance as a financial service is to transfer risk from insurance companies to reinsurance companies. The headquarters of the reinsured insurance company is in the Czech Republic. It should be emphasised that the reinsurance company itself canvassed potential clients in the Czech Republic with a view to signing an agreement, i.e. it offered a service in the Czech Republic.

Example b): A Swiss reinsurance company does not send representatives to the Czech Republic, but merely advertises its services in international insurance journals. A Czech insurance company finds out about the reinsurance company from these sources and, on the basis of its own research, decides to reinsure with it and to that end sends a representative to visit it. An employee of the Swiss reinsurance company then visits the headquarters of the Czech insurance company several times to conduct preliminary negotiations. The final contract is signed in Switzerland.

Solution: The Swiss reinsurance company does not need authorisation to provide services in the Czech Republic, because the insurance company sought it out itself in another country and the Swiss reinsurer is not actively canvassing insurers in the Czech Republic even though it is reinsuring a Czech-based insurance company.

F) Buying or selling securities

Example a): A foreign investment firm based in another member state of the European Economic Area accepts telephone orders to buy and sell securities listed on the stock exchange in that member state from a customer in the Czech Republic. The customer fills in and signs the investor questionnaire and other contractual documents in the Czech Republic at the branch of a bank which belongs to the same business group as the foreign investment firm and actively offers the services of that firm in the Czech Republic. The questionnaires are processed in the other country.

Solution: The foreign investment firm needs authorisation to provide services in the Czech Republic, because the customer transfers orders and other instructions from the Czech Republic and the investment firm's services are actively offered in the Czech Republic.

Example b): A foreign investment firm based in another member state of the European Economic Area accepts orders to buy and sell securities listed on stock exchanges all over the world through an internet trading application. Potential customers are actively canvassed by an investment intermediary registered in accordance with Article 30 of the AoCMU, with whom the foreign investment firm has an introducing broker agreement. The customer fills in and signs the contractual documentation in the Czech Republic and sends a certified copy by post to the foreign investment firm's registered address. For the duration of the contractual relationship between the foreign investment firm and the customer, the investment intermediary is remunerated in proportion to the volume of trades executed by the customer with whom he brokered the contract.

Solution: The foreign investment firm needs authorisation to provide services in the Czech Republic, because the investment broker is operating within the territory of the Czech Republic as its agent and is actively developing activities directed at canvassing a group of persons in the Czech Republic (in particular canvassing prospective investment service customers by means of advertisements in the Czech media, letters, e-mails, telephone calls or personal visits) with whom a general agreement to procure orders for investment instrument transactions submitted through an internet trading application is subsequently signed at a distance. The service is therefore offered and used from the Czech Republic.

G) Execution of customer orders

A foreign investment firm based in another member state of the European Economic Area carries out a customer's orders on the basis of a general agreement executed in the foreign investment firm's home country in accordance with telephone orders received from the customer in the Czech Republic. The customer found out about the foreign investment firm's services on its Czech language website and signed the agreement at the firm's CEE desk at a branch in the other country.

Solution: The foreign investment firm needs authorisation to provide services in the Czech Republic, because it is offering its services in the Czech Republic over the internet and providing services in the Czech Republic at a distance by telephone. If the foreign investment firm is a bank it may canvas prospective customers in the Czech Republic, because the AoB, which in this section transposes the applicable directive, expressly permits the free advertising of banks without the need to obtain authorisation. However, since the customer may additionally issue orders directly from the Czech Republic, even a bank investment firm needs to obtain the necessary authorisation, because it is providing services in the Czech Republic.

H) Managing customer assets

A foreign investment firm based in a non-member state of the European Economic Area provides the service of asset management to a customer from the Czech Republic. All investment decisions, including those related to asset management, are received and executed in the other country. The assets were inherited and the customer chose the foreign investment firm herself in that country.

Solution: The foreign investment firm does not need authorisation to provide services in the Czech Republic, because the customer sought it out herself in another country, the contract was signed in another country, and the investment firm manages the portfolio independently without receiving orders from the Czech Republic. A service is being provided to the customer, but without the active performance of the service within the territory of the Czech Republic.

I) Establishing and managing an UCITS

A management company from another Member State who has authorisation according the directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) intends to establish and manage an UCITS in the Czech Republic, but the fund will be managed from the management company's head office in the other Member State. The UCITS will be offered primarily to customers in the Czech Republic.

Solution: In this case, the management company established in another Member State needs authorisation to provide services in the Czech Republic, i.e. it must give notification to the Czech Republic, because the characteristic performance is management of UCITS, including compliance with Czech regulatory requirements, the possibility of offering investment in the UCITS to Czech investors and this performance is provided in relation to the domestic UCITS (Art. 16(1) first subparagraph and Art. 16(3) directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)).

J) Representative office of a foreign bank

A foreign bank established in another Member State has a representative office in the Czech Republic through which it systematically, permanently and regularly markets its head office's banking services without carrying on activities resulting in the characteristic performance of the service within the territory of the Czech Republic, and the head office of the bank does not provide services to Czech customers through the internet. This representative office is registered with the Czech National Bank in accordance with Article 39 of Act No. 6/1993 Coll., on the Czech National Bank, as amended.

Solution: The activities of the organisational unit do not display the features of service provision in the Czech Republic, because the bank neither provides, nor intends to provide services in the Czech Republic, and the offering of banking services does not on its own require authorisation.

K) Using payment cards

A foreign bank issues its customer with a debit card to go with his current account in another country. The customer uses this card in the Czech Republic

- a) to make payments, and
- b) to withdraw cash from a cash machine; the bank to which this machine belongs is, in accordance with established contractual practice, a representative of the bank that issued the card.

Solution: In this case, the bank that issued the card to its client in another country to go with his account maintained in another country is not providing the service within the territory of the Czech Republic.⁸

⁸ See the European Commission document "Payment Services Directive (PSD) – Provision of Payment Services in Other Member States", 1 February 2008.