

OFFICIAL INFORMATION OF THE CZECH NATIONAL BANK

**of 31 January 2002
regarding the conclusion of control agreements by banks**

The amendment to Act No. 513/1991 Coll., the Commercial Code (hereinafter referred to as the “Commercial Code”), as implemented by Act No. 370/2000 Coll., has introduced the institute of control agreements into the Czech legislation. In order to provide an interpretation of the issue of the conclusion of control agreements by banks, the Czech National Bank hereby provides this information:

- 1) The conclusion of a control agreement under which a bank becomes a parent undertaking (controlling person) is in contravention of Article 12(1) of Act No. 21/1992 Coll., on Banks, as amended (hereinafter referred to as the “Act on Banks”) for the following reasons in particular:
 - a) pursuant to Article 12(1) of the Act on Banks, a bank must carry on its activities with prudence. By entering into the control agreement, the parent undertaking (controlling person) incurs the obligation under Article 190c(5) of the Commercial Code to settle any loss of the subsidiary (controlled person) if this loss cannot be settled from the subsidiary’s reserve fund or other disposable funds. The Commercial Code imposes this obligation to settle the loss of the subsidiary on the parent undertaking regardless of whether the loss is due to inappropriate business transactions carried out on the parent bank’s instructions or without such instructions, and this exposes the bank to the risk of unlimited and uncontrollable losses. Therefore, with respect to the Act on Banks, the bank’s assumption of the obligation to settle the subsidiary’s losses pursuant to Article 190c(5) of the Commercial Code is deemed imprudent conduct by the bank, which in turn is in contravention of the principle of prudential bank business set forth in Article 12(1) of the Act on Banks;
 - b) also in contravention of Article 12(1) of the Act on Banks is the parent bank’s guarantor obligation to provide compensation for any damage caused to the subsidiary or to creditors of the subsidiary by the actions of persons who give instructions in the name of the parent undertaking to the subsidiary’s statutory body should those persons not act with due diligence. This obligation of the parent undertaking is laid down by law and is set forth in Article 190b(3) and (5) of the Commercial Code.

In view of the aforementioned facts, the conclusion of a control agreement by a bank as a parent undertaking constitutes a breach of the Act on Banks, with all the consequences that entails.

- 2) The conclusion of a control agreement under which a bank becomes a subsidiary does not rid the bank of the obligation when carrying on its business to comply with the provisions of the Act on Banks, as the Act on Banks is a special legislative act in respect of the Commercial Code. Accordingly, banks are obliged, when pursuing their business, to respect the priority of the provisions of the Act on Banks over the provisions of the Commercial Code. In particular, a bank may not execute any instructions of a parent undertaking which would be in contravention of the provisions of Article 12 of the Act on Banks.

Bank Board Member
Pavel Racoča

Banking Regulation Department
Responsible:
Dřevínek, tel: 2441 3175