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THE NEW COMMERCIAL CODE OF THE CZECH REPUBLIC

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The Velvet Revolution in Czechoslovakia in 1989 produced great changes in every aspect of the Czechoslovakian legal and political systems. Political differences between the Czech and Slovak parts of the country led to the splitting of Czechoslovakia into two republics on January 1, 1993. Both countries, but particularly the Czech Republic, have continued the changes in legal philosophy, practice and procedures which began in 1989.

The Czech Republic, first as a part of Czechoslovakia and then as an independent republic, has fared well in developing a stable and growing economy.[1] However, the changes have built upon the legal and economic systems of the past. Even before 1989, Czechoslovakia was one of the ten largest industrialized economies in the world,[2] and the Czech Republic has continued to build upon that economic base. Indeed, the history of the free market economy of the Czech Republic has its roots in its pre-1989 industrial status.

With the recent changes in the economic and political system have come equally significant developments in the drafting of a myriad of rules and laws to regulate the new business climate. In addition, there have been significant developments in the revision of domestic and foreign business laws and practices of the Czech

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1. *See generally* LYNEE HOULE ET AL., CZECHOSLOVAKIAN BUSINESS LAW (1992).

2. Richard S. Gruner, *Of Czechoslovakia and Ourselves: Essential Legal Supports for a Free Market Economy*, 15 HASTINGS INT'L & COMP. L. REV. 33, 33 n.1 (1991) (citing U.S. DEP'T OF THE ARMY, CZECHOSLOVAKIA: A COUNTRY STUDY 32 (Ihor Gawdiak ed., 3d ed. 1989)); *see also* Heather V. Weibel, Note, *Avenues for Investment in the Former Czechoslovakia: Privatization and the Historical Development of the New Commercial Code*, 18 DEL. J. CORP. L. 889, 890 (1993).

> Prior to World War II and its forty-year suffocation by Communism, the [Czech and Slovak Federal Republic] was one of the most developed countries in Eastern Europe; a democratic government was in place, and the country's industry enjoyed world-wide renown for its superior quality goods. This history demonstrates that the idea of a market economy is not entirely foreign . . . .

Id.

Republic. The need for creating new commercial law became apparent after the Velvet Revolution. The amendments to the Economic Code could not meet the requirements of the newly born market economy. A group of Czech lawyers, headed by Professor Stanislav Stuna, had the challenging task of drafting the new Code. One of the most important changes in business law in the Czech Republic has been the promulgation of the Commercial Code in 1991.[3] The Code became effective January 1, 1992, exactly one year before Czechoslovakia became two separate republics, and is the paramount law regulating business in the Czech Republic.

The new Commercial Code includes 775 articles, which are grouped into three main parts. The first part deals with general commercial law. The second part deals with legal forms of business. Finally, the third part focuses on commercial obligations, "including those arising under specific contracts such as sale, agency or credit contracts and liability for damages."[4]

The new Commercial Code has effectively launched the Czech business community into a free market economy protected and supported by law. The new Code contains provisions to stimulate business, trade and investment. Also within the new Code are provisions which allow "natural persons and legal entities to enter into foreign trade relations at a trading status equal to that of their foreign counterparts."[5] This assures Czech businesspeople and entities that they are free to trade abroad. Since the Commercial Code became effective, Czech businesses and their foreign business partners have acquired a significant amount of valuable experience with a free market economy. In particular, Czech businesses have gained much practical experience in improving the quality of contracts, avoiding commercial disputes before they oc-

3. COMMERCIAL CODE [COM. C.] Act No. 513 (1991) (Czech Rep.). The Commercial Code was adopted by the Federal Assembly of the Czech and Slovak Federal Republic on November 5, 1991, and amended by Czech Federal Act No. 264/1992 Coll., Czech Act No. 591/1992 Coll., and Czech Act No. 286/1993 Coll. After the division of the former Czechoslovakia into the Czech Republic and the Slovak Republic on January 1, 1993, the Commercial Code in effect in the Czech Republic applied in the "new" Czech Republic. Similarly, the Commercial Code in effect in the Slovak Republic (as amended by Slovak Act No. 264/1992 Coll., Slovak Act No. 600/1992, and Slovak Act No. 278/1993) applied in the Slovak Republic.

4. STEPHEN DENYER ET AL., LEGAL ASPECTS OF DOING BUSINESS IN THE CZECH AND SLOVAK REPUBLICS 17 (1993).

5. HOULE, *supra* note 1, at 65. Although the new Commercial Code provides broad rights, it also requires that natural persons and legal entities who enter into foreign trade relations must register "either in the Commercial Register or with the appropriate authority under specific areas of law, such as those laws governing the activities of attorneys, traders, interpreters, and sworn experts." *Id. See also* COM. C. §§ 1-3 (Czech Rep.) (stating the broad scope of the Commercial Code).

cur and resolving any disputes that do arise.

However, it is important to remember that contemporary business practices in the Czech Republic sometimes rest, at least in part, on the legacy of interpreting legal norms or concepts applicable to contracts in earlier times. In short, anyone seeking to understand the commercial law and practices of the Czech Republic today must have some understanding of the law and practices of the past.

An explanation of these laws and practices during the socialist era can offer Western observers a perspective and insight not usually possessed by advisors of those seeking to invest in the Czech Republic or to trade with Czech businesses. Such an explanation could also offer those in the Czech Republic an opportunity to document and reflect upon the fundamental shifts in law in the past few years and to consider the directions that Czech business law and practices may follow. This Article provides an explanation of the Czech Republic's past and present business practices for both the Western observer and the Czech businessperson or lawyer. This Article first presents a background of the Czech legal system, focusing on the several previous codes which regulated Czech business law. Next, this Article discusses the new Commercial Code and its effect on business practices throughout the Czech Republic. To the extent that the Czech Republic works under a new Commercial Code today, much of the country's legal and political history shaped the provisions of the new Code, and a thorough discussion of Czech legal history clearly aids in the understanding of the Commercial Code.

I. THE LAWS REGULATING PROPERTY DURING THE SOCIALIST ERA AND THE TRANSITION TO A LEGAL SYSTEM FOR A FREE MARKET ECONOMY

This Part surveys three major laws used to regulate property and particularly commerce under the former socialist legal system: the Civil Code,[6] the Economic Code,[7] and the International Trade Code.[8] This Part first discusses the effects those laws had on economic development and on the subsequent need to shift to a new legal system to support a free market economy. Finally, this Part introduces the current structure of the Czech Commercial Code.

6. Act No. 141/1950 Coll.

7. Act No. 109/1964 Coll., later amended by Act No. 82/1966 Coll., Legal Measure No. 13/1967 Coll, Act No. 69/1967 Coll., Act No. 72/1970 Coll., Act No. 138/1970 Coll., Act No. 144/1975 Coll., Act No. 165/1982 Coll., Act No. 98/1988 Coll., and Act No. 103/1990 Coll..

8. Act No. 101/1963 Coll.

A. The Historical Framework

Before World War I, the Austrian Commercial Code of 1863 governed business and economic relations in what is now the Czech Republic. This old Austrian regulation was in force until 1950, when it was amended by the Act No. 141/1950 Coll. In 1948, the Communists took over Czechoslovakia and in 1949 they abrogated the existing Commercial Code.[9] This revocation of the pre-1948 Commercial Code, and the passage of other acts to enable the nationalization of property, marked the practical end of private enterprise in Czechoslovakia.[10] From the early 1950s and continuing through the 1960s, legal and economic decay continued as the socialist regime arbitrarily divided the laws regulating property relations in Czechoslovakia into three codes: the Civil Code; the Economic Code; and the Code of International Trade.[11]

1. The Civil Code

The Civil Code, as far as the law of property was concerned, applied only to relations between citizens and "socialist organizations."[12] The determination of an organization as a "socialist organization" was an ideological and often arbitrary determination. Yet, the determination of status as a "socialist organization" was very important because it affected the organization's relations with others. Thus, if an organization was not a "socialist organization," the Civil Code did not apply to it, even in the unusual case when socialist organizations had an urgent need to deal with either the few private entrepreneurs or with domestic "non-socialist organizations." In those cases, legal relationships were, at best, ambiguous.

2. The Economic Code

The Economic Code regulated the management and operation of socialist organizations. The Economic Code preferred the "vertical" regulation, or public law, over regulations reached as a result of the parties' contractual freedom.[13] Indeed, the Economic Code actually suppressed contractual freedom and distorted the relative equality of bargaining power in exchange for attempts to

9. *See* DENYER ET AL., *supra* note 4, at 16 (describing a brief history of the Commercial Code).

10. *Id.*

11. Other laws such as those governing joint stock companies and joint ventures also had an indirect role in the regulation of property in that these laws affected the possible systems of ownership and control. *See* Robert L. Drake, *Legal Aspects of Financing in Czechoslovakia, Hungary, and Poland*, 26 INT'L L. 505, 505-08 (1992).

12. Josef Bejcek, *To the Changes of the Czech Law of Contract*, *in* INTRODUCTION TO CZECH LAW, 105, 105 (Karel Schelle et al. eds., 1993).

13. Id. at 105.

promote economic growth and fulfillment of the "Central Plan."[14] The Economic Code effectuated this intent by implementing a contractual duty. In addition, the Economic Code instituted obligatory and closed contracts if it coincided with the needs of the national economy's desire for proportional development.

Under the Economic Code, socialist organizations enjoyed many advantages over other entities, including entrepreneurs and "un-socialist organizations." Socialist organizations enjoyed better access to resources and finances, in addition to more favorable tax rates.[15] Socialist organizations also enjoyed a superior legal status. This system created many anomalies. Many nominally "socialist" organizations actually harmed the economy, while "non-socialist organizations" were often socially useful and successful despite their inferior status.

In effect, the Economic Code was a tool of the "dirigistic," or state-controlled, philosophy of the government.[16] It rejected a market approach in favor of a socialist approach.[17] One stated goal of business was "to promote socialist relations," but that was often the name given to disguise the redistribution of goods and capital. In turn, this redistribution was often a substitute for wealth creation.

Both the Economic Code and the Civil Code blurred the long-standing distinctions between "public law"[18] and "private law."[19]

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14. *Id.* at 105-06.

15. *Id.* at 105.

16. Dirigism means "economic planning and control by the state." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY OF THE ENGLISH LANGUAGE 642 (1981).

17. *See* Iva Smidova, *On the Transition of the Czech Economy to the Market Economy*, *in* INTRODUCTION TO CZECH LAW 31, 32 (Karel Schelle et al. eds., 1993) (describing the characteristics of a centrally-planned economy, including the existence of only one bank).

18. As used in this sense, public law may be generally defined as "that portion of the law that defines rights and duties with either the operation of government, or the relationships between the government and individuals, associations, and corporations." BLACK'S LAW DICTIONARY 1230 (6th ed. 1990). Public law is also defined as:

> The part of the law that deals with the constitution and functions of the organs of central and local government, the relationship between individuals and the state, and relationships between individuals that are of direct concern to the state. It includes constitutional law, administrative law, tax law, and criminal law

A DICTIONARY OF LAW 318 (3d ed. 1994).

19. Private law, on the other hand, as used here, may be generally defined as:

> That portion of law which defines, regulates, enforces, and administers relationships among individuals, associations, and corporations. As used in contradistinction to public law, . . . [private law] means all that part of the law which is administered between citizen and citizen, or which is concerned with the definition, regulation, and enforcement of rights in cases where both the person in whom the right inheres and the

The Economic Code allowed both the State and the "supervising bodies of the socialist organizations" to intervene in the internal corporate management of socialist organizations. There was no adequate legal redress for the mistakes dictated by this intervention because the State never acknowledged any harm to the economy brought about by its attempts at supervision. Ultimately, the Economic Code did not regulate any forms of private business and it ensured the "socialist" organizations a relatively privileged status.

The Czechoslovakian Economic Code enabled the socialist regime to destroy the unitary property system. The Economic Code, with the support of the allegedly consumer-oriented aspects of the Civil Code, deepened the theoretical and actual differences among the several forms of property ownership.[20] This destroyed an element perceived to be an essential element of a market economy in pre-war Czechoslovakia: a unitary system of property ownership formally subjecting everyone to the same economic conditions and legal regulation.

The destruction of a unitary system of property ownership had several important results, all of which affected the prosperity of the Czech economy. One result was the curbing of the freedom to contract. Another result was that the relative positions of those entering into contracts were no longer equal and independent. The third result was the abandonment of many traditional legal principles in favor of a narrowing of the scope of many legal regulations governing corporations, forms of security, many special contracts, anti-monopoly measures, unfair trading practices and bankruptcy.[21]

Even the limited number of laws regulating economic activity had to adapt to certain public law concepts, such as central planning, fulfillment of contractual obligations, arbitration of economic disputes and the organization of economic management.[22] Yet, in an economy known as "real socialism," the meanings of some of these terms became empty or illusory.[23] For example, "economic competition" was often a meaningless term in the dirigist and monopolistic economy. Terms like "economic contracts" disguised inadequate contractual subject matter in that the contracts did not really cover the subject matter intended. In short, the meaning of "economic competition" and "economic contracts" was very differ-

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person upon whom the obligation is incident are private individuals. BLACK'S LAW DICTIONARY 1196 (6th ed. 1990). Perhaps more directly, the term can also be defined as "[t]he part of the law that deals with such aspects of relationships between individuals that are of no direct concern to the state." A DICTIONARY OF LAW 305 (3d ed. 1994).

20. Bejcek, *supra* note 12, at 106.

21. *Id.*

22. *Id.*

23. *Id.*

ent from the meaning those terms would have had in a private law system.[24]

3. *The Code of International Trade*

Because the Czechoslovakian Economic Code was designed for a centrally-planned economy in which the state could often intervene, foreign business partners did not have the assurance that they would be able to contract freely with Czech businesses. Furthermore, the structure of the Economic Code prevented foreign parties from determining their legal rights and obligations with any degree of certainty. In market economies, such assurances would be regarded as "givens" and considered necessary to the conduct of a successful business transaction. To foreign investors, this lack of certainty was a risk inherent in any business dealing in any socialist country. In light of this environment, Czechoslovakia adopted a Code of International Trade. Specifically, the Code of International Trade was to increase the legal certainty for foreign business partners, regulate relations with foreign business partners, and finally, to develop international economic cooperation.[25]

Even though the Code of International Trade was thus a departure from the domestic laws regulating commerce, it still lacked the classic principles of private law. Consequently, it could not adequately accommodate foreign investment, joint ventures, or other forms of non-socialist economic cooperation.

B. The Period of Transition 1989-1997

After 1989, laws such as the Civil Code, the Economic Code and the Code of International Trade were clearly inadequate to govern the regulation of business and trade in the emerging Czech market economy. The economic development of Czechoslovakia faced other political and economic obstacles. These included restrictions on currency conversion,[26] counter-trade or barter practices and material supply agreements with other members of the Council for Mutual Economic Assistance ("CMEA," the Soviet bloc economic community).[27]

Economic development in Czechoslovakia also faced interna-

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24. *Id.*

25. *Id.* Since the presence of a socialist regime was an inherent deterrent when foreign businesses faced dealings with their Czech counterparts, the Code of International Trade sought to remedy this obstacle despite the still-apparent socialist structure.

26. *See generally* DENYER ET AL., *supra* note 4, at 6, 10 (explaining the Foreign Exchange Act and its applicability to foreign exchange residents and foreign exchange non-residents).

27. *See* Sabrina P. Ramet, *Eastern Europe's Painful Transition*, 95 CURRENT HISTORY 97, 98 (1996).

tional market problems, such as the denial of most-favored-nation tariff treatment for products exported to the United States and other countries, since Czechoslovakia was still "a communist country."[28] After four decades of socialism, Czechoslovakia also had inadequate access to education on free market principles, world market supply and cost statistics, and information on many types of sourcing, transportation and marketing matters.

To the extent that political changes after the Velvet Revolution of 1989 allowed business entities to enter into a free market, businesses had unequal degrees of commercial independence and inconsistent levels of responsibility with respect to their management decisions.[29] To the disappointment of many, political change and the mere introduction of a market economy did not bring overnight relief from decades of oppression.

There were also practical limitations on the restructuring power of a free market, where all parties are theoretically relatively equal and can operate in the market under relatively similar conditions. An Eastern European free market economy must attempt to overcome an array of difficulties in restructuring the region.[30] Professor Sabrina Ramet observed that these difficulties are not new. In her view, the political configuration of Eastern Europe in the 1990s mirrors patterns of the 1920s. Professor Ramet observed that:

> Now, as then, the states of Eastern Europe are newly freed from foreign rule and are struggling to create new systems and new bodies of law. Now, as then, the political elites speak of building democracies, look to the West for assistance, and wrestle with problems of land redistribution, ethnic animosities, and legitimation. Now, as then, extreme-right parties have emerged, preaching racism and intolerance as solutions to society's problems. Now, as then, the Catholic Church is attempting to build its kingdom on earth. And now, as then, political transition has been characterized by the "acceleration of history," with vast changes compressed in a

28. Imports from countries that have most-favored-nation (MFN) status have customs duties assessed at a lower tariff rate than imports that do not have MFN status. Under the Harmonized Tariff System of the United States (HTSUS), for example, imports from MFN countries were dutiable at a lower, "column 1" rate. Imports from non-MFN countries were dutiable at a significantly higher "column 2" rate. The columns refer to the HTSUS tables themselves, or the predecessor tables, the Tariff Schedules of the United States. Products from communist countries, including the former Czechoslovakia, were usually subject to the higher "column 2" rates under General Headnote 3(f) of the Tariff Schedules. *See generally* Kurt S. Adler, Inc. v. United States, 496 F.2d 1220 (C.C.P.A. 1974); Crystal Clear Indus. v. United States, 843 F. Supp. 721 (Ct. Int'l Trade 1994); Greenhalgh Mills Corp. v. United States, 576 F. Supp. 646, 647 (Ct. Int'l Trade 1983), *aff'd,* 746 F.2d 1491 (Fed. Cir. 1984).

29. Bejcek, *supra* note 12, at 107.

30. Ramet, *supra* note 27, at 97.

short time span engulfing the entire region.[31]

The experiences in the Czech Republic reflect many growing pains of transition.[32] Fortunately, the Czech Republic has not suffered the severe misfortunes of other countries in the region. Instead, for several reasons, the Czech Republic has been "[t]he big success story in Eastern Europe"[33] because of its successful transition from a socialist system to a free market economy.[34]

C. *Legal Transitions*

Socialist law limited free and fair competition, which is a key factor in any economic reform. In order to create a functional and operating environment for participants in a free market, it was necessary to remove the socialist legal system and restore the dual system of public and private law. This required both the destruction of the monolithic vertical control that facilitated state intervention in the economy and the creation of a plurality of mutually-independent and autonomous subjects of business ownership.

Within this context, a vital condition to developing a market economy was the development of a strict definition of business "ownership." "Private ownership" implicated the ability to control the business entity and to respond to market forces.[35] On many levels, individuals became responsible for the consequences of their own decisions in the market. "Private ownership" thus became the basic concept behind "privatization."[36]

It was necessary to reorganize the applicable laws for the

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31. *Id.* at 102.

32. *See, e.g.*, Carol Skalnik Leff, *Could This Marriage Have Been Saved? The Czechoslovak Divorce*, 95 CURRENT HISTORY 129, 133-34 (1996).

33. Ramet, *supra* note 27, at 97. "Thanks to the austerity program of Prime Minister Vaclav Klaus, [the Czech Republic] could claim complete conversion to a free market economy by 1995, with a low unemployment rate of 3.5 percent. The Czech inflation rate of 10 percent is, moreover, the third lowest in the region." *Id.*

34. *See* Sergio Salani & Jerry Sloan, *An Overview of Legal and Financing Aspects for Doing Business in Hungary, Poland, and The Czech Republic*, 9 TEMP. INT'L COMP. L.J. 27, 29-30 (1995).

35. *See* Bejcek, *supra* note 12, at 107.

36. In 1994, for example, "[t]he Czech Republic completed a coupon privatization program" that sold approximately one-third of formerly state-owned enterprises to more than six million individuals. *See* Richard L. Holman, *Czech Sell-Off Round Ends*, WALL ST. J., Nov. 28, 1994, at A14. Holman notes that including an earlier phase of the privatization program, approximately 80% of Czech citizens had purchased shares in 1849 companies. *Id.* Coupons were purchased and exchanged for shares that were then to be held individually or through investment firms. *Id.* Overall, the privatization program placed 80% of state assets in private hands. *Id.* In contrast, political factors delayed the privatization in countries such as Romania, Slovenia, and Bulgaria. *See* Ramet, *supra* note 27, at 98. In Romania, for example, only 700 of 6700 state enterprises had been privatized by 1994. *Id.*

benefit of both national business organizations and potential foreign business partners and investors. Consequently, when the new Commercial Code became effective on January 1, 1992, it repealed the International Trade Code,[37] the Economic Code,[38] and a section of the Civil Code.[39] The new Commercial Code also repealed certain other laws in their entirety, including such relatively recent enactments as the Joint Venture Law,[40] the Act on National Economic Planning,[41] and the Joint Stock Companies Act,[42] as well as parts of the Act on Economic Relations with Foreign Countries.[43] Finally, the new Commercial Code repealed several ministerial decrees,[44] federal government orders,[45] and highly-specific ordinances.[46]

The sheer breadth of the repeals demonstrates the magnitude

37. Section 772(2) of the Commercial Code repealed the International Trade Code No. 101/1963 Coll. COM. C. § 772 (Czech Rep.).

38. Section 772(3) of the Commercial Code repealed the Economic Code No. 109/1964 Coll. as amended by Act No. 82/1966 Coll., Legal Measure No. 13/1967 Coll., Act No. 69/1967 Coll., Act No. 72/1970 Coll., Act No. 138/1970 Coll., Act No. 144/1975 Coll., Act No. 165/1982 Coll., Act No. 98/1988 Coll., and Act. No. 103/1990 Coll. COM. C. § 772 (Czech Rep.).

39. Section 772(1) of the Commercial Code repealed § 352 of the Civil Code No. 141/1950 Coll. COM. C. § 772 (Czech Rep.).

40. Section 772(4) of the Commercial Code repealed the Act on Enterprise with Foreign Property Participation, No. 173/1988 Coll., as amended by Act No. 112/1990 Coll. COM. C. § 772 (Czech Rep.) The Act was more commonly known as the Joint Venture Law. *See* Drake, *supra* note 12, at 505.

41. Section 772(5) of the Commercial Code repealed the Act on National Economic Planning, No. 67/1989 Coll. COM. C. § 772 (Czech Rep.).

42. Section 772(6) of the Commercial Code repealed the Joint Stock Companies Act, No. 104/1990 Coll. *See also* DENYER ET AL., *supra* note 4, at 16 (stating that "[m]uch of the legislation relating to commercial matters passed over the last decade and some of the laws enacted or revised in 1990, such as the Joint Stock Companies Act, have been repealed" and new provisions for these areas placed in the Commercial Code of 1991).

43. Section 772(10) of the Commercial Code repealed the Act on Economic Relations with Foreign Countries No. 42/1980 Coll. as amended by Act No. 102/1988 Coll., and Act No. 113/1990 Coll., except for the provisions of sections 2, 3, 13-16, 17(2)(c), 18(1), 19(1)(i), 22(j), 43-56, 58, 64. COM. C. § 772 (Czech Rep.).

44. For example, § 772(38) of the Commercial Code repealed the Decree of the Federal Ministry of Foreign Trade and the Federal Ministry of Technical and Investment Development No. 64/1980 Coll., which governed procedures concerning "intangible industrial rights" and "know-how" in relation to foreign countries. COM. C. § 772 (Czech Rep.) Similarly, § 772(49) repealed another Decree of the Federal Ministry of Foreign Trade No. 104/1983 Coll., which concerned the importation of capital equipment. COM. C. § 772 (Czech Rep).

45. For example, § 772(14) of the Commercial Code repealed the Federal Government Order No. 132/1991 Coll., which stipulated when a joint-venture might be established without need for a license. COM. C. § 772 (Czech Rep.).

46. Section 772(86) of the Commercial Code repealed a 1978 Ordinance of the Federal Ministry of Foreign Trade, "stipulating fundamental conditions for the supply of glass products exported by the joint stock company Skloexport." COM. C. § 772 (Czech Rep.).

of the changes brought on by the promulgation of the new Commercial Code. The Commercial Code offers an effort to bring stability to the Czech business climate and economy. In light of the Czech political and economic history, it remains only to discuss, in some detail, the new legal framework of the development of private competition and a market economy.

II. A CURRENT CZECH ANALYSIS OF THE NEW COMMERCIAL CODE

The Velvet Revolution and the demise of a "Central Plan" resulted in a new legal scheme as well as new perceptions. This Part discusses, from a Czech perspective, basic changes in the law of contracts since the enactment of the Commercial Code. This Part also examines the application of the Commercial Code in international trade. Next, this Part analyzes the interaction between the Commercial and Civil Codes. This Part also recognizes both the application of the Commercial Code to specific commercial transactions, and the conflicts between the Commercial and Civil Codes. Finally, this Part discusses the retroactive application of the new legal norms.

A. Basic Changes in the Law of Contracts

The Commercial Code, along with other significant legal, political and social changes, influenced the burgeoning development of private competition and economic growth in the post-socialist Czech Republic.[47] The paramount characteristic of this development was the abandonment of a planned economy in favor of one based upon a free market. As far as contract law is concerned, there were six major changes from the socialist system, all of which were effectuated, at least in part, by the changes in the Commercial Code. These changes were: the liberalization of contractual freedom;[48] the dispositive, or subsidiary, legal regulation of business relations;[49] the increase in legal certainty;[50] the promotion of contractual freedom;[51] the assimilation of contracts and other business obligations into foreign and international commercial law;[52] and finally, the rekindling of the entrepreneurial spirit.[53]

1. The Liberalization of Contractual Freedom

Socialist law previously imposed "legal contractual duties."[54]

47. Bejcek, *supra* note 12, at 107.
48. *Id.* at 108.
49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.* at 108-09.
53. *Id.*
54. *See* Act No. 109/1964 Coll. §§ 115-18.

The new Commercial Code abolished legal duties and replaced them with voluntary contractual obligations, or *pactum de contrahendo*. Voluntary promises of performance have thus replaced the pseudo-contractual burden of obligatory contractual duty, *contradictio in adiecto*, that denied the principle of free contractual will. In common law terms, this would represent a shift from obligations arising out of "status" to obligations arising out of "contract" or "agreement/bargain."

This transition to voluntary contractual obligations represents a fundamental shift in the philosophy of contracts. Parties who have negotiated the terms of individual contracts are more likely to fulfill their freely-negotiated agreements. Moreover, the subject matter of a negotiated contract is within the ability of those entering into the contract to determine, because offerors would be unlikely to offer promises they could not fulfill, and offerees could be unlikely to accept offers if they could not perform on their side.

If either party to a freely-negotiated contract doubts that the other can perform, there are free market protections in place to help assure performance.[55] These protections include insurance and letters of credit. Admittedly, even in a Western free market legal system, there are some restraints on negotiations for a contract. The fundamental principle, however, is that the liberalization of contractual freedom has opened many possibilities for national and international business transactions.

2. *Dispositive Legal Regulation of Business Relations*

The mandatory provisions of the Economic Code and related laws prohibited any market deviation from the point of view of the time. The laws existed to satisfy the perceived needs of a dirigist economy, often without regard to the actual consequences or lost opportunities in the economic sphere. By contrast, the contracts provisions of the new Commercial Code allow parties to exclude or modify specific provisions of the Commercial Code, albeit with specific exceptions that are listed in the Code.[56]

For most purposes, the power to choose applicable rules will simplify the contracting parties' task of drafting a better contract. The benefits of this power will become apparent when the parties consciously decide to exclude, include or modify a specific provision. The knowledge that the parties can choose the rules and obligations under which they will perform, that they "can write their own contract," will encourage business partners to consider care-

55. *See* COM. C. §§ 682-91 (Czech Rep.) (discussing letters of credit).

56. Section 263 of the Commercial Code allows the parties to elect not to follow the provisions set forth in the Commercial Code in whole or in part, with the exception of certain specific provisions listed in the text of the section. COM. C. § 263 (Czech Rep.).

fully the advantages and disadvantages of specific provisions that would govern their agreement.

The Czech Civil Code, which has subsidiary application to certain business relations,[57] does not set forth a specific list of exceptions to the power to choose which sections of the Civil Code apply. In that sense, the Civil Code differs from the Commercial Code. Some may see this difference as an omission, one that is a disadvantage because there could be inconsistent provisions and solutions as between the two codes. Such an inconsistency would not promote the principle of legal certainty in business relations. Others may view the absence of a list of exceptions as an advantage, however, because it could allow the legal system to solve some problems over the years by experience, rather than by an inflexible statute. This view values risk over certainty and deems it wise to enable private parties to establish the rules of their business relationship.[58]

However one views the absence of a list of exceptions to the power to "write the contract" in the Commercial Code, it is clear that changes in the underlying legal framework allow the parties to construct a contract that is inherently more suitable for them. This new flexibility allows the parties to set the terms of their agreement, to anticipate areas of possible dispute and to provide in their contract for the mutually satisfactory resolution of potential problems. It is impossible to anticipate every problem, however, and for these unforeseen circumstances, parties should specify a dispute mechanism that would ease resolution of their disagreements.[59]

3. The Increase in Legal Certainty on Objective and Subjective Levels

The new Commercial Code is now an integral part of Czech private law although at first the legislation engendered legal problems and concerns that many were unprepared to handle. The shift from the relative commercial isolation of socialist Czechoslovakia to full participation in the world market was a great shock for many Czechs. Those educated only in the socialist system had little time or material support to adjust to the introduction of new

57. *See* Bejcek, *supra* note 12, at 108; HOULE, *supra* note 1, at 1; CIVIL CODE [CIV. C.] No. 40/1964 Coll. (Czech Rep.). The Czech Civil Code applies where the Commercial Code does not cover a specific situation such as the requirements for an offer or an acceptance.

58. Bejcek, *supra* note 12, at 108.

59. *See* Nadezda Rozehnalova, *Arbitration in International Trade from the Perspective of Czech Law*, *in* INTRODUCTION TO CZECH LAW, at 164 (Karen Schelle et al. eds, 1993) (discussing the possibility of arbitration as a means of dispute resolution). Alternative dispute resolution in the Czech Republic includes the newly implemented disputes resolution procedures in conjunction with independent arbitrators.

rules to regulate Czech business relations and contracts with diverse foreign legal systems.

With increased understanding of the new rules of the Commercial Code has come increased legal certainty on both the subjective and objective levels. The positive experiences that many businesses had with the Commercial Code also brought greater certainty and confidence in the viability of the new business rules. For example, the exclusion of arbitrary state interventions has assisted in raising the credibility of the new Commercial Code's applicability to the new market economy.

Initially, however, there was uncertainty about the interaction in areas possibly covered by the Civil Code and the Commercial Code. As yet there is a lack of definitive court rulings on issues of possible overlap between the two codes.[60] This lack of precedent has not substantially hindered economic development. Moreover, continuing development and confidence in the new system of legal regulation are essential to the realization of the ultimate goal of privatization of business. Where these areas of potential overlap exist, it is once more incumbent upon parties to specify appropriate resolutions in their contracts as expressly as possible.

4. The Promotion of Contractual Freedom

The new Commercial Code applies to both nominate contracts and innominate contracts. "Nominate contracts" are common business contracts, and the subsidiary provisions of the Code apply to parts of these contracts that might otherwise be ambiguous or incomplete because the parties have left certain issues open. "Innominate contracts" do not fall within this purview. These are the "unclassified" contracts of Roman law,[61] one of the ancestors of traditional Czech legal thought. There are four principal types of innominate contracts: *permutatio*,[62] *de aestimato*,[63] *precarium*[64] and *transactio*.[65]

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60. *See* Ilona Schelleova, *Courts of Law, Notaries and Advocacy*, *in* INTRODUCTION TO CZECH LAW 63-69 (Karel Schelle et al. eds., 1993) (explaining how the Czech judiciary is arranged in accordance with the Czech Constitution).

61. BLACK'S LAW DICTIONARY 789 (6th ed. 1990). *See also* Renata Vesela & Michaela Zidlicka, *Roman Law from the Ancient Times to Our Days*, *in* INTRODUCTION TO CZECH LAW 3, 10 (Karel Schelle et al., eds., 1993) (discussing the historical relationship between Roman and Czech law).

62. BLACK'S LAW DICTIONARY 1140 (6th ed. 1990) (defining *permutatio* as "exchange or barter").

63. *See id.* at 398 (stating that "[i]n Roman law, one of the innominate contracts, and, in effect, a sale of land or goods at a price fixed . . ., and guarantied by some third party, who undertook to find a purchaser"). *Id.*

64. *See id.* at 1176. "A convention whereby one allows the use of a thing or the exercise of a right gratuitously until revocation." *Id.*

65. *See id.* at 1496. "The settlement of a suit or matter in controversy, by the litigating parties, between themselves, without referring it to arbitration."

If parties make an agreement in one of these "unclassified" areas, they have created an "innominate contract" even though they may have intended to create a "nominate contract." If, for example, the parties sign a contract under the name "franchise agreement," it will be nevertheless an "innominate contract" because the Czech law does not regulate franchise contract as a "ready-to-use" type of nominate contract. On the other hand, the intent of the parties to make an innominate contract will prevail even if they have labeled their contract as one that is "nominate." The parties choose, for example, a contract obtaining *inter alia* all features of a purchase contract. Nevertheless, the parties want to avoid some binding provisions of a nominate contract and therefore they chose an innominate contract. The parties' will has to be respected. Such is the continuing force of this aspect of Roman law.[66]

If an innominate contract is ambiguous or incomplete, the subsidiary provisions of the Commercial Code concerning nominate contracts will not clear up the ambiguity or complete the contract. For example, an incomplete franchise agreement cannot be "supplemented" by provisions of purchase contract, or employment contracts. Only general provisions on contracts affecting all contracts, without regard to the type of contract, can be used. Innominate contracts therefore require extraordinary care in drafting to avoid ambiguity or omission. In exercising this care, however, the parties enjoy significant contractual freedom.

5. The Assimilation of Contracts and Other Business Obligations into Foreign and International Commercial Law

Even before the promulgation of the new Commercial Code, Czech entrepreneurs had to adapt to the expectations and requirements of foreign business partners. This was particularly true when a choice of law provision in a contract between a Czech partner and a foreign partner required interpretation and enforcement according to the foreign legal system. The implementation of many business law pacts and customs in the Commercial Code has facilitated this adaptation.[67]

Many large foreign corporations, especially multi-national corporations, use choice of law provisions in their contracts with partners in foreign countries. A multi-national corporation, for instance, finds it easier to specify its home country's law rather than to vary its contractual obligations with each country in which it makes deals. Contracting parties in two different countries may also specify that the law of a third country will govern the trans-

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Id.

66. Bejcek, *supra* note 12, at 108.

67. *Id.* at 109-10 (stating further that such provisions will bring about uniformity with respect to the rules governing transactions with foreign parties).

action as long as the law of that third country bears a rational relationship to the subject of the contract.[68]

Choice of law provisions can actually enhance the Czech Republic's prospects for trade because a foreign investor or trading partner who is unfamiliar with the Czech legal system may prefer to deal with a Czech partner who is willing to transact business according to the foreigner's legal system. A choice of law provision specifying the non-Czech legal system requires the Czech partner to learn about and adjust to the foreign legal system. However, foreign partners will soon learn that Czech business law, as recently revised, more closely approximates and incorporates many of the essential legal norms and business rules found in their own legal systems, whether the common law or civil law system.

6. Rekindling the Entrepreneurial Spirit

Business experience with the new Commercial Code since January 1, 1992, has generally been positive. The Code abrogated outdated laws from the socialist era that could not regulate business and trade in the post-socialist Czech market economy. The new Commercial Code also replaced economic rules and policies inconsistent with market economy that had hindered economic development and the natural evolution of market relations.

In short, the new Commercial Code played a very significant role in rekindling the entrepreneurial spirit in the Czech Republic by providing the legal framework for commerce in a market economy. By emulating the legal framework of its Western trading partners, the Czech Republic can entice investment and spur economic development.[69]

B. Application of the Commercial Code in International Trade

The repeal of the Code of International Trade transferred all international business matters to the provisions of the Commercial Code. One result of this transfer has been the unification of the rules for domestic subjects of business regulation, such as eliminating earlier anti-competition preferences formerly available only to some entities, but not to others.[70] Another result has been the equalization of domestic entities with foreign businesses, which can now compete on the same terms and conditions.[71] This has already had an effect upon sourcing, because domestic entities can

68. Act of International Private and Process Law, Act No. 97/1963 Coll.

69. Salani & Sloam, *supra* note 34, at 53-54.

70. For a general discussion of current anti-competition preferences, see Russell Pittman, *Some Critical Provisions in the Antimonopoly Laws of Central and Eastern Europe*, 26 INT'L L. 485 (1992) (giving foreigners the same rights and obligations in business as Czech citizens).

71. *See* COM. C. §§ 24 (3), 43 (2) (giving foreigners equal protection against unfair competition).

now purchase materials or services from abroad. This has also had an effect upon distribution, because domestic entities can now sell their products wherever they can find buyers.

If a Czech partner and a foreign partner choose to have Czech law apply to their transaction, they will find that the Commercial Code applies to both of them equally. According to the generally accepted principles of conflict of laws, a foreign court generally would be bound by the private international law of the country whose law governs the transaction.[72]

The Czech Commercial Code does not prohibit regulation of transactions with foreigners. Instead, the Code supplements international agreements that are part of the Czech legal system unless the contract between the Czech and foreign partners excludes those international agreements.[73] In the absence of international agreements, foreign business partners have the same rights as their Czech business partners because, again, the Commercial Code treats foreign parties as business equals to Czech entities.

C. The Commercial Code and the Civil Code

So far, the Czech Republic has rejected the concept of a uniform commercial civil code such as that of Switzerland. Instead, as is true in some European countries such as Germany and Austria, some business relations fall into the sphere of the more specialized Commercial Code, while others fall into the sphere of the more general Civil Code.[74]

Because a given business may be regulated by the Commercial Code in some instances and by the Civil Code in other instances, questions arise concerning the interrelationship of the provisions of these two codes.[75] Certainly, it is desirable to avoid inconsistency between the two codes. Because the two codes themselves do not solve the more complex issues of their interrelationship, scholars using methods of statutory analysis have made suggestive interpretations of the codes to solve these issues.[76] Authoritative judicial decisions interpreting the provisions in the Czech courts are still lacking.[77] Anticipated amendments to the

72. *See, e.g.*, RESTATEMENT (SECOND) OF CONFLICTS, §§ 186-88 (1971) (discussing the general principles on the validity of contracts and contractual rights).

73. *See* United Nations Convention on Contracts for the International Sale of Goods (CISG), opened for signature Apr. 11, 1980, S. Treaty Doc. 98-9, 19 I.L.M. 671. Article 6 of the CISG, for example, allows parties to either exclude the application of the Convention or, subject to limitations, "derogate from or vary the effect of any of its provisions." *Id.*

74. COM. C. § 261 (Czech Rep.).

75. *See generally* DENYER ET AL., *supra* note 4, at 16.

76. *Id.* at 19

77. *Id.*

Civil Code will affect its relationship to the Commercial Code. Recently, there is the tendency to create a unified private law code in the Czech Republic. For now, we can say that, as a general rule, the Civil Code and other civil law regulations apply to business obligations either when the Commercial Code is silent,[78] as is the case regarding misrepresentation or mistake,[79] or when the Commercial Code merely supplements general regulations in the Civil Code,[80] as is the situation regarding business relations involving a lien or contract penalty.[81]

D. Application of the Commercial Code to Specific Commercial Transactions

The Czech legal system recognizes four types of obligations, although their classification has developed from practice rather than from definitions in a statute. The chief significance of these four types of obligations lies in how they are regulated by either the Civil Code, the Commercial Code or both codes. The four types of obligations are: relative commercial transactions; absolute commercial transactions; facultative commercial transactions; and, absolute non-commercial transactions.[82]

1. Relative Commercial Transactions

Relative commercial transactions are obligations between entrepreneurs. However, as a condition to this obligation, each party to the contract at the time of contracting must be a businessperson.[83] Furthermore, the contract must concern the parties' business activity.[84] A relative commercial transaction also arises when there is an obligation between the state or a self-governing territorial unit on the one side and an entrepreneur on the other side, as long as the business transaction contemplated can satisfy some

78. *Id. See also* COM. C. § 1(1) (discussing the scope the Czech Commercial Code).

79. CIV. C. 586 § 49(a). (Czech Rep.).

80. COM. C. § 1(1) (Czech Rep.).

81. COM. C. §§ 299-302 (Czech Rep.); CIV. C. § 151(a) - (v), § 544-45 (Czech Rep.).

82. Bejcek, *supra* note 12, at 111.

83. COM. C. § 261 (1) (Czech Rep.) (stating, specifically, that the Business Obligation Part of the Code pertains to those transactions between entrepreneurs).

84. *Id.* This might be compared to Article 2(a) of the Convention on the International Sales of Goods, which excludes its application if the sale involves "goods bought for personal, family or household use, unless the seller, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the goods were bought for such use[.]" United Nations Convention on Contracts for the International Sale of Goods, opened for signature Apr. 11, 1980, S. Treaty Doc. 98-9, 19 I.L.M. 671 (to be codified at 15 U.S.C.). *See* COM. C. § 261 (1) (Czech Rep.).

public need or purpose.

2. Absolute Commercial Transactions

Absolute commercial transactions are obligations whose "absoluteness" arises from the possible application of the Commercial Code to all transactions of that type without regard to the nature of their contracting parties, even non-entrepreneurs, or the intended use of the "discharge" or contract fulfillment, which need not be intended for business purposes. Approximately twenty legal relations in the Commercial Code are absolute commercial transactions.[85] Among them are relations between the founders of companies; partner-company relations; relations among partners; relations based on stock exchange transactions and brokers' services; relations arising out of securing obligations based on absolute or relative commercial transactions, such as bank guarantees.[86]

All of the actions classified as "absolute commercial transactions" are by definition entirely commercial. It is difficult to imagine anyone who is involved in one of the listed transactions, but not engaged in a "commercial act." For example, the relation between a bank (i.e., an entrepreneur) and a citizen (i.e., a non-entrepreneur), concerning a bank guarantee, is an "absolute commercial transaction."

3. Facultative Commercial Transactions

Facultative commercial transactions are neither relative nor absolute. Instead, they are "optional" or "contingent" transactions regulated by the Commercial Code according to the written agreement of the parties.[87] In short, the parties can "opt into" the Commercial Code.

Opting into the Commercial Code is a problematic example of a choice of law available to Czech domestic parties. It allows consumers and entrepreneurs to reject the mandatory provisions of the Civil Code in favor of regulation by the Commercial Code. As long as the parties are not engaged in a relative or absolute commercial transaction, they are free to abandon the relatively strict regulation of the Civil Code and obtain the rights and obligations of parties under the Commercial Code.

Parties seeking regulation by the Commercial Code are trying to avoid the perceived disadvantages of the Civil Code, such as the provisions concerning nominate or innominate commercial law contracts. If the parties have an innominate contract under the Commercial Code, they are subject to only the general provisions

85. COM. C. § 261(3)(a)-(e) (Czech Rep.). *See also* HOULE, *supra* note 1, at 55 (discussing the various legal relations that are commercial transactions).

86. COM. C. § 261 (2) (Czech Rep.).

87. *Id.* at § 262(1)- (2).

of the Commercial Code and those provisions of the Civil Code reflecting its position toward the Commercial Code.[88]

4. Absolute Non-Commercial Transactions

Absolute non-commercial transactions are contracts not regulated by the Commercial Code in the form of specific types of business contracts. Instead, the Civil Code regulates these contracts.[89] Examples of absolute non-commercial transactions are contracts for the purchase of land, employment contracts[90] and insurance contracts.[91]

E. Conflicts Between the Commercial and Civil Codes

Provisions for nominate contracts under the Commercial Code govern relative transactions, absolute transactions, and facultative transactions. First, the provisions apply to relative transactions according to the parties to the contract and purposes of the contract, if the contract concerns business activity of both parties.[92] Second, the Code provisions apply to absolute transactions without regard to the nature of the subjects or the purpose of the contract,[93] but including the relations based on securing obligations that arise from absolute and relative transactions.[94] Finally, they apply also to facultative transactions without regard to the nature of the parties or the purpose of the contract, including contracts to secure other obligations, so long as the guarantor knew of or consented to the given type of security.[95]

Although the relationship between the Civil and Commercial Codes is complex, further complications arise by the very nature of the regulation which should apply in individual cases. The issue of whether certain regulations in each Code govern turns upon whether the appropriate provision of the Code is mandatory or dispositive.

The provisions of the Economic Code of 1964, which was chiefly an instrument of dirigism, were mostly mandatory. They were predominantly public law norms, in keeping with the thesis that there was nothing of a private law nature in a socialist economy, because all transactions were of a public law nature. In a free market economy, Civil Code and Commercial Code regulations

88. Bejcek, *Supra* note 12, at 112.
89. CIVIL C. §§ 588-610 (Czech Rep.). *See also* COM. C. § 261(6) (Czech Rep.) (discussing the regulatory authority of the Civil Code with respect to certain contracts).
90. CIVIL C. §§ 724-46 (Czech Rep.).
91. CIVIL C. §§ 788-828 (Czech Rep.).
92. COM. C. § 261(1) (Czech Rep.).
93. *Id.* § 261(3).
94. *Id.* § 261(4).
95. *Id.* § 262(3).

are generally based on the preference of private law over public law. If the state has any proper role in setting other rules of business behavior, it should be the role of establishing rules that complement or facilitate business transactions. Binding rules in the form of contractually unchangeable and mandatory norms should be enacted only to create and maintain conditions necessary to a functioning free market.[96]

The impact of regulation upon the freedom of entrepreneurs to make decisions justifies a requirement that one should be able to discern whether a provision is mandatory or dispositive from a plain reading of its language. Ideally, the contract should express its intentions and obligations so clearly that there would be no need to fill any contractual gaps. Also, the language of the contract would be so plain that there should be no need to ask a court for judicial interpretation of a provision.

The axiomatic feature of a legal state, namely the requirement that reference to published law determine a citizen's rights and duties, also militates in favor of determining the nature of all legal norms with great certainty. The Czech Constitution itself expresses a list of the basic rights and liberties of all Czechs.[97] Within the sphere of business, this should also mean that everyone ought to know clearly whether a provision in a code is peremptory or dispositive. In private law matters, areas where the public interest of society is generally not concerned, the agreement of the parties ought to control. Dispositive legal regulations should be secondary, filling in only when the primary agreement is insufficient.

For example, if a regulation restricts private contracts without defining the conditions under which those restrictions apply, then those persons potentially affected by the law will live in uncertainty and their freedom to contract will be diminished. If a businessperson believes that a legal restriction applies to a private contract, that individual would not be likely to test that restriction if there is good reason to believe it is mandatory. On the other hand, if the businessperson believed the legal restriction was only subsidiary, that individual might learn for the first time in court that the regulation was in fact mandatory and that perhaps the contract is void.

The Czech Commercial Code adequately satisfies the legitimate claim for making a distinction between mandatory and dispositive norms by its inclusion of an exhaustive list of provisions

96. The conditions would be those such as guaranteeing contractual freedom, equal access to resources or opportunities, protection of bona fide, third-party rights, and measures that support free competition rather than monopolies or cartels.

97. Wiktor Osiatynski, *Rights in New Constitutions of East Central Europe*, 26 COLUM. HUM. RTS. L. REV. 111, 123-28 (1994).

concerning obligations.[98] The Civil Code makes the distinction less clearly. It based the distinction between peremptory and "dispositive" or "subsidiary" obligations upon the "nature of the relation" involved.[99] This is somewhat obscure and uncertain because although private persons may differ on the nature of particular relations, only a judge can decide finally what "the nature of the relation" is, as a matter of law.

F. Retroactive Application of the New Legal Norms

The new Commercial Code became effective at a time when many economic relations were based on socialist laws and regulations, most of which were inconsistent with the new principles contained in the Code. This gave rise to the issue of the Code's applicability to relations entered into before January 1, 1992. There were three options.[100] The first option was to give the Commercial Code direct retroactive effect.[101] The second option was to give the Code only an indirect retroactive effect.[102] Finally, the third option was to maintain the effectiveness or status quo of the existing contracts. In the end the last option prevailed.[103]

1. Direct Retroactive Effect

The first option considered was to declare void all the pre-Commercial Code contracts found to be inconsistent with the new provisions of the Code. This would have impaired legal certainty in existing business relations. It could also have impaired future business relations because this option, once exercised, might be used again and nullify contracts entered into after the Commercial Code came into effect. It would have been generally a strike against legal certainty. There would also have been problems in deciding which contracts were void in their entirety, which were void in part, and which were still valid. In order to avoid the chaos inherent in making essentially arbitrary determinations of contract validity, Czechoslovakia rejected this option.

2. Indirect Retroactive Effect

The second option was to deem the existing contractual relations valid if they were valid under the old legal system, but to apply the new provisions of the Commercial Code to them.[104] This would have given the Commercial Code an indirect effect upon

98. COM. C. § 263 (Czech Rep.).
99. CIV. C. §§ 1(1)-(3) (Czech Rep.).
100. Bejcek, *supra* note 12, at 114.
101. *Id.*
102. *Id.*
103. *Id.*
104. Bejcek, *supra* note 12, at 114.

pre-existing contracts. Perhaps the issue of its effect would have arisen only in cases of dispute over contractual provisions.

Czechoslovakia rejected this option because the circumstances of forming a contractual relation in a dirigist economy were qualitatively miles away from the circumstances already existing when the Commercial Code became effective. A chief reason was that the earlier business relationships were often negotiated under pressure and the earlier means of enforcing these relationships were no longer available.

3. *Status Quo*

The third option, the one chosen, was to maintain the old legal system under which the earlier relationships were created, including contracts related to liability, until these earlier relationships expired.[105] In effect, the transition period envisioned a dual legal system: one for relationships created before the Commercial Code and one for relationships created when the Code came into effect. With minor exceptions,[106] this is the current situation. One advantage of this particular option is that it allows parties to modify their existing relationships by agreement or to abolish their contracts and negotiate them again using the provisions of the new Commercial Code.

III. THE CZECH LEGAL SYSTEM AS PART OF THE WORLD OF INTERNATIONAL COMMERCE

Although the legal framework for creating contracts naturally varies from country to country, there is a gradual unification of written commercial law. The practices of businesspeople around the world are also becoming harmonized. One of the values of the Czech Commercial Code is that, along with the new Civil Code, it grew out of this trend to discern and adopt internationally accepted standards of contract formation. Like the former Code of International Trade, it seeks acceptance from foreign partners dealing with Czech businesses.

The legal regulation of contracts in market economies is based upon well-known and seldom-modified principles, which stem from the "theory of perfect contract." These principles, which are prerequisites for the law of contracts and are familiar to lawyers in most countries, are now part of the new Czech business law. These principles include a valid offer or *offerta*;[107] a proper accep-

105. COM. C. § 763 (1) (Czech Rep.).

106. COM. C. § 763 (1), § 764 (Czech Rep.).

107. The offer, verbal or written, must be clear to specify the offeror's intention distinctly. Not every offer has the binding effects of the *offerta*. First, the subject matter of the proposed contract must be specific, as well as the performance expected from the would-be partner, such as the terms of his participation in the contract. A communication addressed to numerous per-

tance;[108] adequate counterperformance or consideration;[109] the absence of fraud, duress, or relevant error, also known as the principle of free will;[110] legal capacity of the parties;[111] harmony with public policy;[112] the observance of proper, legally determined form;[113] and harmony with special rules regulating the specific type of contract.[114]

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sons will generally not be an offer, but instead, an invitation for offers which may then become contracts through acceptance. Czech law may sometimes set minimum contract requirements for some types of contractual offers. Additionally, although an offer must be made expressly, with a real intention to be bound, an acceptance need not always be express. If the offer meets these requirements, the offeror will be bound by it.

108. Acceptance is an objective manifestation of voluntary agreement by words or deeds to the terms of an offer. Typically it is a successive expression of consent to the offer and its content. Acceptance must be a manifestation of the free will of a contracting party, made with the intention to create a contract. Acceptance may be informal, so long as a reasonable person could interpret the behavior as agreement to the terms of the offer. Acceptance must be by real behavior, however, and not just tacitly or by inaction. This is tagged as a principle of true mutual acceptance, when both parties enter the contract willfully, freely, and intentionally. The period in which acceptance may normally be made should be a reasonable one, subject to varying circumstances of individual cases, such as particular time requirements of offeror that are made known as a condition of the offer. Where there is excessive delay in communicating acceptance, an offer may lapse. *See* A DICTIONARY OF LAW 4-5 (3d ed. 1994).

109. Every contract is connected with the principle of mutual counterperformance or consideration. A promise should be binding only if each of the parties provides something valuable to the other, value not being only money or goods, but also forbearance or abandonment of a claim. Mutuality of the counterperformance is regarded as sufficient if both parties give the performance considered to be sufficient when the contract was made.

110. The exercise of genuinely free will in contract negotiation requires that both the offer and acceptance are made without pressure, fraud, or material error. Because business relations require high levels of certainty, the provisions concerning errors in contracts should not be subject to subsequent misuse by the other party. The effects of a legal error should thus be covered by its character.

111. Legal capacity of the parties is a *sine qua non* representative of the conditions protecting public interests and lawfulness. Given the higher level of legal certainty needed in business relations, the business law regulations require some additional formal prerequisites of legal capacity to act on behalf of business entities.

112. The contract must also be in harmony with public policy; it must be lawful, permitted, and observant of public peace and good manners. Harmony with public policy should, in the first instance, be protected by the framework of contract-making. Even where a contract is considered perfect, the law still includes provisions to avoid misusing the law. A claim will not enjoy legal protection from the court if the contract is contrary to the rules of fair trade.

113. Because formal elements of a contract rank among the legally regulated requirements, it might also be possible to place observance of the proper form of contracts under the label of harmony with the public interest.

114. Very few contracts will be perfect if only the basic requirements are met. Most of the contractual relations exist on the basis of legally regulated types of contract, with special prerequisites for the rise, duration, fulfillment,

CONCLUSION

While these and many of the other legal principles described in this Article are familiar to Western lawyers and business investors, they are new concepts for business and investment in the Czech Republic. Today, contracts are more than an enforceable writing that may evidence a bargain or agreement between business partners. Contracts embody mutual promises of performance that, if not fulfilled, must be remedied by the party that does not fulfill its obligations. As Czech businesses and those lawyers who advise them continue to adjust to the new regulatory and free market climate, foreign business partners will have greater and greater confidence in the legal certainty of the contract they make with Czechs.

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termination and various other features. A contract must thus also comply with any special rules that may regulate a specific type of contract.