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**Public Benefit Corporation -
A New Type of a Civic Organization in the Czech Law**

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I. Needs and Expectations

The legal framework for the so called not-for-profit organizations in the Czech Republic was formed early after the Velvet Revolution by adopting the Act No. 83/1990, On Association of Citizens and later by amendments to the Act No. 40/1964, Civic Code, in a complete text given by the Act No. 49/1992.

The Act No. 83/1990 regulates the registration of the **civic association** as a voluntary membership organization with all rights of an independent legal person. A civic association may be established by three citizens and it should not be misunderstood for a political party, for an establishment of a church nor for a business company or a chamber of professionals, all of them being regulated by special laws.

The Civic Code defines a legal person in general and a **foundation** as a special one. A foundation may be established by natural or legal persons, as well as by a will, for some of the generally defined public benefit purposes, like development of cultural values and other humanitarian needs, care for human rights and preservation of nature and environment, as well as care for the architectural monuments and cultural heritage. It follows from the context of the traditional legal framework, that the foundation is to be interpreted as an establishment that cares for funds dedicated by the founder(s) to be used by third persons according to specified regulations and for a specified purpose.

The amended text of the Civic Code refers also to a special (at that time federal) law to define in more detail the framework for activities of foundations.

For foundations and for civic associations there exist general tax laws provisions of certain exemptions from taxes and fees.

The vague definition of foundations and problems concerning business related activities of civic associations caused a controversial discussions about principles of not-for-profit activities, as well as whether and how should be such entities subsidized and supported from public resources.

As a consequence, the drafting of the law on non-profit organization, announced by the Ministry of Finances in 1992 raised many expectations.

Some people, including many foreign friends and experts, looked for an umbrella law, that would deal with all those civic

organizations that are motivated not by the profit but by other public or mutual interests.

Others warned, that the foundations and civic associations are already defined and regulated by existing laws and that it would be appropriate to amend these laws as to prevent foundations being run as civic associations and vice versa, as well as to allow for organizations that would provide public benefit services under strict and transparent regulations. It was also required to introduce measures that would minimize risks of misuse of tax exempts and other benefits given to civic organizations by the law.

II. Concept of a public benefit corporation

The drafting procedure of the new legislation for the civic organizations continues on three levels. The Office for Legislation and Public Administration prepares the new law on foundations, the Ministry of Finances has prepared the draft of a law for non-profit legal persons and the Ministry of Interior is preparing an amendment to the Act No. 83/1990, On Association of Citizens.

The work of the Ministry of Finances culminated in September 1995, when the Czech Parliament adopted the Act. No. 284/1995, On Public Benefit Corporations (in Czech "obecně prospěšné společnosti").

Already the name of the Act shows, that the expectations of those who wanted a general law for the not-for-profit organizations were not fulfilled. The new law defines a new and complementary type of a civic organizations to foundations and civic associations.

The Public Benefit Corporation (hereafter also a **PBC**) is to provide public benefit services to all on equal access rights under well defined conditions. It is not excluded from making profit of its activities, but such a profit must not be distributed to the founders, members of governing bodies nor to be used for employees. Any profit has to be assigned to a reserve fund of the PBC to cover any future possible losses, first of all and it should be used for the extension of the services for which the PBC was established, after all. In this way the new law defines for the first time the **not-for-profit status**.

A PBC may be established by a natural person or a legal person. This includes also the Czech Republic and any municipality. The founder may be individual, but there may be more founders as well. The founder(s) have to explicitly define in the **founding document** or agreement the name and seat of the PBC, the type of public benefit services it should provide and the conditions, under which the services are to be provided, as well as whether it is established for an indefinite period of time or for a finite one. It is also upon the founder(s) to nominate the **Board of Trustees** and to decide, how the Board should make decisions. The law also requires from the founder(s)

to prescribe, how is to be published the annual report.

The Law gives the founder(s) an optional right to specify the circle of persons, out of which the Trustees may be nominated as well as the proportion of them to be restricted in such a way. It is also possible to prohibit in the founding document to sell or donate certain property given by the founder(s) to the PBC and what should be done with the assets of the BPC upon liquidation. On the other hand, the founder(s) may specify that some of the services provided by the PBC may be changed under specific conditions.

III. Other important features

The BPC is to be registered by the territorially relevant **Register Court** in a manner similar to that applied for business companies. In many respects the regulations governing the cessation and liquidation of the PBC are similar to those of the business corporations. However, the Law allows the founder(s) to override the decision of the Board of Trustees to end the operations of the PBC under the condition, that the founder(s) will guarantee the necessary operations.

The Board of Trustees of the PBC is to be nominated by the founder(s) and the Law prescribes the change of it by thirds and does not allow a Trustee to serve without interruption for more than two terms, which are three years long. The Trustees may not be paid in any way nor is it allowed to compensate them for other than travel expenditures and in a way that is not regulated by some law.

The Board responsibilities include publishing the Statute of the PBC, to decide on the budget, annual report and annual balance of incomes and expenditures, as well as on changes in property. The Board may also nominate a Director and decides on its salary. Having all these responsibilities in mind, it is also required that Trustees may not be employed by the PBC nor be in any close relation to employees of it.

The Director of the PBC must not be a member of the Board of Trustees, but may take part in its proceedings.

Any PBC that uses the property of the state or has annual incomes greater than 3 million Czech crowns must have besides the Board of Trustees also a Supervisory Board of three members and its books must undergo **auditing** by a chartered auditor.

The **business activities** of a PBC are limited to those connected with its purpose and any additional ones, under the condition, that such additional activities will not hinder provision of main services and the income from them will allow for more effective use of its property. PBC may not participate in a business company nor it may have its branches outside of the Czech Republic.

The PBC is to be financed from the **assets** given to it by the

founder(s), from gifts, acquired heritage, donations and its own funds. The PBC may apply for grants and donations of the state or municipalities in open tenders, but such funds may not be provided from more than one source for the same activity.

Finally, it is required by the Law from the PBC to publish regularly **annual reports** that should contain both description of the services provided as well as account for its incomes and expenditures and the status of its current overall property. Such reports are considered to be public documents.

The Law allows for **sanctions** with respect to a PBC that is not providing the public benefit services as stated in the register under respective conditions, or that has violated the business restrictions imposed by the Law, or that is not reporting as required by the Law. Such a PBC may not make use of the benefits given to it by tax exemptions for the given fiscal year and must pay the property tax in the succeeding fiscal year. It may be also dissolved by the decision of the court upon the proposal of a state organ, a founder or any effected person if for more than a year there was no meeting of the Board of Trustees and if other provisions of the Law are not duly respected or are otherwise violated.

IV. Some drawbacks of the Law

As already mentioned, the PBC is to be governed by a Board that is more a Board of Trustees than a Board of Directors. The Board has no self-perpetuation capacity, since its nomination is fully dependent on founder(s) decisions. The Law does not solve the situation of non-existent founder(s), as far as perpetuation of the Board is concerned. However, the relevant Chief of the State District Office has the right to call off a Trustee from its position in those cases when the Trustee no longer fulfils the pre-requisitions for such a function. However, there are no provisions that would enable to call off a Trustee in a case of his or her inactivity or non-loyalty or any other breakage of good morals.

In the case that founder(s) do not specify how the assets and property of a PBC should be used upon its liquidation, these assets will be transferred to the community where is the seat of the PBC or even to the state through the relevant State District Office.

The Law does not define mechanisms by which a PBC may be supervised by some authority other than its Board of Trustees or its Supervising Committee. Therefore, it is upon the responsibility of founder(s) and/or general public to exercise the necessary degree of supervision.

V. Conclusions

Despite some drawbacks mentioned above, the new Law on Public Benefit Corporations is an important part of the emerging legislation for civic society in the Czech Republic. It defines

clearly the not-for-profit status, while introducing the requirements for transparent reporting and accounting connected with it, as well as sanctions for not meeting the requirements of the Law.

Having in mind the same development with regard the draft of the Law on Foundations, we may hope to have in force an acceptable and workable set of laws governing the Third Sector in the Czech Republic already since the Fall of 1996.

Public Benefit Corporations Short Overview

Petr Pajas, Canter for Democracy and Free Enterprise

1. **Types of civic [not-for-profit] organizations and governing laws**
 - a. Civic Associations and Trade Unions
 - Law No. 83/1990, On Associations of Citizens
 - b. Foundations
 - Law No. 40/1992, Civic Code
 - c. Political Parties
 - Law No. 424/1991, On Association in Political Parties and Political Movements
 - d. Churches and Religious Organizations
 - Law No. 161/1992, On Registration of Churches And Religious Societies
 - e. **Public Benefit Corporations**
 - Law No. 248/1992, On Public Benefit Organizations and Amendments of Some Other Laws
2. **Main required features of Public Benefit Corporations (P.B.C.)**
 - a. Founder(s)

Any natural person, the Czech Republic or any legal person may individually or together found a P.B.C.

The rights and responsibilities of a founder are taken over by its legal successor
 - b. Purpose

To provide public benefit services on equal basis for all relevant parties and according to registered conditions
 - c. Status of Not-for-Profitness

Not to distribute any annual profit to founder(s), members of governing bodies nor to employees; use only after transfer to a reserve fund and for purposes registered
 - d. Founding document:
 - i. Obligatory content:
 - (1) name, seat and identity code of founder(s)
 - (2) name and seat of the P.B.C.
 - (3) type of public benefit services provided
 - (4) conditions for provision of services
 - (5) time limits for existence of the P.B.C., if any
 - (6) any additional activity allowed

- (7) name, address and identity numbers of members of the Board of Trustees and of the Supervising Committee, if any
- (8) value and identification of property assigned by founder(s) on individual basis
- (9) way of publishing annual reports
- ii. Facultative content:
 - (1) constrains on choice of Trustees
 - (2) limitations on number of Trustees to be chosen under constrains
 - (3) constrains on the use of the property assigned by founder(s)
 - (4) provision allowing the Board of Trustees to change some conditions under which the public benefit services might be provided
 - (5) determination of another P.B.C. to which the remaining assets should be transferred upon eventual liquidation or provision for the Board of Trustees to make such a decision

e. Registering

At the Register Court into a Register of B.P.C. according to the proposal of founder(s) or empowered person; the proposal must be accompanied by founding document signed not earlier then 90 days ago.

f. Data Registered

Same as 2.d.i.(1) to 2.d.i.(3) and 2.d.i.(7), as well as

- way of decision making of the Board of Trustees
- kind of any additional activity, if to be executed

It must be proved by documents, that P.B.O. has in staff persons able to respond for particular activities, for which it is required by Law No. 455/1991, On Craftsmanship Business

g. Board of Trustees (B.T.)

B.T. is a statutory organ of the P.B.C. compost of at least 3 natural persons. Members of the B.T. are appointed by the founder(s), if not determined otherwise in the founding document.

h. Supervising Committee (S.C.)

S.C. is a supervisory organ of the P.B.C. of 3 to 7 members.

Founder(s) appoint the members of the first S.C.

S.C. is an obligatory organ in following cases:

- i. P.B.C. uses or was given into ownership a property of the state or a municipality
- ii. P.B.C. has annual income more then CZK 3,000,000 (USD 100,000)

i. Requirements on Members of B.T. and S.C.

A Trustee must be eligible for legal responsibility

and may not be a person indicted for a criminal act. It may not be employed by the P.B.C. nor be in a close relation to any employee of the P.B.C.

j. Terms for members of B.T. and S.C.

The term of a Member of B.T. or of the S.C. is 3 years long. It may be repeated without interruption only twice.

Every year one third of terms must terminate.

The membership in the B.T. and S.C. ends in case of

i. termination of the term

ii. death

iii. resignation

iv. dismissal by a founder in the case, when the person does not fulfil the requirements set by the law (see 2.i)

In case of non-existence of a founder or a person taking over its legal rights the right of calling off a member of B.T. or S.C. goes over to the Chief Executive Officer of the relevant State District Office.

Unoccupied positions in the B.T. or S.C. must be filled by cooptation on the next meeting of the organ.

k. Responsibilities of the B.T.

These include:

i. to issue not later then 6 month after registration a Statute, which regulates in more detail the inner organizational arrangements of the P.B.C. respecting the foundation document

ii. to approve changes to the founding document in parts not explicitly excluded from a change by founder(s)

iii. to decide on cessation of the P.B.C. and on the P.B.C., which should take over the remaining property

iv. to take care of the fulfilment of the purpose for which the P.B.C. was established

v. to approve the annual account and annual report of the P.B.C.

vi. to decide on kind and scope of additional activities that go beyond the framework set up by the founding document

vii. to approve selling or commissioning real estate property of the P.B.C. or letting it for more then one year, unless the Statute does not allow for a shorter period only

viii. to appoint and dismiss the Executive Director, supervise its activities and determine its salary

ix. to decide on other issues according to the provisions of the founding document

The B.T. convenes at least twice a year.

- l. Responsibilities and rights of the S.C.
These include:
 - i. to examine the annual account and annual report of the P.B.C.
 - ii. to inform the B.T. at least once a year on the results of its supervising activities
 - iii. to look after the fulfilment of the activities of the P.B.C. according to the law and the founding document and to inform the B.T. on cases of not compliance
 - iv. to propose to B.T. dismissal of the Executive Director
 - v. to examine the books and other documents of the P.B.C. and to check the data therein
 - vi. to convene an extraordinary session of the B.T. in case of concern
 - vii. to take part in sessions of the B.T. with a right to speak, whenever they ask for it.
- m. Responsibilities and rights of the Executive Director (E.D.)
 - i. E.D. may be only a person not indicted for a criminal act
 - ii. E.D. may not be a member of the B.T. and S.C.
 - iii. E.D. may take part in the sessions of the B.T. with advisory voice
 - iv. E.D. manages the P.B.C. with respect to all its activities, which are not in sole responsibility of the B.T. or other organ of the P.B.C. as determined by the founding document or Statute.
- n. Financial sources
Financial sources of P.B.C. come from
 - i. value of property provided by founder(s)
 - ii. value of accepted gifts and inheritance
 - iii. special funds
 - iv. donations

The P.B.C. may pursue for grants and donations of state or communities or any other territorial units, but such donations may not come from more than one source for the same activity or same project
- o. Economic activities
 - i. Besides the public benefit services, for which the P.B.C. was established, it may provide also other additional services under the conditions of
 - (1) better and more effective use of its property
 - (2) not jeopardizing the quality, scope and availability of its main services
 - ii. P.B.C. may not take part in business activities of other persons

- iii. P.B.C. may not set up its organizational parts outside the Czech Republic
- iv. The net annual profit of the P.B.C. must be transferred to a Reserve Fund, that is used to cover losses in next fiscal years, first of all

p. Accounting

- Double-entry accounting is required of P.B.C., which
- i. executes an additional economic activity
 - ii. has total annual incomes in past year greater than CZK 3,000,000

Under separate accounting must be kept the expenditures and incomes related to

- (1) additional economic activities
- (2) public benefit services
- (3) other activities and administrative ones

q. Auditing

Annual accounting report, balance sheet and profit and loss account must be submitted to a chartered auditor in case of a P.B.C., which

- i. is a recipient of a donation or other incomes from the state budget, budget of a municipality or any other territorial administrative unit of total amount exceeding in the year of report CZK 1,000,000
- ii. have not established a S.C.
- iii. have the net turnover exceeding CZK 10,000,000

r. Annual report

- i. Must be published not later than 6 month after the end of the evaluated period (in practice not later than in June of the next year, in case of a school and educational establishment this may be February, since the period may be identical with the school year from September to August)
- ii. The first annual report must be published not later than 18 month since registering
- iii. The annual report should contain
 - (1) overview of activities executed during the period in relation to the purpose of the P.B.C.
 - (2) annual accounting report with evaluation of the data in it
 - (3) statement of the auditor, if available
 - (4) expenditure and income overview
 - (5) balance sheet with respect to all financial sources
 - (6) development and closing account of all funds (reserve fund, premium fund etc.)
 - (7) closing status and changes in property and liabilities
 - (8) total amount of expenditures itemized according to requirements under 2.p

- (9) changes in the founding document and in membership of governing bodies during the period
- (10) other information as required by the B.T.

s. Sanctions

The P.B.C., which violates the requirements under 2.b, 2.c, 2.o and 2.r loses

- i. for the given year all tax benefits on income, heritage, gifts and property transfer
- ii. for the next fiscal year tax benefits on property tax

t. Natural or voluntary cessation

A natural or voluntary cessation of a P.B.C. is possible

- i. due to termination of time period for which it was established
- ii. because it achieved purposes for which it was established
- iii. at the date stated in the decision of the B.T. on cessation of the P.B.C.
- iv. due to merging or integration with another P.B.C.
- v. due to a split into two or more individual P.B.C.s
- vi. at the date given by the verdict of the court on termination of the P.B.C., otherwise at the date when such a verdict becomes legally effective
- vii. by announcement of bankruptcy tender or by refusal of a bankruptcy tender due to insufficient property

In the case of a B.T. decision on cessation, such a resolution must be announced at least 2 month prior to the date of cessation to the founder(s), who are entitled to change or cancel such a resolution; in such a case the founder(s) must take measures allowing the activities of the P.B.C. in the extend relevant to the reasons, why the resolution of the B.T. was changed or cancelled

u. Involuntary cessation

The court may decide on cessation of a P.B.C. on the motion of a state organ, founder or a person with proven legal concern, if

- i. no governing organs of the P.B.C. were appointed and the current organs have passed their terms for more then one year
- ii. there did not take place no session of the B.T. in the past year
- iii. the P.B.C. does not provide the public benefit services determined by the founding document for more then 6 months
- iv. due to the additional economic activities there

was for a period of 6 month repeatedly jeopardised the quality, scope and accessibility of the public benefit services, for which the P.B.C. was established

- v. the P.B.C. uses the incomes from its activities in violation to the Law
- vi. the P.B.C. violates requirements of the Law

The court may provide a remedy period of time

v. Liquidation

- i. In order to liquidate the P.B.C., the B.T. must nominate a liquidator officer
- ii. If a liquidator officer is not nominated by the B.T., the court does this without delay
- iii. The liquidator officer begins liquidation by
 - (1) checking, whether the founder(s) were notified about liquidation in due time
 - (2) invitation of all persons concerned to apply for their assets, claims and titles in a period of time of minimum 3 months
 - (3) announcement of the liquidation of the P.B.C. in the Official Business Bulletin
 - (4) noticing the relevant community and the financial office on the entering into liquidation
- iv. The liquidation should proceed in such a way, that only such proportion of the property is sold, that is needed to cover the liabilities of the P.B.S.
- v. In case, when neither the founding document nor the resolution of the B.T. determines, which P.B.C. is to take over the property after liquidation, such property must be offered to the community, where the P.B.C. has its seat; free of charge might be the property transferred to the community only under the contract bidding the community to use it fully for public benefit services, for which the P.B.C. was established
- vi. If the community does not in written accept the offered property, the liquidation officer assigns it to the assets of the State District Office relevant to the seat of the P.B.C.; the State District Office should use this property for public benefit services
- vii. The liquidator officer proposes in less then 30 days to the court to delete the P.B.C. from the register of P.B.C.s.

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