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Legal Risks in Property Acquisition

In recent years, the Czech Republic has experienced a stable growth of real estate prices, especially with regard to apartments and buildings for commercial use, such as offices or business premises. As a result, the real estate market is offering ideal conditions for vendors at present. On the contrary, a weaker position stems in this situation for buyers, especially as to their negotiation strength and possibilities for affecting the form of transactions. To put it simply, buyers cannot dictate too much as there are not so many suitable offers. Contrarily, there are usually more interested parties. The above-mentioned circumstances then exert pressure on real estate investors to diminish their prudence regarding an appropriate treatment of potential legal risks related to the real estate acquired, in addition to other transaction parameters. However, we can by no means recommend such a concession from prudence in respect of legal risks.

Due to the lack of suitable properties on offer, real estate with an unresolved legal status is more often put on the market. Such real estate often represents a favourable investment as the existing owner, being aware of the flaws in the offered asset, is willing to sell it at a low price, whereby the unsatisfactory legal status can usually be resolved. Yet in a way demanding a considerable amount of time and money. If one handles this successfully, a risky investment immediately turns into a very good one. However, at first it is necessary to duly scrutinise the property on offer from a legal perspective so that the buyer is aware of the facts that should result in a decrease in the purchase price if they decide to proceed with the transaction.

Apparently, a thorough legal due diligence is currently essential in respect of real estate transactions, whereby it can often not only clarify the risks involved, but also reduce the purchase price of the selected real estate.

History of the property to acquire

A serious risk involved in purchasing property is a possibility that, in fact, this real estate is owned by a person other than the vendor, or that another person has justified claims thereon. There are a number of possibilities of how such a situation can arise. The property has usually existed for a long time (land has existed since time immemorial) and thus a number of various legal statuses and dispositions form its history, some of which – even those relatively old – always have an effect in these days. Typically, real estate has a long chain of owners, from the past ones to the current one. Each of these owners acquired an ownership right to the property based on a certain legal title.

However, if a legal title, based on which the property is to be acquired, is invalid for any reason, a person that was to acquire the property based on this invalid title does not become the beneficial owner. Accordingly, they are not entitled to transfer the relevant property to other persons. The affected persons do not have to be aware of this fact, which can give rise to substantial problems.

Principle of material publicity

Act No. 89/2012 Coll., the Civil Code, as amended, regulating the acquisition of property ownership strives to minimise the above-mentioned risk by the legal regulation of the so-called principle of material publicity. The principle of material publicity relies on a publicly accessible register of real estate, which is a land and property register in the Czech Republic. The land and property register lists plots of land and buildings, including registration of their owner according to the record in this land and property register.

Putting it very simply, the principle of material publicity means that legal protection pertains to the person who acts with reliance on the status registered in the land and property register. The Civil Code thus determines in Section 984 (1) that if the state registered in a public register is not in accordance with the actual legal status, the registered state is in favour of the person who has acquired the ownership right for consideration in good faith from the person authorised thereto according to the registered state. Accordingly, if a person acquires real estate from a person registered in the land and property register as the owner of the real estate for a consideration and in good faith that the transferor is the owner, he/she should acquire an ownership right independently of the fact whether the-above mentioned uninterrupted chain of legal titles is attached to this real estate.

The Supreme Court of the Czech Republic replied in its decision-making practice to the question when an acquirer can be in good faith as regards the state registered in the land and property register, ie when the principle of material publicity applies to the situation. In its ruling file no. 22 Cdo 4174/2017 the court expressed an opinion according to which it is necessary to investigate in the intended transaction not only the state of records in the land and property register, but also factual circumstances of the case and the actual legal state of the property. Thus, it is not possible to rely solely on the recorded state in the land and property register. This opinion corresponds to the existing decision-making practice before the effectiveness of the Civil Code and has also been confirmed by the Constitutional Court. The Constitutional Court, in its ruling file no. IV. ÚS 4115/17, evaluated a mere reliance on the accuracy of data registered in the land and property register to the detriment of complainants and refused that it would be possible in the given situation to admit positive effects of the principle of material publicity. At this point, it is necessary to state that Czech courts have construed the principle of material publicity too narrowly so far in order for it to represent the so much needed institute for real estate investors, bringing about the missing certainty in relation to the history of the property acquired.

Here the necessity to implement a thorough legal scrutiny of the real estate to be acquired turns out again, as only then the acquirer can determine whether justified doubts exist

or not regarding the accuracy of the state recorded in relation to the relevant real estate in the land and property register and thus whether he/she is or not in good faith, given the circumstances of the case.

Acquisitive prescription

Another possibility for remedying potential historical flaws concerning acquisition titles in relation to real estate is a traditional institute of acquisitive prescription. Simply, this institute presumes that if a person treats an immovable property as if it were its owner for 10 consecutive years with no interruption and at the same time presumes in good faith to be its owner for the entire period, such person will acquire the ownership right to this real estate. A record of the person's ownership right to the property in the land and property register is, obviously, the assumption of good faith.

However, the acquisitive prescription will probably newly find its application especially in transfers of real estate without consideration as the above-described principle of material publicity will be more useful for transfers of real estate for consideration, which also presumes good faith but does not require the lapse of ten years for the acquisition of the ownership right.

Extraordinary acquisitive prescription

The institute of extraordinary acquisitive prescription is a novelty introduced by the Civil Code. Extraordinary acquisitive prescription is defined in the Civil Code as follows: where a person treats an immovable property as if it were its owner for 20 consecutive years with no interruption, such person will acquire the ownership right on condition that their bad faith has not been proved. The Civil Code postponed the application of the extraordinary acquisitive prescription by five years. Accordingly, it has only been possible to apply new institute since 1 January 2019 (providing that 20 years have passed in the meantime).

Only time will tell to which extent this institute will be utilised. Nevertheless, a reasonable application by courts has, in theory, a potential to settle all historical flaws relating to acquisition titles in situations when the acquisition of real estate is not questioned but, due to formal deficiencies, the acquisition title may be considered invalid and, as a consequence, the acquirer cannot be in good faith.

This article did not aim to provide an exhaustive list of legal risks pertaining to the acquisition of real estate. This would not be possible after all. Instead, by providing several examples (as repetition is the mother of wisdom), we wanted to emphasise the crucial fact: a **thorough due diligence is essential for making safe real estate investments!** At any time.

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Legal News in e-Commerce, Blockchain and FinTech

The latest news in the area of e-commerce includes the adoption of an EU regulation for multilateral platforms, a bill that may enable the utilisation of banking identities in online legal acts, new obligations concerning Strong Customer Authentication and progress achieved in the implementation of new consumer directives. As a matter of interest, we are also presenting a study focusing on appropriate forms of communicating legal information.

Proposed EU regulation for multilateral platforms

Regulation (EU) 2019/1150 of the European Parliament and the Council on promoting fairness and transparency for business users of online intermediation services was published on 20 June 2019. The new rules aim to safeguard a fair, transparent and predictable business environment for small businesses and traders using online platforms. The regulation applies to providers and intermediaries of online services used, for example, by hotels, traders selling online, app developers and all other companies that rely on search engines. While the rules define new duties for online services providers, traders using these services are placed in the position of a "pseudo-weaker" party, obtaining a wide range of rights and advantages.

The new rules primarily aim to **increase the transparency of online intermediation** services by formulating specific elements of business terms and conditions, such as defining a duty to publish rules and mechanisms under which providers order and publish offers of individual traders, generate and save user data or whether selected traders may be advantaged within an offer (premium accounts with highlighted offers, service providers preferring own offers etc).

The regulation also places a greater emphasis on **resolving disputes more effectively** as well as on the transparent

decision-making of online service providers. Among other things, the regulation aims to ensure that online service providers will be required to render an appropriate explanation of any service suspension or termination and, simultaneously, establish an internal system for handling complaints and disclose in their business terms and conditions qualified and independent mediators with whom it will be possible to resolve potential conflicts arising from the provider's services.

Although the regulation does not specify any particular sanctions, the EU member states will be obliged to seek a due and effective enforcement of the regulation. It is thus necessary to wait how the Czech legislators will tackle this challenge and which sanctions and coercive measures towards providers will be available for traders. The **regulation will come into force on 12 July 2020.**

Proposal for establishing a banking identity

On 12 July 2019, a group of Deputies presented an amendment to the Bank Act and the AML Act (Act on Selected Anti-Money Laundering Measures), introducing the so-called banking identity in Czech law. The goals of the banking identity is to provide simple but reliable forms of identification to the widest circle of addressees that may be used to access e-Government services as well as private sector platforms.

Banks will be able to access data from basic registers and selected agency information systems in order to fulfil their statutory duties, especially in the area of measures against money laundering and terrorism financing.

The amendment has currently received a concurring opinion from the government and will be referred to the first reading in the Chamber of Deputies.

New Strong Customer Authentication duties

Given that the effectiveness of the PDS2 directive will soon be terminated, Strong Customer Authentication (SCA) has been introduced, principally defining a duty for payment services providers (PSP) to perform two-factor authentication. This consists of verifying two of three mutually independent elements of users – knowledge (eg a password), possession (eg user's mobile phone) and the user's biometric data (usually a fingerprint). This duty must always apply when the account owner accesses their bank account, pays by payment card and makes a payment via online banking. Theoretically, the changes will not affect modern payment methods including, for example, Google Pay or Apple Pay services, which had already performed two-factor authentication before the statutory measure took effect.

The measure had to be launched by payment service providers by 14 September 2019.

Transposition of new directives affecting consumer contracts

An inter-ministry consultation is currently taking place with respect to a bill aimed at transposing two new EU directives regulating the sale of goods and provision of digital content and digital services in Czech law, as we informed you in the monitoring published in March and May. The above-specified directives will primarily affect **contractual relations.**

The directive regulating the sales of goods concentrates on contracts based on which the ownership right to a tangible movable asset is transferred in return for payment. The directive has newly introduced an extended period over which it is presumed that the goods were already faulty when taken over by the customer. This period, which is currently six months, will newly be extended to one year. The directive also newly defines the customer's right to withdraw from a contract without any undue delay if the nature of the product defect is so significant that it substantiates the immediate termination of a contractual relationship.

The bill has further introduced a definition of digital content in line with the respective EU directive. Digital content refers to **data produced and supplied in digital form**. This definition will comprise, for example, video files, audio files, music files, computer software, applications, digital games, e-books and other electronic publications. Furthermore, the bill also contains detailed legal regulation concerning the specifics of purchasing digital content, such as a new responsibility of the seller to supply updates of digital content in the necessary scope ensuring that the digital content has the same qualities as it had upon takeover and for a period that may reasonably expected by the purchaser. We will keep you informed on the particular wording of this bill.

Interesting study concerning appropriate forms of communicating mandatory legal information – BIT best practice guide

Behavioural Insights Team (BIT), a UK-based beneficiary association dealing with a possible application of behavioural psychology in various humanistic, including economic and legal, disciplines, which is jointly owned by the UK Cabinet Office, has recently issued a public study examining the methods of an effective disclosure of information to customers with a focus on business terms and privacy policies. What differentiates this study from other research of consumer rights is that it exclusively examines the form rather than the content of legal documents.

The study has a two-dimensional character. First of all, it explores the question of how the form of communication may help increase the level of understanding business terms on part of consumers and, subsequently, how consumers' pro-active approach to business terms may be achieved (i.e. increase the level of probability that consumers will read the business terms).

BIT recommendation

In the above-specified context, BIT tested 18 different methods concluding that six of them may be considered effective for the above purposes.

Based on BIT's findings, the comprehensibility of business terms may be increased primarily by **implementing the FAQ section with an explanation of key terms**, as well as by **making business terms more visual** (i.e. including icons, graphics and comics) and **displaying them in a scroll-down** window rather than via a hypertext link redirecting users outside the website being displayed. To increase the consumers' willingness to read business terms, BIT recommends informing consumers in advance about the **estimated time necessary for reading the business terms** and specifying that it is the **last possibility for consumers to read the content of the business terms prior to entering into the contract as such**.

The results of the study may be beneficial primarily with regard to increasingly more-demanding statutory requirements for transparent and comprehensible disclosures of mandatory legal information in various industries.

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