ALLEN & OVERY

Covid–19 update

Czech Republic crisis measures and the possibility to claim compensation for damage

In connection with the COVID-19 disease caused by the SARS-CoV-2 coronavirus, a number of crisis measures have been adopted in the Czech Republic restricting the activities of businesses. As a result of these restrictions, the affected entities may suffer damage.

The current situation is unprecedented and fluent. It has brought a number of questions we did not have to deal with in the past.

The Crisis Act expressly deals with compensation for damage which is caused by crisis measures. Most of the measures, except for the initial ones, were declared by the state under other laws. Some of the measures were subsequently quashed by a court. The question is whether the affected businesses may now seek compensation for damage under the Crisis Act or otherwise, and what the results will be.

What does the decision of the Municipal Court in Prague mean?

The Municipal Court in Prague has quashed certain measures declared under the Public Health Protection Act on the grounds that the Ministry of Health had not been authorised to declare them. Once the state of emergency had been declared, the crisis measures should have been announced by the government under the Crisis Act. The court also clearly stated that it did not contest the efficiency of the quashed measures, and provided time for the government to adopt measures with the same content as under the Crisis Act. The decision is effective but may be overturned by the Supreme Administrative Court.

Can I claim compensation for damage?

The possibility to claim compensation stems directly from the Crisis Act in relation to crisis measures declared under the Crisis Act. The fact that certain measures have been quashed as illegal also opens the possibility of compensation for damage pursuant to the Act on Liability for Damage Caused in the Exercise of Public Authority by a Decision or Maladministration.

The relationship between the two possibilities will need to be clarified. It should also be borne in mind that the Supreme Administrative Court may make the final decision on the legality of the quashed measures.

For example, it could be argued that, for the purposes of compensation for damage, all the relevant measures, including the quashed ones, should be considered to be crisis measures pursuant to the Crisis Act. In particular, it will likely be crucial that these were organisational or technical measures aimed at solving a crisis

situation and alleviating its consequences, including measures affecting the rights and obligations of persons (i.e. that the material element of a crisis measure has been met).

Under the Crisis Act, the Czech Republic must provide compensation for damage which occurred to the injured party as a result of the crisis measures. For the liability to arise, all the following prerequisites must be met at the same time:

- existence of crisis measure;
- occurrence of damage;
- causal link between the crisis measure and the occurrence of damage (i.e. the damage must occur as a result of the crisis measure); and
- the injured party must not cause the damage to itself.

This is a strict liability of the state for damage. Therefore, for the liability to arise, the crisis measure need not be incorrect or illegal. To the contrary, the relevant provision of the Crisis Act is based on the premise that compensation should be due for a forced restriction made in the interests of others, even if the restriction is entirely legal.

Even if the Crisis Act did not apply to the measures that have been quashed by the court, it should be possible to seek compensation for damage pursuant to the Act on Liability for Damage Caused in the Exercise of Public Authority by a Decision or Maladministration. However, in this case the procedural steps would be complicated due to the combination of several regimes.

In exceptional cases, it should also be possible to seek compensation for damage directly based on the Charter of Fundamental Rights and Freedoms. Claims under international treaties on protection of investments have started to be mentioned tentatively, but this matter is not the subject of our summary.

How much compensation for damage can I seek?

It is possible to seek compensation not only for actual damage, but also for lost profit, irrespective of the statements of certain members of the executive.

Actual damage may mean a decrease of the injured party's assets, for example due to the perishing of goods that, due to a forced closure of the establishment, could not be sold or otherwise used. The calculation of the actual damage should be fairly straightforward as the claim will be based on tangible losses.

However, the actual damage may be also less tangible. For example, it may consist of increased costs of financing of unsold stock, although the causal link will play an important role here.

In addition to compensation for actual damage, there is compensation for lost profit. Lost profit may be described as an increase in the assets of the injured party that did not occur, although it would have been expected to have occurred in a "business as usual" scenario. However, the calculation of lost profit will be much more difficult than the calculation of actual damage.

On the other hand, the injured party will not have the right to compensation for damage caused by the injured party itself, whether by acting or failing to act. To the extent the damage could have been prevented, the party has no right to compensation. An example is a restaurateur that could have sold take-away meals, but did not do so. In this connection, an important role is played also by diligent use of all available forms of state support.

How to calculate lost profit?

To calculate lost profit, it is not enough to compare the profit before and after introduction of a crisis measure. Therefore, it cannot be argued that before the introduction of the crisis measure the party had revenues in a certain amount, and after the introduction it has lower revenues and the costs have remained the same, so it is seeking compensation for lost profit in the amount calculated in this way. For a correct calculation, it will be necessary to compare the actual state with the state that would have existed had the crisis measures not been declared.

The determination of this theoretical state that could have occurred had the crisis measures not been introduced will not be easy. In practice, it will be necessary to estimate how the epidemic would have developed without the introduction of the crisis measures and what impact this would have had on revenues. For example, in the case of the restaurateur, it would have to be estimated how many meals he would have sold had his restaurant not been closed. This calculation would have to reflect, among others, people's fears of getting infected, and the related decrease in the number of customers visiting the restaurant.

The burden of proof in respect of the occurrence and amount of the damage will rest with the affected businessman. Therefore, it is clear that, in many cases, submitting the claim for compensation will not be possible without a high-quality expert opinion regarding the above matters. In all cases, it is important to continually collect and preserve all evidence relating to the calculation of the damage. The burden of proof will rest with the affected businessman also in respect of the causal link between the damage and the crisis measures. Typically, Czech courts are fairly strict when assessing causal links.

When and where should I seek the compensation for damage?

The procedure and periods for exercise of the claim depend on the Act under which the claim is submitted.

Under the Crisis Act, the affected person must submit the claim for compensation of damage within six months after the person has learned about the damage, but in any event no later than five years after the damage has occurred. If the affected person fails to exercise the claim within this period, the claim will case to exist and it will not be possible to successfully seek the compensation.

The claim for compensation for damage must be filed with the relevant crisis-management body (e.g. the government or the relevant ministry). The determination of the body will depend on the facts of the particular case.

If the crisis-management body fails to recognize the claim, or recognizes it in an insufficient amount, the compensation for damage must be sought in court.

Is seeking the compensation for damage worth it?

We need to stress that many questions still lack clear answers.

The good news is that in Czech law there is a legal basis for exercising a claim for the compensation for damage that arose as a result of crisis measures, and that there are good reasons why this legislation should apply to all the measures that have been adopted in connection with COVID-19. This reasoning is, to a certain extent, helped also by how the courts have reacted to the undignified zigzagging by the government in extending its crisis measures.

On the other hand, it is clear that compensating all the damage would be extraordinarily expensive for the Czech Republic. It can therefore be expected that, in assessing claims for the compensation of damage, courts would act pragmatically and would take into consideration the impact on state finances.

Therefore, although it is not possible at the moment to give a general answer or to guarantee the result of a particular dispute, each business acting responsibly should carefully consider the possibility of submitting a claim for the compensation for damage that occurred in connection with the crisis measures.

A court dispute may be merely the solution of last resort. Given what we have discussed above, the state may also be interested in avoiding well-prepared and well-reasoned claims by coming to an out-of-court solution.

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