CZECH REPUBLIC


<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Political Rights</td>
<td>6</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Civil Liberties</td>
<td>6</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Status</td>
<td>NF</td>
<td>F</td>
<td>F</td>
<td>F</td>
<td>F</td>
<td>F</td>
<td>F</td>
<td>F</td>
</tr>
</tbody>
</table>

Polity: Consolidated Democracy  
Economy: Consolidated Market  
Population: 10,357,000  
PPP: $9,775  
Ethnic Groups: Czechs (94 percent), Slovak (3 percent), Roma (2 percent)  
Capital: Prague

* FH ratings through 1992-1993 are for the Czechoslovak Federal State

1. When did national legislative elections occur? Were they free and fair? How were they judged by domestic and international election monitoring organizations? Who composes the government?  
The June 1996 parliamentary elections for the Czech Republic’s Chamber of Deputies heralded the end of the transitional phase in the country’s political scene, with the emergence of two strong parties on the left and right in the Western European mold. In a result nearly identical to that in 1992, the center-right Civic Democratic Party (ODS) won nearly 30 percent of the vote (68 seats). For the opposition, the center-left Czech Social Democrats (CSSD), led by Milos Zeman, was victorious. The party’s 26-percent share (61 seats) quadrupled its returns from 1992. Unlike the typical Central and Eastern Europe social democratic party, which is a “reformed” Communist party, the CSSD comes from a long pre-Communist tradition of center-left politics. The other parties winning seats in the Chamber were the unreconstructed Communist Party of Bohemia and Moravia (KSCM), with 10.3 percent (22 seats); the Christian Democratic Union (KDU), with eight percent (18 seats); the extremist nationalist Republican Party, with 8 percent (18 seats); and the free-market Civic Democratic Alliance (ODA), with 6.3 percent (13 seats).

Of 200 parliamentary seats, the parties of the governing coalition managed only to win 99, a loss of six from their pre-election standings. As a result of its failure to win an outright majority, the ODS-led coalition was not assured of forming a government. The CSSD extracted concessions from the ODS-led coalition in return for its acquiescence in the formation of a minority government, which was named in July 1996, with Vaclav Klaus as Prime Minister.

In November 1997, allegations that the ODS had improperly accepted more than $200,000 in financial donations led the ODA and CDU to withdraw from the governing coalition and forced Klaus and his government to resign. Josef Tosovsky, who is not affiliated with any party, was named interim prime minister in January 1998, in a government that still included the three parties in the
original coalition. While elections had been scheduled for 2000, the political deadlock in parliament and the interim government led to a change in the electoral law to allow for new elections in June 1998.

The 1992 constitution established a Senate along with the dominant Chamber. A lack of clarity in the constitutional text and political wrangling over electoral procedures, however, postponed Senate elections for four years. Two rounds of Senate elections were held in November 1996. Approximately 570 candidates registered to compete for Senate seats in 81 electoral districts. However, 100 of these registrations were rejected by the Central Electoral Commission due to technical errors, some of which were subsequently overturned by the constitutional court. Only three parties — ODS, KSCM, and CSSD — nominated a candidate in every district. ODS won the election, but with only a 39.6-percent share of the vote, which gave it 32 seats. The Social Democrats followed with 25 seats and 30.9 percent of the vote. The Christian Democrats won 13 seats; the ODA, seven; and the Communists, two. The second-round vote was viewed as a referendum on the ODS’s performance. A total of 76 ODS candidates stood in the second round, but only 40 percent of them won. This poor showing was the result of a joint decision by all of the other parties, including ODS’ coalition allies, to back whoever opposed the ODS candidate in a particular district. Over the objections of the ODS and with the support of the Social Democrats, the KDU successfully nominated its candidate, Petr Pithart, the Czechoslovak premier from 1990 to 1992, as Senate chairman.

In June 1990, the first post-1989 national legislative elections in Czechoslovakia were won by dissident Vaclav Havel’s Civic Forum movement, which led peaceful demonstrations that brought down the hard-line Communist government. In the June 1992, national elections, two opposing parties each gained clear majorities in the different republics. Vaclav Klaus’ center-right and pro-radical reform ODS, emerged victorious in the Czech lands. In the Slovak Republic, the Movement for a Democratic Slovakia (HZDS), which was headed by Vladimir Meciar, was the clear winner. Irreconcilable differences between the parties and their leadership led to the breakup of the Czechoslovak federation. With the countries’ divorce on January 1, 1993, Klaus and Meciar became the leaders of their respective republics.

Foreign observers have determined that the 1990, 1992, and 1996 elections were free and fair.

2. **When did presidential elections occur? Were they free and fair?** Vaclav Havel was re-elected president of the Czech Republic by the parliament in January 1998. Under the constitution, presidents serve five-year terms. Since the dissolution of Civic Forum, Havel has had no political party affiliation.

Havel had been elected president of the Czechoslovak Federation in December 1989, by the Federal Assembly. He was then elected president of the Czech Republic by the Chamber of Deputies in January 1993.

3. **Is the electoral system multiparty-based? Are there at least two viable political parties functioning at all levels of government?** The electoral system is multiparty-based. Article 5 of the constitution states that the “political system is based on free and voluntary formation of and free competition between political parties.”

In late 1989 and early 1990, parties began to form for the June 1990 legislative elections in
Czechoslovakia. At least two political parties function at different levels of government. Candidates often run independently in local elections, in which personal popularity can be more important than party membership. Independent candidates won approximately 40 percent of the vote in the November 1994 local elections. One newly elected senator is an independent, and another is a member of the extra-parliamentary Democratic Union Party.

4. How many parties have been legalized? Are any political parties illegal? More than 50 parties have emerged since the revolution of 1989. Fewer than 25 parties registered for the local elections in November 1994, and fewer than ten of these are of national importance. Twenty parties registered for the June 1996 parliamentary elections, but only six managed to clear the 5 percent threshold necessary for representation.

During their campaigns for the July 1996 elections, small parties complained of discrimination by the Central Electoral Commission, which is composed of individual party representatives who make decisions by majority vote. The commission ruled that the Free Democrats-Liberal National Social Party (FD-LNSP) was a coalition and not a single party, thereby raising its required share for Chamber representation from five to seven percent. The party complained that the Social Democrats and the other leftist parties were attempting to disqualify them through legalistic means. The Constitutional Court then ruled in favor of the FD-LNSP. Nevertheless, the FD-LNSP was unable to break even the 5-percent barrier.

In March 1996, internal affairs minister Jan Rumil announced that he would attempt to outlaw the new Party of Czechoslovak Communists, led by Miroslav Stepan, who is the only Communist imprisoned after 1989. Arguing that Stepan sought a “renewal of socialism,” Rumil wanted to use the authority of the Crimes of Communism Act. Vaclav Klaus, however, later vetoed the move.

5. What proportion of the population belongs to political parties? The number of party members registered is between 8 and 12 percent of the adult population. In light of the relatively high level of voter turnout, however, this is not a very accurate measure of support.

6. What has been the trend of voter turnout at the municipal, provincial and national levels in recent years? Voter turnout in the Czech Republic has fallen since transition. In the first post-transition election in 1990, more than 90 percent of citizens voted. In the 1992 federal (Czechoslovak) elections, 85 percent of the population voted, although turnout was higher in the Czech republic than in the Slovak republic. Turnout in the November 1990 Czechoslovak local elections was 73 percent in the Czech lands and 63 percent in Slovakia, with an approximate national average of 70 percent. Excluding Prague, turnout in the November 1994 local elections averaged 54 percent in large cities and approximately 64 percent in towns and villages.

Voter turnout in 1996 was at two disparate levels. The Chamber election turnout was relatively high at 76 percent, while turnout for the Senate election was extraordinarily low with 35 percent in the first round, and 30 percent in the second round. The fact that the Senate is an unpopular institution — it is even less popular than the Chamber — together with the electoral fatigue resulting from two nationwide polls in quick succession — help to account for this result.
1. How many non-governmental organizations have come into existence since 1986? How many charitable/nonprofit organizations? Are there locally led efforts to increase philanthropy and volunteerism? What proportion of the population is active in private voluntary activity (from polling data)? As of early 1998, there were more than 30,000 NGOs operating in the Czech Republic. In 1988, there were approximately 2,000. As of mid-1995, there were approximately 2,500 foundations in the Czech Republic. Some international charitable organizations, such as the Salvation Army, have extensive operations in the Czech Republic.

2. What is the legal and regulatory environment for NGOs (i.e., ease of registration, legal rights, government regulation, taxation, procurement and access-to-information issues)? To what extent is NGO activism focused on improving the legal and regulatory environment? The growth of the NGO sector has been obstructed by economic constraints and delays in the passage of legislation on nonprofit organizations. In addition, a tax law passed in 1994 over the objections of President Havel ended the favorable treatment enjoyed by nonprofit organizations. In a compromise measure, the legislature empowered the Finance Ministry to enact appropriate regulations for nonprofit organizations. Draft laws have been long-delayed.

The right of public access to information is not enshrined in legislation, a deficiency that has drawn criticism from the European Union (EU).

3. What is the organizational capacity of NGOs? Do management structures clearly delineate authority and responsibility? Is information available on NGO management issues in the native language? Is there a core of experienced practitioners/trainers to serve as consultants or mentors to less developed organizations? The Prague Post Foundation hosts a monthly forum on Czech NGO management issues. The forum is known as the “International Roundtable for Not-For-Profit Organizations.” Meetings are conducted in both English and Czech.

4. Are NGOs financially viable? What is their tax status? Are they obliged to and do they typically disclose revenue sources? Do government procurement opportunities exist for private, not-for-profit providers of services? Foreign sources of funding have supplied approximately half of the revenue used by Czech nonprofit organizations. NGOs have come to rely more and more on corporate and individual contributions as governmental, U.S., and EU (PHARE) assistance is slowly being phased out.

U.S. Agency for International Development is a major sponsor of Czech NGOs. The Democracy Network, a U.S. AID program designed to strengthen the nonprofit sector, has provided $1.5 million in assistance to NGOs.

5. Are there free trade unions? How many workers belong to these unions? Is the number of workers belonging to trade unions growing or decreasing? What is the numerical/proportional membership of farmers’ groups, small business associations, etc.? The Communist Revolutionary Trade Union was abolished in March 1990. Most unionized workers belong to the Czech-Moravian Chamber of Trade Unions (CMKOS), which was established in April 1990 and currently
includes 35 individual unions. Some unions are not a part of CMKOS, but these remain marginal.

Approximately two-thirds of all workers are members of a union. Despite this apparent strength, CMKOS generally remains politically independent. This is the result of many factors, the foremost being the severe mistrust that unions earned in the pre-1989 period as puppets of the Communist Party.

There are at least three farmers’ groups. They are not very large, as farmers constitute only 5 percent of the workforce. Two small business associations merged in 1994 to consolidate their interests. Their membership and influence continue to grow.

6. What forms of interest group participation in politics are legal? The participation of interest groups in the political policy process is not yet legally regulated. Although some such activity exists, interest groups currently have relatively little power in the political process. Public petitions and demonstrations are legal and unrestricted.

7. How is the not-for-profit/NGO sector perceived by the public and government officials? What is the nature of media coverage of NGOs? To what extent do government officials engage with NGOs? While Havel has been supportive of NGOs, the limited powers of the presidency have also limited the impact of his support. The former Klaus government did not view NGOs as important political players. There is some indication, including a February 1998 resolution that recognized NGOs as important partners in social affairs, that the Tosovsky-led interim government views them more favorably.

In early 1998, an NGO publicity campaign entitled “30 Days” featured more than 290 events across the country and nearly 2,500 stories in the print and electronic media. TV-Nova was a major sponsor of the event.

The English-language *Prague Post* publishes a weekly column on a wide variety of issues that affect Czech NGOs. The column is translated and published in *Reflex*, a weekly newsmagazine.

**Independent Media 1.50/7**

1. Are there legal protections for press freedom? The Charter of Basic Rights and Freedoms protects the right to a free press. Current legislation protects both print and broadcast media, but is out of date. Much-debated revisions of the law had still not been adopted by the end of 1997. Czech journalists have criticized the draft laws for not requiring that state bodies give information to the press and for failing to protect journalists’ rights to maintain the confidentiality of their sources.

2. Are there legal penalties for libeling officials? Are there legal penalties for “irresponsible” journalism? Have these laws been enforced to harass journalists? In April 1994, the Constitutional Court abolished a law that allowed for the prosecution of those accused of defaming government officials. A provision against defamation of the President and the Republic was retained, however, as was a provision allowing prosecution for the slander of government officials or departments.

In September 1997, Havel signed a law to repeal the provision against defamation of the president and the Republic. Until then, violators could be punished with prison terms of up to two years. The few people who were actually convicted under this law, however, only received suspended
sentences. Even in these cases, Havel routinely pardoned the offenders.

There are no penalties for irresponsible journalism.

3. What proportion of media is privatized? What are the major private newspapers, television stations, and radio stations? The Czech Republic has scores of private newspapers and magazines. Of the Czech Republic’s four television stations, two are private – TV-Nova, which enjoys a 71 percent market share, and TV Prima, which emerged from the struggling Premiera TV. There are 60 private radio stations, in addition to Czech Public Radio. Some major cities can connect to cable stations. Local stations are permitted but are not common, generally due to financial concerns). One private news agency, CTA, began operations in October 1994 and will compete with the state CTK agency.

4. Are the private media financially viable? From 1992 to 1995, print media costs increased 300 percent. This, together with the overcrowded nature of the market, has caused major turbulence, with the rapid disappearance of old publications and the quick appearance of new, merged, or re-formed publications. Many of these are more financially secure, primarily as a result of foreign investment. By March 1996, over half of the Czech press was foreign-owned. The largest holders are the Germans, followed by the Swiss and French. Media without foreign investment, government support or party support often have only limited solvency. Advertising rates and revenue have increased rapidly and are expected to reach 10.6 billion koruna ($393 million) in 1996.

5. Are the media editorially independent? Are the media’s news-gathering functions affected by interference from government or private owners? The media are not always editorially independent. The case of Vladimir Stehlik, owner of the giant and bankrupt Poldi Steel Company, illustrates some of the problems with editorial independence in the Czech Republic. Both the government and TV-Nova have been very critical of Stehlik and his business practices, which are under investigation. Stehlik managed to purchase Prace, a trade-union daily, which now regularly attacks both the government and TV-Nova. Such editorial allegations are not uncommon: Denni Telegraf, for example, is widely viewed as a mouthpiece of the ODS.

A parliamentary commission has oversight powers for the Television and Radio Council. The Council regulates the telecommunications media by issuing and revoking licenses and monitoring programming. There is an independent journalists’ association.

6. Is the distribution system for newspapers privately or governmentally controlled? There are three main printing companies in the Czech Republic. Typografia, a large printing company in Prague, is responsible for the printing of many national dailies. It is scheduled to be privatized.

7. What proportion of the population is connected to the Internet? Are there any restrictions on Internet access to private citizens? Paul Houcer, an editor of Computerworld magazine, estimates that there are as many as 250,000 regular Internet users in the Czech Republic. Approximately 15 percent are connected at home. Thirty percent are connected at school, while 55 percent are connected work.
8. What has been the trend in press freedom as measured by Freedom House’s *Survey of Press Freedom*? Freedom House’s annual *Survey of Press Freedom* rated Czechoslovakia “Partly Free” for 1989, and “Free” from 1990 through 1992. The Survey rated the Czech Republic “Free” from 1993 through the present. *The Economist* calculates that the Czech Republic has the world’s fourth most free press, which ranks it ahead of both Germany (seventh) and Britain (ninth). Current press laws, however, do not provide for the right of media to have access to state information, and the legal protection of sources’ confidentiality is not clearly provided.

**Governance and Public Administration 2.00/7**

1. **Is the legislature the effective rule-making institution?** The Czech parliament is an effective rule-making institution. In 1995, the Chamber of Deputies adopted approximately 300 statutes. Vaclav Klaus and the ODS effectively ran the legislature to advance their reform programs from 1992 to 1996. As a result of two inconclusive parliamentary elections in 1996, however, a tense political stalemate has slowed legislative action on a host of pressing issues.

2. **Is substantial power decentralized to sub-national levels of government? What specific authority do sub-national levels have?** In November 1990, under the Czechoslovak administration, several regional reforms took place. The ten-region system (seven Czech and three Slovak regions) of government under communism was eliminated, districts were placed under the administration of each republic, and municipal governments were converted into self-governing bodies. Thus, the Czech republic is subdivided, first, into 76 non-autonomous districts and, second, into thousands of autonomous local municipalities.

   Article 8 of the constitution specifies that “self-government of territorial self-governing units is guaranteed,” while Article 101 states that the state “may intervene in the activities of self-governing territorial divisions only if such intervention is required by protection of the law and only in a manner defined by law.” Chapter 7 of the constitution deals specifically with local rule. It establishes the division of the Czech Republic into communities that “shall be the basic self-governing territorial divisions” and that shall be “administered by a community assembly.” These include city councils that govern towns, villages and small cities, as well as district councils that govern sections of larger cities.

   The constitution further states, however, that the “superior self-governing territorial divisions shall be lands or regions” that shall be “administered by an assembly of representatives.” Thus, although the constitution establishes the order of authority, it does not specify in more detail the composition and features of this middle tier of government.

   The continued process of regional reform has been a subject of intense debate in both successor republics to the Czechoslovak state. In the Czech Republic, the establishment of self-administrative regions has been complicated by fears of increased nationalist sentiment in the historical lands of Moravia and Silesia, as well as conflicts among parties. On the other hand, there is widespread feeling that failure to establish such regions could delay the country’s entrance into the European Union.

   An ODA-authored constitutional amendment on the establishment of a medium tier of elected government between the central government and the community councils was considered in March
and April 1996. It was to establish nine regional bodies. The constitution actually calls for such bodies, but does not specify how they are to be composed or when they should be created. The bill was opposed principally by the ODS, which questioned whether creating these regional bodies was wise in a country as small as the Czech Republic. A January 1996 poll indicated that only 25 percent of Czechs considered the lack of such institutions to be a pressing problem. Nevertheless, 43 percent believed the creation of such bodies would improve state administration. Twenty-nine percent thought that these bodies would represent an improvement.

The coalition agreement signed after the June 1996, elections committed the government to establish these regions before the end of its term in 2000. ODA chairman and then-justice minister Jan Kalvoda proposed the establishment of 13 regions with considerable authority, including management of roads, schools, cultural institutions, health facilities, and forests.

3. Are sub-national officials chosen in free and fair elections? Article 102 of the constitution mandates that “Assembly members shall be elected by secret ballot on the basis of universal, equal and direct suffrage.” According to the 1990 reforms, municipal or communal governments consist of assemblies chosen in local elections. These bodies then elect mayors and their deputies. District officials are appointed by the state, as districts are branches of the state. The first post-Communist local elections in 5,766 municipalities were held under these new rules in November 1990. Civic Forum won with 35.6 percent of the vote. This victory, which took place during a national debate over economic reform, gave a mandate to the government to continue on the path of radical reform.

The ODS won the largest percentage of support in the November 1994 local elections with 28 percent in the district councils and nearly 11 percent in the city councils. It was also victorious in Prague, with 41.2 percent of the vote. Josef Lux’s KDU, however, received the greatest actual number of seats because its strength was in the more rural city councils where fewer voters were apportioned per seat. Despite expectations that they would do well, the Communists fared poorly. Independent candidates won slightly less than half of the city council seats and 13 percent of the district council seats.

The 1990 and 1994 local elections were generally deemed free and fair. The next local elections are scheduled for November 1998.

4. Do legislative bodies actually function? Is draft legislation easily accessible to the media and the public? In theory, the presence of the Senate should aid in stabilizing the political process in the Czech Republic. Article 33 of the constitution stipulates that, if the Chamber is dissolved, the Senate assumes legislative control until new elections are held. Due to the absence of a Senate, however, there was no practical constitutional way to dissolve the Chamber before November 1996. In the future, the low popularity of the Senate as an institution and the low turnout for its elections could undermine its legitimacy.

Local assemblies have the power to pass ordinances, call local referenda, and approve budgets. They have executive and legislative powers. Districts function as branches of the state and appear to operate smoothly.
5. Do the executive and legislative bodies operate openly and with transparency? Article 36 of the constitution guarantees that “meetings of both chambers [of parliament] shall be public” and that the “public may be excluded only under conditions defined by law.” Legislative sessions are generally open to the public in practice and new laws are published. The transparency of local actions depends largely upon the quality of local media, which vary among regions.

6. Do municipal governments have sufficient revenues to carry out their duties? Do municipal governments have control of their own local budgets? Do they raise revenues autonomously or from the central state budget? Article 101 of the constitution stipulates that the self-governing regions have their own budgets and may have their own property. Former ODA Chairman Jan Kalvoda’s proposed regions would have control of their own budgets. They would draw revenue from local taxes, property income, administrative fees, and state subsidies. Municipal governments have the power to approve budgets. It is estimated that municipalities received 43.5 percent of revenues from the state budget in 1995, versus 40.6 percent in 1994. With the exception of Prague, selling and renting real estate is an important source of revenue.

Municipalities are generally financially strapped, and mayors of small communities often do not receive financial compensation. Municipal governments in poor, industrialized areas such as northern Bohemia have reported difficulty in raising funds to attend to their communities’ needs.

7. Do the elected local leaders and local civil servants know how to manage municipal governments effectively? There is substantial inefficiency at the local level due to the presence of incompetent, politically connected officials appointed by the Communists, as well as uncertainty about the procedural changes accompanying multiple reforms. These problems should diminish with time. Between 1989 and 1990, municipalities splintered and thereby increased in total number by 50 percent without regulatory consent. This situation has increased inefficiency. According to observers, petty corruption, such as small bribes to expedite matters, is common. For example, there have been allegations that civil servants request bribes in order to expedite the installation of telephone lines.

8. When did the constitutional/legislative changes on local power come into effect? Has there been a reform of the civil service code/system? Are local civil servants employees of the local or central government? A reformed civil service law has yet to be adopted in the Czech Republic. This has led to confusion about civil servants’ status and responsibilities. Debate on drafts of such laws has been extensive.

Local reforms were enacted in November 1990. Further reforms were tabled until the division of the Czechoslovak state; specific legislation has not yet been passed. Reforms of the civil code have not yet been passed. Local civil servants are paid out of municipal budgets. District officials are appointed by the state.

**Rule of Law 1.50/7**

1. Is there a post-Communist constitution? How does the judicial system interpret and enforce the constitution? Are there specific examples of judicial enforcement of the constitution?
in the last year? In December 1992, the Czech constitution was adopted by the Czech National Council. It took effect in January 1993 with the dissolution of the federal state.

2. Does the constitutional framework provide for human rights? Do the human rights include business and property rights? The Czechoslovak Federal Assembly adopted the Charter of Fundamental Rights and Freedoms in January 1991 to protect human rights. Although this charter is not in the constitution per se, according to Article 3 of the new Czech constitution, it is an “integral component of the constitutional system.” Furthermore, Article 10 commits the Czech Republic to abide by ratified international treaties on human rights. Under Article 11 of the Charter, everyone has the right to own property.

3. Has there been basic reform of the criminal code/criminal law? Who authorizes searches and issues warrants? Are suspects and prisoners beaten or abused? Are there excessive delays in the criminal justice system? While the criminal code has undergone many revisions and amendments since 1989, including the adoption of a major law in 1993, an entirely reformed penal code still has not been adopted.

The civilian Internal Security Service (BIS) is independent of control by the Ministry of the Interior and reports to parliament and the Prime Minister’s office. The police and BIS generally protect the individual rights that are guaranteed by law. Some members of the police, however, have been guilty of occasional abuses, which have been disproportionately directed at Roma and foreigners.

Police may hold suspects without charge for no longer than 24 hours, a right that was recently upheld in the Constitutional Court. Court cases themselves have been greatly delayed due to the lack of experienced judges and investigators and a still-evolving legal environment. The time it takes for a case to go to trial has increased from 89 days in 1989 to 212 days in 1997, during which time defendants are held in custody. Approximately 35 percent of prisoners are detainees awaiting trial.

4. Do most judges rule fairly and impartially? How many remain from the Communist era? Judges rule fairly and impartially. A large number of judges were dismissed between 1989 and 1992 for connections with the former Communist regime. Many resigned voluntarily and now have private legal practices. The 1991 law on the judiciary designated judges appointed after January 1990 to be life-appointees. Those appointed before 1990 were dismissed as of August 1992 unless they were re-appointed within twelve months. Once re-appointed, they can hold their positions for life. Many new judges have been hired since the transition from communism began.

On the Constitutional Court, which was established in 1993, there are now 15 presidentially-appointed judges with ten-year terms.

5. Are the courts free of political control and influence? Are the courts linked directly to the Ministry of Justice or any other executive body? The judiciary is independent in law and in practice. Article 82 of the constitution states that judges “shall be independent in the performance of their office” and that “no one may jeopardize their impartiality.” In addition, a “judge may not
be recalled or transferred to another court against his will; exceptions, ensuing in particular from disciplinary liability, shall be specified by law.” Under Article 86, judges on the Constitutional Court are protected from interference. These protections are upheld in practice. New judges enjoy life tenure and are not demoted or transferred for political reasons.

Nevertheless, judges retain administrative connections with the Ministry of Justice, through which they are appointed and promoted. A 1995 Czech Helsinki Committee report took note of frequent interference in ongoing investigations and court trials by politicians making pronouncements through the media.

The earnings gap between judges and private sector attorneys is much larger than those in the West. In part as a result of Czech legal education, which trains lawyers and judges separately, and in part due to the public’s mistrust of the profession under the Communists, magistrates do not yet enjoy Western-style non-pecuniary benefits of prestige and respect. They also do not always have adequate support in the form of law clerks, court reporters, bailiffs, and legal materials.

6. **What proportion of lawyers is in private practice?** How does this compare with the previous year? It is estimated that over half of all lawyers are employed by the private sector, including Czech and foreign groups, legal firms, and other corporations. This represents no significant change from 1996-97. Salaries for lawyers in the private sector are substantially larger than for those in the public sector. Lawyers must belong to the Czech Bar Association in order to practice law.

7. **Does the state provide public defenders?** The Charter of Fundamental Rights and Freedoms guarantees access to legal assistance by accused indigents. In practice, the state does provide public defenders in criminal and some civil cases. The International Helsinki Committee has found, however, that many who would otherwise be eligible for such aid do not receive it because the process involved is complicated.

8. **Has there been a comprehensive reform of anti-bias/discrimination laws, including protection of ethnic minority rights?** Hate crimes, particularly against Roma, are not unusual. There have been reports of neglect and even abuse by policemen, who are often slow to respond to calls for help by Roma who have been victimized in hate crimes. Observers have noted that local courts sometimes issue minor penalties for hate crimes, and deal more harshly with Roma than with Czechs. In June 1997, a judge in Hradec Králové refused to penalize a Czech for hate crimes on the grounds that Czechs and Roma belonged to the same race. The justice ministry, however, appealed the decision, which was reversed by the Supreme Court in October 1997.

In January 1996, a special department was established to deal with extremist groups, and directives were issued to prosecutors to seek higher penalties in hate-crime cases. In December 1997, the parliament ratified the Council of Europe’s Framework Convention for the Protection of National Minorities.

Approximately 3,500 people, most of whom are Roma, are de facto stateless. This is due to the cumbersome and overly bureaucratic naturalization procedures in Czech law.
1. What is the magnitude of official corruption in the civil service? Must an average citizen pay a bribe to a bureaucrat in order to receive a service? What services are subject to bribe requests — for example, university entrance, hospital admission, telephone installation, obtaining a license to operate a business, applying for a passport or other official documents? What is the average salary of civil servants at various levels? Observers report that the system of military contracting is the area most prone to corruption.

2. Do top policy-makers (the President, ministers, vice-ministers, top court justices, and heads of agencies and commissions) have direct ties to businesses? How strong are such connections, and what kinds of businesses are these? In May 1996, journalists uncovered evidence that contributions of $220,000 had been made to the ruling ODS in the names of a dead Hungarian and a Mauritian who had no known major sources of income. In November 1997, former foreign minister Josef Zieleniec stated that this money was likely to have come from a businessman involved in current privatization deliberations.

3. Do laws requiring financial disclosure and disallowing conflict of interest exist? Have publicized anti-corruption cases been pursued? To what conclusion? The privatization process has generally been free of major scandals. In October 1994, however, Jaroslav Lizner, the director of the Coupon Privatization Center, was arrested and charged with corruption in the privatization of the Klatovy Dairy. Lizner apparently accepted an 8 koruna ($300,000) bribe during a police sting operation.

   The Czech Republic has been the scene of numerous shoot-outs involving mafia members from republics of the former Soviet Union. In August 1997, three people were wounded in a Prague gunfight between members of Tajik and Ukrainian mafias. Chechen gangsters were involved in an earlier shooting incident.

4. What major anti-corruption initiatives have been implemented? How often are anti-corruption laws and decrees adopted? The Czech Republic signed the Convention on Combatting Bribery of Foreign Public Officials in November 1997. This document makes the bribery of foreign officials as much a crime as bribery of domestic officials. It also requires stricter accounting and record-keeping to increase transparency and reduce the bureaucratic concealment of corruption.

5. How do major corruption-ranking organizations like Transparency International rate this country? In July 1997, Transparency International ranked the Czech Republic 27th in its list of 52 countries surveyed for its Corruption Perception Index (CPI). The country’s CPI score was 5.20 in 1997 (on a one to ten scale on which low numbers indicate greater corruption, which represented a decline from 5.37 in 1996. Its corruption score is virtually the same as those of Hungary and Poland.
1. What percentage of the GDP comes from private ownership? What percentage of the labor force is employed in the private sector? How large is the informal sector of the economy?

In 1990, Czechoslovakia had the largest state sector of all the emerging post-Communist CEE countries, with only a negligible portion of national output from the private sector. As of the end of 1996, almost 75 percent of GDP had been produced in the private sector.

2. What major privatization legislation has been passed? What were its substantive features?

Restitution of Communist-confiscated property began in November 1990, and lasted until September 1991. Property with a value of 75 to 125 billion koruna was transferred into private hands through restitution. This included approximately 100,000 physical properties, such as houses, farms, and shops.

Privatization of small enterprises such as shops, service establishments, and restaurants followed the restitution process and created more controversy. Despite strong pressure for preferences in the form of closed rounds of auctions restricted solely to employees of the firms being privatized, the parliament rejected such preferences in the summer of 1990. After assets were selected to be privatized, the auctions were open to all Czech citizens, with no special preferences. The auctions began in January 1991, and were concluded at the end of 1993, although the majority of small enterprises were sold by April 1992. More than 22,000 small enterprises were sold, with shops constituting 58 percent of sales; service establishments, 18 percent; restaurants, 8 percent; and motor vehicles, 7 percent. The total value transferred through the program for the privatization of small enterprises amounted to more than 30 billion koruna, or more than $1 billion.

The foundation for large-scale privatization was created in April 1990, when laws established the legal foundation for converting state-owned enterprises (SOEs) into joint-stock companies. In the first half of 1990, the 100 large trusts that dominated the state sector were split into 330 independent enterprises, while the vast majority of Communist-appointed top-level directors were dismissed in favor of their deputies. With the need for speed and competition in mind, the large-scale privatization law was passed in April 1991. The initial large-scale privatization program was divided into two waves. The first began in February 1992, and the second was launched in April 1994. Privatization of each enterprise was based on the “privatization project.” These were proposals for the future of each firm, including restructuring and some combination of five different privatization instruments: transformation into a joint-stock company (or “voucher privatization”), direct sale to predetermined buyers, public auction, free transfer to municipalities, and trust funds. Management was required to submit a basic privatization project, but anyone was allowed to submit competing projects. These projects were submitted to a “black box” decision-making process at the Ministry of Privatization. Mirroring the experience with restitution and small privatization, speed was emphasized as a primary goal.

The Ministry of Privatization’s criteria for project selection gave priority to mass privatization components in competing proposals. As a result of this institutional bias, the voucher program became the core of the privatization program for large-scale enterprises. Three-fourths of medium and large enterprises in the beginning of the reform program had mass privatization components, however, the program had never been attempted on a large scale. Most Western academics and
observers had predicted that it would fail.

Beginning in 1991, all Czechoslovak citizens aged 18 or more were made eligible to purchase a voucher booklet from one of 648 distribution centers. The nominal purchase price was 1,000 koruna (approximately $35, or one week’s wages for the average worker). Trading was disallowed until the secondary market began after share allocation. Investment privatization funds (IPFs), which managed citizens’ vouchers and promised large returns, piqued public interest in vouchers. Approximately 72 percent of voucher purchasers of vouchers invested their points in IPFs. Eventually, 264 IPFs formed in the Czech lands for the first wave and another 353 formed in the second wave. The largest IPFs were run by insurance companies and commercial and savings banks.

Privatization has slowed considerably since the process began. Shares worth 229 billion koruna ($8.3 billion) are still in state hands. In part, this is due to the fact that all of the easy sales have already been made. Currently, 77 percent of these unsold shares are in 56 “strategic” enterprises and will be exceedingly difficult to privatize for political reasons. The privatization of the remaining enterprises, which are owned directly by the state or indirectly through the National Property Fund (NPF), the state body that holds unprivatized equity, will be made on a case-by-case basis.

The other major portion of privatization is the gradual sale of residual state shares in enterprises privatized in the two waves of voucher privatization. By the end of 1995, these had been valued at 52 billion koruna ($2 billion). The government sold these shares at the pace of 2 billion koruna per month through 1996.

### 3. What proportion of agriculture, housing and land, industry, and small business and services is in private hands?

**Agriculture:** Most agricultural land was privatized under restitution, a process that began in 1991. Other farms were put up for auction. As of mid-1995, it was estimated that approximately 90 percent of agriculture had been privatized, including all former cooperatives and most state farms.

**Housing and Land:** As part of property reform, the government passed a law soon after the 1989 revolution to give housing and land to the municipality in which they were located. Persons living in these units could then apply to buy them from the municipal government at a discounted price. This process may vary by municipality. In 1994, legislation was passed to provide for the discounted purchase of apartment houses by cooperative groups if members of the groups resided in the building. As of late 1994, it was estimated that approximately 40 to 60 percent of all housing units had been privatized.

**Industry:** It is estimated that the private share of industry exceeded 80 percent by early 1996. The remaining industries will be much more difficult to privatize. These industries are in the so-called strategic sector: communications, energy, mining and metallurgy, and transportation. In June 1995, a Dutch-Swiss consortium purchased a 27 percent stake in the SPT telecommunications monopoly. Twenty-six percent of the enterprise was sold for vouchers, while the remainder was held by the NPF.

Another important factor is the retention of ownership by the government through two major mechanisms. The first is the National Property Fund, which holds minority shares in firms sold through mass privatization. Studies have shown, however, that NPF board members have been extremely passive. Thus, state ownership of enterprise shares has not necessarily led to a politicization of
business decisions. The second mechanism of government ownership is the complex web of cross-ownership in the financial sector. The largest banks are still state-owned.

They hold large equity stakes in investment funds, which in turn own newly-privatized companies. While there has not been significant evidence of government interference through these links in privatized firms, there is still some legitimate cause for caution. The ongoing privatization of state-owned banks is an important step toward finding a long-term solution to this problem.

*Business and Services:* Nearly all small businesses and services have been privatized. Out of a workforce of 5 million, the Czech Republic now has nearly 900,000 entrepreneurs, most of whom are involved with newly founded businesses rather than former state companies. Small businesses are the fastest growing portion of the private sector. They now provide 20 percent of industrial output.

### 4. What has been the extent of insider (management, labor, and nomenklatura) participation in the privatization process? What explicit and implicit preferences have been awarded to insiders?

The “small privatization” process of retail, trade, and consumer service establishments was competitive. In auctions, winning bids were, on average, approximately 6.3 times the opening price. This indicates that insiders were not able to buy formerly state-owned businesses without substantial competition from outsiders. This contrasts with Poland, where winning bids were approximately the same as the opening price.

In the first two waves of sales of large enterprises in 1992 and 1994, outsiders were allowed to submit competing privatization projects. Competition was intense, with an average of 17 proposals received for each state firm. There was no institutional bias in favor of insiders. In fact, winning privatization projects had overwhelming voucher components. Observers have called the voucher process the least insider-dominated form of privatization.

### 5. How much public awareness of and support for privatization has there been? What major interest groups oppose and advocate privatization?

The CSSD, led by a vocal Zeman, has been an opponent of the privatization process as conducted by the former governing coalition. It is particularly opposed to further privatization in the health care and energy sectors, as well as to the restitution of property to the church. The unreformed Communists are also major opponents of privatization, but they remain marginal as a political force.

### Macroeconomics

1. Has the taxation system been reformed? (What areas have and have not been overhauled? To what degree are taxpayers complying? Is tax compliance difficult to achieve? Has the level of revenues increased? Is the revenue-collection body overburdened? What is the overall tax burden?)

The old tax system was only slightly reformed between 1990 and 1992. This tax system relied mainly on implicit taxation in the form of turnover taxes and confiscation of SOE profits. In January 1993, the Czech Republic introduced a major tax reform through a value-added tax (VAT) and new corporate and individual income taxes. There have been three major goals of tax reform since the transition. The first of these was to subject the mushrooming private sector to normal taxation, especially as the government was essentially giving away its tax base through privatization.
and the restructure of SOEs. The second goal was to broaden the tax base. Accordingly, services were included for the first time. The final goal was to reduce the overall burden of taxation. This was accomplished by lowering tax rates, which had been as high as 85 percent with further levies on profits, and increasing depreciation allowances. The new taxes also achieved this goal by being much less distorting, which reduced taxation’s excess burden on the economy.

Major taxes currently levied in the Czech Republic include a personal income tax of 15 to 40 percent; a corporate income tax of 35 percent; a social security fund tax of 12.5 percent for employees and 35 percent for employers; a VAT of 22 percent, but only 5 percent for some items; a social insurance tax of 35 percent. There is no capital gains tax.

The VAT was reduced by one percent in January 1995. Another tax reduction took effect in January 1996, when all corporate and personal income taxes were reduced by several percentage points. In January 1998, several tax rate reductions were introduced. The VAT rate on energy was reduced from 22 to 5 percent, and the corporate income tax rate was cut from 39 to 35 percent.

Enforcement of taxes is relatively lax, especially in small-scale enterprises. Underreporting profits and keeping two sets of accounting books (one accurate book and another for the tax collector) are widespread practices. Some shops reportedly ask customers if they want to buy a product “with Klaus or without Klaus”, that is to say, with or without sales tax. Czech police and tax authorities complain that irregularities in the tax and commercial codes prevent proper investigation and prosecution of tax violations. According to one police estimate, only 10 percent of tax violators are caught. The problem is compounded by the frequent changes in the tax code in the early transition years and by the prevalence of easily hidden cash transactions.

The most spectacular decline in tax revenue in the region between 1989 and 1993 took place in the Czech Republic. While this record improved in the following years, a decline in tax revenue in the second half of 1996 has increased the government’s willingness to increase tax compliance, especially in the area of the VAT.

2. Does fiscal policy encourage private savings, investment and earnings? (Has there been any reform/alteration of revenue and budget policies? How large are budget deficits and overall debt? Is the financing of the social insurance/pension system sustainable? What proportion of the budget is taken up by subsidies to firms and individuals?) The bulk of macro-economic reform began in September 1990. This included stabilization of the economy through a restrictive fiscal and monetary regime and the reduction in the size and interventionism of government. Czechoslovakia had inherited not only a swollen state enterprise sector, but also an expansive and intrusive government, even by the standards of Communist countries in the region. In 1989, government revenue and expenditure amounted to 62.1 percent and 64.5 percent, respectively, of GDP, compared with 41.4 percent and 48.8 percent for Poland. The governing coalition has reiterated its commitment to lowering government expenditures as a proportion of GDP by 1 percent annually.

The Czech Republic has come closest to the balanced budget ideal of all transition economies and actually achieved a surplus in 1993, 1994, and 1995. The budget deficit rose to 2.3 percent of GDP by the end of 1996. Local governments’ budgets are generally balanced. Gross indebtedness is only 18 percent of GDP.

A balanced 1998 budget was passed in October 1997. This was a considerable achievement in
the aftermath of the substantial budgetary cuts necessitated by the May 1997 currency crisis.

The solid general macroeconomic picture led Standard and Poor’s to give the Czech Republic an “A” investment grade rating. The Organization for Economic Cooperation and Development (OECD) admitted the republic — the first post-Communist nation to gain admission — in December 1995.

Prior to 1989, Czechoslovakia had been spending an astonishing 25 percent of GDP on industrial subsidies. The massive decrease in this spending provided the bulk of the reduction in government expenditures between 1990 and 1992. Subsidies then fell to only 4.6 percent of GDP — an average rate for market economies. Curtailing the growth in the money supply and inexpensive credits to SOEs drastically reduced a large indirect subsidy. Together, these reductions in subsidies represented a genuine hardening of budget constraints of SOEs.

Subsidies for housing cost 13.7 billion koruna ($507 million) in the 1997 budget. Heating subsidies cost 4.5 billion koruna ($167 million), a decrease from the previous year’s 6.9 billion koruna ($256 million). The new power of the CSSD-led opposition in parliament may lead to an increase in social expenditures, since its cooperation in other areas of economic policy is needed. Nevertheless, real reform is needed in health insurance and pension programs, where an awkward mix of state and market policies manages to be both unstable and inefficient.

The government’s balanced 1998 budget was passed by parliament in October 1997.

3. Has there been banking reform? (Is the central bank independent? What are its responsibilities? Is it effective in setting and/or implementing monetary policy? What is the actual state of the private banking sector? Does it conform to international standards? Are depositors protected?)

The State Bank of Czechoslovakia was established as the independent central bank in charge of monetary policy in 1990. Its Czech successor, the CNB, is independent by law. Article 98 of the Constitution notes that “the main purpose of [the CNB’s] operations shall be to care for the stability of the currency” and that “intercessions in its operations may be effected only on the basis of law.” It is also autonomous in practice. It is responsible for money market policy, the money supply, regulation of the banking sector, and the determination of interest rates. Most regulations accord with EU-standard banking regulations. The CNB’s supervisory authority was augmented by two amendments to the banking code in 1994. These amendments also established deposit insurance, which guarantee deposits of up to 100,000 koruna (approximately $3600).

The Czech banking sector is one of the weakest and least reformed areas of the economy. It suffers from numerous problems, including a lack of experience in management and lending, cases of outright fraud, a lack of transparency, and inadequate supervision from above by the CNB. Bank-sector privatization also lags behind that of other sectors of the economy.

A more systemic problem in the banking sector is the complex web of interlocking ownership and credit arrangements between the banks, investment funds, the government, and the NPF. For example, the Investicinia Postovni Banka (IPB) directly or indirectly owns many Czech companies. At the same time, these companies are owners of the IPB bank. This sort of confused ownership undermines shareholder control of banks and leaves management free from the discipline imposed by profit-maximizing owners. In early 1997, however, the CNB proposed reforms to begin to address this problem. These include restrictions on ownership of non-bank firms, as well as a ban on
shareholder ownership of more than a 10 percent stake in a bank.

In 1996, the Czech banking system underwent a severe crisis. Initially, the problems were confined to small banks that could not meet capital requirements. In August 1996, the Kreditni and Investicni Banka, the nation’s sixth largest, collapsed. Its fall resulted in the loss of 12 billion koruna ($440 million). In September 1996, the CNB placed Agrobanka, the largest private bank and the fifth largest overall, under forced administration. An auditor estimated losses in that case to be 10 billion koruna ($330 million). In all, 12 of 60 banks failed in the crisis. Six of these are in bankruptcy, and the rest under forced administration. As of June 1996, 39 percent of bank loans were “classified,” which means that “there exists uncertainty about their repayment.”

In September 1996, Czech police charged five people with fraud in connection with the Kreditni collapse. The government soon established a special investigative team to examine issues of bank fraud. A special parliamentary commission was also formed. In April 1997, 11 people were charged in connection to the Agrobanka collapse. In May, two managers of Investicni bank were arrested on embezzlement charges.

A state company was established in October 1996 to buy bad loans from small banks in order to help stabilize them. Thus far, however, the collapses have only affected 4 percent of all banking assets. The costs of bank reconstruction in 1996 amounted to 37 billion koruna ($1.2 billion). Depositors were fully compensated by the Deposit Insurance Fund and credits provided by the CNB.

By early 1997, there were 54 licensed banks in the Czech Republic. Five banks dominate the sector, with 67 percent of its assets. Foreign banks hold 18 percent of its assets.

The pace of bank privatization has increased considerably, particularly of the four largest state-owned banks. In July 1997, the government announced the sale of its 36.3 percent stake in Investicnia Postovni Banka to Nomura International. In August, the state decided to sell the majority of the state’s shares in the other three — Komercni Banka, Ceska Sporitelna, and Ceskoslovenska obchodnibanka — to strategic investors.

4. How sound is the national currency? (To what extent has inflation eroded its value? Is the value of the currency fixed or does it float? Is the currency convertible? How large are the hard currency reserves? Has exchange rate policy been stable and predictable?) Since May 1993, the value of the koruna has been fixed to a two-currency basket. Thirty-five percent is fixed to the dollar, and the remaining 65 percent is fixed to the German mark. In October 1995, the Foreign Exchange Law made the koruna fully convertible for current account transactions and partially convertible for capital account transactions. Firms are not restricted in borrowing funds from abroad.

From 1990 until 1995, the koruna’s fixed exchange rate was quite stable due to a determined Central Bank and extensive foreign exchange reserves. Substantial capital flows made it necessary to widen the fluctuation band to plus or minus 7.5 percent in February 1996. International speculative attacks on the koruna increased in early 1997, when markets gambled that the CNB would not be able to sustain the fixed exchange rate. While initially attempting to resist international forces, the CNB was forced to float the koruna in May 1997. The initial level of devaluation was 15 percent, but the level fell to 10 percent by the end of the summer.

Fiscal and monetary discipline is responsible for the moderate inflation record of the Czech
Republic, which is the best in post-Communist Europe. Inflation dropped from 10 percent in 1994 to 8.8 percent in 1996.

5. Is there a functioning capital market infrastructure? (Are there existing or planned commodities, bond, and stock markets? What are the mechanisms for investment and lending? What government bodies have authority to regulate capital markets?) The Prague Stock Exchange (PSE) is the highest-capitalized equity market in the region. There are approximately 1,700 companies on the exchange, the majority of which were created by the two waves of voucher privatization. There are two alternatives to the PSE: the electronic RM-system for over-the-counter trades, and the Ministry of Finance-created Center for Securities. Both of these were originally created to trade privatization vouchers, but real shares are now traded on each.

Unfortunately, since its creation, the PSE has experienced numerous problems and has acquired the reputation of being an insiders’ market. The biggest of these problems is the lack of transparency. Many of the traded companies fail to provide information on their operations to potential investors. They also do not inform current shareholders of arguably important events like earnings and mergers. Another problem is the high number of bottlenecks in trading activity. These problems have led to chronically low liquidity.

In April 1998, a new Securities Commission began to address these problems. The commission’s enforcement powers are limited, however, in that it can only make recommendations to the Ministry of Finance.

Liquidity is low because most of the companies on the exchange are not regularly traded on the PSE itself. Most transactions are made privately. The average daily trading volume in 1995 was only $30.9 million. In 1997, 1,000 blocks of shares were removed from the PSE for lack of trading activity. The PSE is currently more of an instrument of trading equity than of raising it.

Amendments to securities law took effect in July 1996. They increased protections for minority shareholders by requiring new majority owners to offer a buyout to all shareholders at a weighted six-month PSE share price. In addition, boards will be prevented from taking a company private without a 75 percent majority decision by all shareholders. They also increase transaction transparency by requiring the disclosure of major share acquisitions, mandating that listed firms publish their annual statements three months after the close of the fiscal year, and establishing stock-lending, which was previously unregulated, as a “legally binding contractual relationship.”

The amendments also require licensing of investment funds, requiring the use of international accounting standards, mandating the segregation of investment fund assets from the assets they manage for their clients, and making them file quarterly reports on their portfolios. The enforcement of the last of these will be key, as investment funds in the past have ignored already-existing reporting rules.

The administrative capacity of the Ministry of Finance, however, may not be up to the task of Western-style regulation of the securities industry. Jan Ververka, the Ministry’s chief of capital markets supervision, complained in November 1996 that his department is only able to regulate actively 20 percent of the 800 investment funds and brokerages. Several Western investors have noted that regulators sometimes ignore clear violations of existing rules.

Two commodity exchanges exist in the Czech Republic. The first is the Brno Farm Produce
Exchange, founded in July 1993. It deals mainly with agricultural commodities. The more general Czech-Moravian Commodity Exchange in Kladno was established in November 1995, and trades a wide variety of commodities.

As a result of a tight and well-managed fiscal policy, the Czech Republic’s bond market is dominated by long-term private sector debt. The market is relatively small, however, and, as a result, a mature secondary market in bonds has yet to emerge. The total nominal value of publicly traded bonds was 10.7 percent of GDP in June 1996. Bonds accounted for 35.7 percent of PSE trading in 1995. Liquidity and transparency in the bond market, as in the equity market, leave much to be desired. The bond derivatives market is immature.

1. Are property rights guaranteed? (Are there both formal and de facto protections of private real estate and intellectual property? Is there a land registry with the authority and capability to ensure accurate recording of who owns what? What are the procedures for expropriation, including measures for compensation and challenge? Have any seizures taken place?) Property rights are guaranteed under Article 10 of the Charter of Fundamental Rights and Freedoms, which, under Article 3 of the new constitution, is “an integral component of the constitutional system.”

The Czech Republic adopted a patent code in 1990 and a trademark law in 1988 and 1990. In June 1995, amendments to the trademark law harmonized the Czech intellectual property rights (IPR) “Law on Trademarks and Copyrights” with EU standards. These amendments make it easier to enforce, register, and sell trademarks, including those of foreign registry. The language on foreign registration was adopted after a small scandal in which the brother of a high-ranking government official registered names such as Jaguar, Toyota, Chevrolet, and Audi as his own. The Czech Republic is a signatory of numerous international IPR conventions. In April 1996, parliament adopted laws that strengthen the protection of computer software.

While Czech legal protections for intellectual property are adequate, enforcement is rather problematic, as in all other post-communist countries. For example, one major difficulty in implementation is the long delays in enforcing IPR laws against violators. The backlog of cases in the courts is approximately two years, enough time for substantial damage to have been incurred. As of the end of 1995, only 366 people had been convicted of IPR crimes. U.S. firms have estimated that more than $117 million was lost to copyright violations in 1997. This gap between law and practice has been recognized by the World Intellectual Property Organization, which has recently suggested that the Czech Republic be added to the list of countries impeding trade.

No expropriation has taken place since the end of Communist rule. Eminent domain is exercised under standards of international law, with due process and without discrimination.

Restitution of property nationalized by the Communists was completed by 1992. Nevertheless, due to the slow pace of courts, not all title has been transferred to new owners. This means that it is not always known who actually owns a particular property.

2. To what extent have prices been liberalized? What subsidies remain? Approximately 85 percent of government-controlled producer and consumer prices were liberalized in the beginning
of 1991. After the first year of liberalization, 18 percent of GDP was valued in regulated prices. Between 1990 and the end of 1992, this figure fell from 85 percent to 5 to 6 percent. Among commodity groups, energy, housing rents, water, transportation (especially passenger), telecommunications, health care, and some agricultural products are still regulated.

Nevertheless, the government has made public its commitment to liberalize these prices within the next several years. Even when prices are controlled, adjustments have been made consistently in the upward direction. In July 1997, for example, public housing rents were raised between 22 and 100 percent, gas and electricity prices were raised 15 percent, and heating prices were increased by 39 percent.

The government has effectively suspended national wage bargaining between labor, employers, and the government under the Tripartite Council. In July 1995, wage regulation by the government was eliminated.

3. Is it possible to own and operate a business? (Has there been legislation regarding the formation, dissolution, and transfer of businesses, and is the law respected? Do there exist overly cumbersome bureaucratic hurdles that effectively hinder the ability to own and dispose of a business? Are citizens given access to information on commercial law? Is the law applied fairly? Does regulation (or do licensing requirements) impose significant costs on business and consumers? Do they create significant barriers to entry and seriously hamper competition?)

Operating a business is relatively easy to do. Forming a business, however, necessitates navigation through a lengthy and complex process of obtaining registrations and licenses.

The Czech Civil and Commercial Codes, which were adopted in 1992, are based heavily on the German and Austrian codes. The Commercial Code, which was adopted in January 1992, replaced 80 scattered regulations and codes and established the framework for inter-business transactions. Many of the provisions of the codes, however, remain vague.

The first Czech bankruptcy law was adopted in 1991. A second law was passed in 1993. The revised bankruptcy law of March 1996 streamlines and simplifies the bankruptcy process, thereby eliminating old bureaucratic obstacles. It now permits forced debt restructuring and prevents “looting” transactions. Nevertheless, the major Czech banks that are the largest creditors remain hesitant to force their debtors — inefficient and large ex-state-owned enterprises — into bankruptcy. The political repercussions of these state-owned banks imperiling the jobs of thousands of workers, for now, outweigh the financial costs incurred by not initiating bankruptcy proceedings. Moreover, bankruptcy remains an uncertain proposition for both debtor and creditor. This is due to the three-to-four-year backlog in bankruptcy courts and the lack of an established secondary market for seized assets. As with dispute resolution, courts do not have enough experience and resources. Bankruptcy statistics show, however, that, even before the recent amendments, firms and courts were gaining experience with the procedure and were disposing of cases more efficiently.

4. Are courts effective, transparent, efficient, and quick in reaching decisions on property and contract disputes? What alternative mechanisms for adjudicating disputes exist? The courts are frequently not effective in settling disputes. This is due to the burden of a very large number of new cases, inadequate number of judges, and the inexperience of these judges in deal-
228 nations in transit

...ing with complex commercial issues. This leads to significant time lags in rendering judgment. Commercial disputes are heard between seven months and two years from the date of filing. Decisions are reached between one and three years later. A large body of established precedent has also yet to be followed. Important trial judgments are published.

The Czech Republic is a member of the New York Convention on Arbitration and is therefore legally bound to recognize and enforce arbitration decisions.

5. Is business competition encouraged? (Are monopolistic practices limited in law and in practice? If so, how? To what degree is “insider” dealing a hindrance to open competition? Are government procurement policies open and unbiased?) The country’s competition law was adopted in 1991. The Office for the Protection of Economic Competition is responsible for policing anti-competitive behavior. The Czech Republic has been judged to have been one of the most successful competition policies in the region. Furthermore, an agreement was reached in January 1996 to coordinate and harmonize the competition policies of the Czech Republic and the European Commission.

As elsewhere in the region, however, the country’s competition office is dominated by staff from the price-control ministries of the old regime. These people and, by extension, the ministry, often see their role as enforcing economic policy rather than establishing fair operating rules. For example, competition authorities have been involved in investigating the justification for insurance price-hikes. They have also meddled in industrial policy-making by allowing a firm to acquire 60 percent of the Czech coffee market in return for employment and investment guarantees. In addition, the problem of industry “capture” of regulatory agencies seems particularly acute across post-Communist Europe, with the Czech Republic as no exception. A snug relationship between managers and regulators has often led to competition policy regulators actually deterring new competition.

Insider trading of public companies is illegal. In practice, however, Czech equity markets have a reputation for being insider-dominated.

Czech procurement procedures are generally fair and open for large contracts at the central level. This is often not the case, however, at local levels, where political connections often count for much in awarding contracts. Another problem is that utility monopolies and other state-owned entities that are not receiving large budget transfers are not required to adhere to government procurement procedures. Finally, domestic firms receive a 10 percent price advantage over their foreign competitors. The impact of this is negligible, however, because most foreign investors establish legal entities in the Czech Republic. The competition ministry advocated procurement law amendments that took effect in July 1996. Improvements include the clarification and simplification of public tender procedures at both the local and federal levels. In addition, they institutionalize transparency-building devices, such as publishing winners and winning amounts, and they force government bodies to reveal selection criteria for tenders.

6. To what extent has international trade been liberalized? To what degree has there been simplification/overhaul of customs and tariff procedures, and are these applied fairly? What informal trade barriers exist? The Czech Republic’s tariffs stand at an average rate of five per-
A deteriorating trade deficit in 1997 prompted two new measures. In April 1997, an import deposit scheme was adopted, only to be eliminated in August after much protest from the EU. In May, anti-dumping legislation was adopted.

With the exception of controlled goods, no export controls exist. Exports account for a large proportion of the Czech economy. In 1995, they accounted for 61 percent of GDP. In May 1994, the government established the Czech Export Bank to encourage exports by providing access to state-subsidized medium- and long-term financing.

Quantitative controls on imports were almost entirely abolished in 1990. To the extent that they exist, non-tariff restrictions are few, very liberal, and generally transparent. Certain imported goods require a license but these are not difficult to obtain. Product and labelling standards, while strict, are rapidly being harmonized with European and international standards. Product testing regulations were streamlined and liberalized in reforms that took effect in January 1997. In the early years, product testing was performed at state-run testing stations and often constituted a bureaucratic nightmare. Now, testing for most products is voluntary and performed at efficient private testing stations. Border customs stops are generally fairly simple for goods in transit to and from Western Europe but are much more onerous for those bound to and from Eastern Europe.

As a member of the General Agreement on Tariffs and Trade, the Czech Republic acceded to the World Trade Organization in January 1995. In addition, it is a founding member of the Central European Free Trade Agreement (CEFTA), which also includes Poland, Hungary, Romania, Slovakia, and Slovenia. All nonagricultural and food trade within CEFTA is scheduled to become duty-free in 1998. The Czech Republic is also a member of the European Free Trade Associate and has an association agreement with the EU. The EU Commission formally recommended that accession negotiations begin with the Czech Republic in July 1997. Membership, however, is not expected before 2002.

7. To what extent has foreign investment and capital flow been encouraged or constrained?
Generally, there is no legal discrimination against foreign firms. Foreigners can establish any form of business organization permitted to citizens. As part of its OECD accession agreement, the country promised not to give preferences to domestic firms in privatization sales. Profits earned on Czech investments can be repatriated, but with a 25 percent tax, which is standard for EU countries and which is lowered if double-taxation treaties are in effect. There are no land ownership restrictions on foreigners.

Nevertheless, in practice, there have been a few instances in which foreign firms have been treated differently. These have occurred in the petrochemical, telecommunications, media, and brewery sectors. These sectors are politically sensitive because they are highly visible and dominated by giant firms. Moreover, there are certain sectors that are explicitly reserved for domestic firms. These so-called strategic sectors include defense-related industries, pure-alcohol distilleries, national monuments, and, at least for now, telecommunications, and banking. Finally, although they were liberalized in 1996, government procurement procedures still give a 10 percent price
advantage to domestic firms.

In the past, the government largely ignored calls to offer special tax incentives to foreign investors. With the political turmoil arising after the May 1997 currency crisis, this is in the process of changing.

On the strength of several major investment deals, foreign direct investment (FDI) reached a record $2.5 billion in 1995, but fell to a disappointing $900 million in 1996. Cumulative FDI over the 1990-1996 period was $6.4 billion. With its 30 percent share, Germany is the top investor. The United States, Switzerland and the Netherlands follow, each with approximately 14 percent.

There are few regulations that limit capital flow.

8. Has there been reform of the energy sector? (To what degree has the energy sector been restructured? Is the energy sector more varied, and is it open to private competition? Is the country overly dependent on one or two other countries for energy [including whether exported fuels must pass through one or more countries to reach markets]?)

Energy sector reforms in the Czech Republic date from 1992, when the distribution and production sub-sectors were separated. Shortly afterwards, Ceske Energetickie Zarody (CEZ), the state electricity monopoly, was “privatized.” (The state has yet to sell the NPF’s 67 percent share). Later, the country’s ten large heat plants were sold to investment funds and individual shareholders. Furthermore, the privatization of state-owned enterprises in itself liberalized the energy sector because these cumbersome, over-sized entities operated their own power plants. In November 1994, the parliament passed legislation to establish the legal framework for energy production and trade.

Since then, liberalization of the energy sector has stalled. While private firms were producing 20 percent of the country’s energy in 1994, by March 1996 the private sector share had only increased to 30 percent. The inadequate 1994 energy law has not been amended, the NPF stake in CEZ has not been sold, trade in electricity on the CEZ network has not been legalized, the nation’s eight distribution companies have not been fully privatized, the creation of an independent regulatory commission has been delayed, and pricing is still not market-driven.

Due to state regulation and subsidy policies, the price of energy does not cover production costs. These controls ensure that households receive a far lower price for electricity by being subsidized through high prices charged to industry. This has led to the inefficient use of electricity in homes for such purposes as heating. Prices are currently increased twice a year in 15 percent increments. In September 1996, the government’s economic ministers recommended a total liberalization of energy prices over a two-year period.

Domestic coal provides slightly more than half of the country’s energy requirements. Eighty percent of the Czech Republic’s natural gas needs are met through imports from Russia. Nuclear energy supplies 22 percent of the country’s energy requirements. Until 1995, when an oil pipeline from Germany was completed, almost all oil supplies were imported from Russia. The pipeline will carry two million tons of crude oil, compared with the five million tons carried by the Russian pipeline.

Recent developments have demonstrated the state’s willingness to allow foreign involvement in the energy sector. In October 1995, the Czech electricity transmission network was connected to UCPTE, the European transmission network. A consortium of Western oil companies, includ-
ing Shell, Conoco, and Agip, finalized the purchase of a 49 percent ($138 million) stake in Ceske
Refinerska in February 1996. The consortium has promised $480 million in investment. Unipetrol,
the state-owned holding company, controls the other 51 percent.