



The CS Fondy: A Test of the Ministry of Finance's Commitment to Investors

A week after the official launch of the *Czech National Strategy for the Development of the Capital Market* the Czech Ministry of Finance (MoF) faces a test of its commitment to better investor protection. News of the MoF's plan to put the 3 former CS Fondy (now managed by AKRO investiční společnost, a.s.) into liquidation has been met by our unit-holders with a mixture of anger and disbelief. A recent lower court decision, which found in favour of the MoF, is subject to appeal to the Supreme Court. It had been assumed no action would be taken to liquidate these funds until after that case had been heard, in the same manner as 2012, when the financial regulator insisted the more than CZK2bn of damages received shouldn't be distributed among the unit-holders until after the Supreme Court had ruled on the MoF's appeal. Fortunately, the MoF has so far shown willing to discuss the matter, so all is not yet lost for the (approximately) 40,000 surviving investors in these funds.

Quick Recap

For those less familiar with the case, in 1997, in the biggest financial scandal of the time, CZK1.23bn was 'tunnelled' from the CS fondy through the purchase of shares in a worthless poultry farm. The money was then quickly transferred abroad. 50,000 investors lost their savings. Although a number of people went to prison, none of the 'big fish' were ever caught and therefore main culprits went unpunished. In 2005, after the Statute of Limitations had expired, František Chobot (alias Frantisek Bušek) came forward claiming he had 'tunnelled' the funds along with Pavel Tykač. To 'rub salt into the wound', Frantisek Bušek posed provocatively in front of the Press.

In 1997, AKRO investiční společnost, a.s. took over the management of what little assets remained in the CS Fondy. On behalf of the CS fondy investors, AKRO brought successful cases against the former custody bank (Plzenska Banka) and against the Ministry of Finance,



AKRO investiční společnost, a.s. Slunná 25, 162 00 Praha 6, IČO: 49241699, tel.: 234 261 600, fax: 234 261 605, internet: www.akro.cz
AKRO investiční společnost, a.s., byla dne 8. října 1993 řádně zapsána do obchodního rejstříku vedeného Krajským obchodním soudem
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whose Financial Analytical Unit (FAU) had allowed the monies to be transferred abroad despite warnings the transfer should be stopped.

However, in a disappointing judgement, last November, the Court of Appeal ruled that the CZK2bn of compensation should be returned to the MoF along with statutory interest at 8.02% p.a. It was argued that the statute of limitations on the claim didn't start from the when the police filed criminal charges against MoF officials but from an earlier date when it ought to have been clear that the MoF was culpable. With the goalposts moved, AKRO's claim fell just outside the Statute of Limitations. AKRO without delay returned the CZK2bn to the MoF and immediately appealed, not only against the decision to return the compensation to the State but also against the default interest which, as one of our professional advisers commented: "seemed to reward the MoF for doing a bad job". Furthermore, along with the appeal, AKRO filed an application for deferment of the enforceability of the judgement to the extent of the default interest, and asked the MoF to delay the recovery of the default interest until after the Supreme Court decision. A link to the judgement and the basis of AKRO's appeal can be found on AKRO's website. Readers can draw their own conclusions.

While the CZK2bn compensation initially awarded to AKRO's investors in the former CS fondy was immediately returned to the MoF, the statutory interest amounts to a staggering CZK700m and would require the liquidation of the funds to repay. A perverse outcome.

We understand that the MoF is in a difficult position in relation to this case. On the one hand the MoF is the lead ministry for promoting the Czech Capital market and for enacting legislation to protect investors. On the other hand, it's found itself a defendant in a long-running court case.



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Don't Despair (Just Yet)!

With so much at stake, more than just the CS fondy, I've decided to speak from the heart. It's well known that I'm the only 'western' portfolio manager working in the domestic mutual fund market. Less well known, is that, in my more than 30 year career, I've managed mutual funds regulated under the jurisdictions of Canada (Ontario), US, UK, Switzerland, Australia, Japan, amongst others. Never have I worked in a jurisdiction where investor protection is so weak. The scams and the undeclared conflicts of interest are so blatant; it is truly depressing. I make no apologies about AKRO's sometimes harsh analysis, e.g. most recently related to Czech laws related to squeeze-outs of minorities. I know I speak for a silent majority. We are promised ANO "Will be different" and the coalition partner CSSD "Social Justice". Well here, with the CS fondy, is the chance to prove it. 40,000 ordinary, now elderly, citizens: How will you protect their interests? What have they done to deserve this? Nothing. The criminal justice system, the legal system, has badly let down these honest and hardworking citizens. In no other jurisdiction I have worked would these citizens be left with a total loss. If that happens: What message does that send?

I'm pleased to say that the current MoF have been open to discussion about the plight of the unit-holders in the former CS fondy (so please no premature despair!). I regard this as an extremely positive development. In the past, we have been seen as the opposition, a nuisance, the enemy even. AKRO investiční společnost, a.s. and the unit-holders of the former CS fondy, are not the enemy: Quite the contrary. Yes, the fund manager may be British, but AKRO is one of the only surviving Czech owned mutual fund groups. AKRO investiční společnost, a.s. is a model of good corporate governance: assets in the safe independent custody of CSOB, trading through an independent brokerage (ING) and audited by the respected BDO. Currently AKRO is the only ISO Quality accredited Czech investment company. Furthermore, recent years have seen a strong performance from all AKRO funds, not just the AKRO fond nových ekonomik but also a truly spectacular performance from the fond progresivních společností. This latter fund, a former CS fond, is one of Europe's best performing funds focused on smaller companies. How is the liquidation of this fund in the interests of the Czech capital market?

Concluding Remarks

I'm either optimistic or naive, but, I believe the current engagement between the MoF and AKRO might well produce a fair resolution to this protracted case. It has certainly facilitated a frank and open dialogue: That in itself is a huge positive. It is clear from the recent *National Strategy for the Development of the Capital Market* that investor protection is recognized as a prerequisite for a successful capital market. Indeed, strong investor protection is the defining characteristic of all successful capital markets, e.g. US, UK, Luxembourg, Switzerland,



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Singapore, Hong Kong. If the dice can be 'loaded' in favour of investors, the Czech Republic won't just end up with a capital market of the 'premier league', it will fill the gap as Central-Europe's regional capital market of choice.

Jeremy Monk,
Investment Director,
AKRO investiční společnost, a.s.
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