MASTER THESIS

Titel der Master Thesis / Title of the Master‘s Thesis

„Possibility of application of piercing the corporate veil- enhancing protection of creditors in unfair liquidation of companies in Slovakia? A comparative analysis of application of the doctrine in Austria, the UK and the Czech Republic“

verfasst von / submitted by

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DECLARATION

I solemnly declare that this Master thesis contains no material that has been submitted and/or accepted for the award of any other degree in any University or institution of higher education. To the best of my knowledge and belief, this thesis contains no material previously published or written by any other person, except where due reference is made in the text. I hereby certify that I am fully aware of the consequences for the academic offence of plagiarism, in accordance with the applicable Program and Exam Regulations of The University of Vienna.

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ABSTRACT

Kohút, Dávid. *Possibility of application of piercing the corporate veil- enhancing protection of creditors in unfair liquidation of companies in Slovakia? A comparative analysis of application of the doctrine in Austria, the UK and the Czech Republic* [Master Thesis]. University of Vienna. School of Law. Department of Commercial and Business Law. Supervisor: Univ.-Prof. Dr. Dr. Thomas Ratka, LL.M. LL.M. Vienna, 2019. 81p.

The presented Master thesis aims at assessing whether the current legal framework of the Slovak Republic offers sufficient protection of creditors in the event of an unfair liquidation of a company. It further assesses and contemplated the possibility of application of the doctrine of piercing the corporate veil as the instrument in process of enhancement of protection of rights of the creditors. Such assessment is realized via analytical comparison of the implementation of the doctrine of piercing the corporate veil in selected jurisdictions. The presented Master thesis is divided into five chapters, with the first chapter briefly discussing the legal obligations that are circumvented via the unfair liquidation. The second chapter is dedicated to the process and forms of realization of the unfair liquidation. The aim of the third chapter is to analyse the current legal framework of the Slovak Republic in the process of protection of creditors in the event of unfair liquidation and to propose the doctrine of piercing the corporate veil as the possible solution to the protection of creditors' rights. The fourth chapter compares the diverse forms of implementation of the doctrine of piercing the corporate veil in the selected jurisdictions of the Czech Republic, the Republic of Austria and the United Kingdom. Lastly, the fifth chapter draws the conclusive final remarks and answers to the research questions of the presented Master thesis.

Key words: unfair liquidation, straw-man, transfer of shares, unfair merger,

ABSTRAKT

Kohút Dávid. *Möglichkeit der Anwendung der Durchdringung des Unternehmensschleiers - Verbesserung des Gläubigerschutzes bei unfairer Liquidation von Unternehmen in der Slowakei? Eine vergleichende Analyse der Anwendung der Doktrin in Österreich, Großbritannien und der Tschechischen Republik* [Masterarbeit]. Universität Wien. Rechtsschule. Abteilung für Handels- und Wirtschaftsrecht. Supervisor: Univ.-Prof. Dr. Dr. Thomas Ratka, LL.M. LL.M. Wien, 2019. 81s.

Mit der vorliegenden Masterarbeit soll bewertet werden, ob der derzeitige rechtliche Rahmen der Slowakischen Republik einen ausreichenden Gläubigerschutz bei einer ungerechtfertigten Liquidation eines Unternehmens bietet. Sie prüft und erwägt ferner die Möglichkeit, die Doktrin des Durchdringens des Unternehmensschleiers als Instrument zur Verbesserung des Schutzes der Rechte der Gläubiger anzuwenden. Eine solche Einschätzung erfolgt durch einen analytischen Vergleich der Umsetzung der Doktrin des Durchdringens des Unternehmensschleiers in ausgewählten Gerichtsbarkeiten. Die vorgestellte Masterarbeit ist in fünf Kapitel gegliedert, wobei im ersten Kapitel kurz auf die rechtlichen Verpflichtungen eingegangen wird, die durch die unfaire Liquidation umgangen werden. Das zweite Kapitel ist dem Prozess und den Realisierungsformen der unfairen Liquidation gewidmet. Ziel des dritten Kapitels ist es, den gegenwärtigen Rechtsrahmen der Slowakischen Republik im Prozess des Gläubigerschutzes im Falle einer unfairen Liquidation zu analysieren und die Doktrin des Durchdringens des Unternehmensschleiers als mögliche Lösung für den Gläubigerschutz vorzuschlagen. Rechte. Das vierte Kapitel vergleicht die verschiedenen Umsetzungsformen der Piercing-Doktrin in den ausgewählten Ländern der Tschechischen Republik, der Republik Österreich und des Vereinigten Königreichs. Abschließend werden im fünften Kapitel die abschließenden Bemerkungen und Antworten zu den Forschungsfragen der vorgestellten Masterarbeit gegeben.

Schlüsselwörter: unfaire Liquidation, Strohmann, Übertragung von Anteilen, unfaire Fusion,

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LIST OF ABBREVIATIONS

s. r. o.	spoločnosť s ručením obmedzeným – private limited liability company in Slovakia
GmbH	Gesellshaft mit beschänkter Haftung – private limited liability company in the Republic of Austria
i.e	id est – "that is"
Commercial Code	Act No. 513/1991 Coll. Commercial Code
Penal Code	Act No. 300/2005 Coll. Penal Code
Act on Bankruptcy	Act No. 7/2005 Coll. on Bankruptcy and Restructuring
Act on Business Registry	Act No. 530/2003 Coll. on Business Registry
Cross-border Merger Directive	Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies
EU	European Union
EEA	European Economic Area
ECJ	European Court of Justice
e.g.	exempli gratia – "for example"
etc.	etcetera
Civil Procedure Regulation	Act No. 160/2015 Coll. Civil Procedure Regulation
Civil Code	Act No. 40/1964 Coll. Civil Code
Tax Procedural Code	Act No. 563/2009 Coll. on administration of taxes (Tax procedural code)

Introduction

"The only man who sticks closer to you in adversity than a friend is a creditor."

(Author unknown)

The phenomenon of utilization of "straw-man" for the purposes of obviating the accountability of one's actions is, unfortunately, rather popular form of circumvention of commercial and criminal law in the Slovak Republic. Despite the fact that such circumvention was an "instrument" primarily pertinent to years following 1989' Velvet revolution that had taken place in then Czechoslovakia, it still remains an actual topic of discussion as it is utilized even in a present day. The problematics of a "straw-man" is a topic frequently discussed in media and in the public. The newly passed and nowadays effective amendment to the Commercial Code and the Amendment of the Penal Code with the insertion of new criminal offence of unfair liquidation, could be regarded as the reaction to the "deeply-rooted" problematic notion of utilizing "straw-man". The importance shall not only be limited to the criminal side of the unfair liquidation; moreover, the focus shall predominantly lie upon the commercial aspects of such action, in particular to the protection of creditors of the unfairly liquidated company.

Methodology

The research methodology used in the process of devising, researching, and writing of the presented thesis is the doctrinal research methodology which allows for critical analysis and examination of the selected legislation and other documents thereof.[1] Stemming from that, the main sources for the presented Master thesis are in following order, based on their relevance: primary legal statues of the selected jurisdictions, jurisprudence, legal principles and academic writing and/or scholarly articles on the presented topic. *Nota bene*, certain legislation of the Slovak Republic and the Czech Republic do not have an official English mutation and as such, the provisions quoted in the presented Master thesis are the paraphrased versions of the original Slovak and/or Czech Republic's legislation.

[1] T. Hutchinson, N. Duncan, '*Defining and Describing What We Do: Doctrinal Legal Research'* [2012] 17 Deakin Law Review 84, 85

Purpose and the thesis outline

The aim of the presented Master thesis is to assess and to compare whether the doctrine of piercing the corporate veil in light of the amended Commercial Code could offer sufficient protection and guarantees for the creditors of the unfairly liquidated companies. In particular, the main aim of the Master thesis is to analyse and to compare the amendment of the Commercial Code of the Slovak Republic in light with instrument of the piercing the corporate veil as implemented in the legal framework of selected jurisdictions. The Master thesis will analyse the amendment to the Commercial Code of the Slovak Republic, taking into account variety of new instruments and their prospective reinforcing effect on protection of the creditors. Subsequently the Master thesis will evaluate similarities and differences of the said amendment with the instrument of piercing the corporate veil at large. Following such analyses, the Master thesis will then focus on the instrument of piercing the corporate veil as implemented in the legal framework of the following EU Member States: the Czech Republic, the Republic of Austria and the United Kingdom and will offer a comparison of their respective implementation and practical usage. The last, residual, aim of the Master thesis is to offer *de lege ferenda* for the legal framework of the Slovak Republic in respect to the protection of creditors via the instrument of piercing the corporate veil based on the findings of the above-mentioned comparisons.

For the purposes of definition of the obligations that are being circumvented by the unfair liquidation, the first chapter of the Master thesis is dedicated to the explanation of specific terms of commercial law and their respective correlation. The second chapter deals with the notion of an unfair liquidation, it describes its mechanics as well as its effect on creditors and their respective claims thereof. The third chapter is dedicated to the amendment of the Commercial Code of the Slovak Republic, the notions that it introduced and their practical implementation, it further discusses the instrument of piercing the corporate veil as the mean of protection of creditors at large. The fourth chapter then analyses and compares the instrument of piercing the corporate veil as implemented in the legal framework of the selected jurisdictions. The fifth chapter draws from the findings of fourth chapter the *pro futuro* actions that could be implemented in the Slovak legal framework to effectively tackle the problematic of an unfair liquidation.

1 Liquidation vs. unfair liquidation

For the purposes of better comprehension of the unfair liquidation the following chapter describes the obligations that are being circumvented by such liquidation in the context of the Slovak legal framework. The Master thesis focuses on the obligations and the unfair liquidation of the private limited liability company (Slovak: *spoločnosť s ručením obmedzeným* [s. r. o.], German: Gesellschaft mit beschränkter Haftung [GmbH]).

A private limited liability company, as a legal person, has similarly to a natural person certain "life cycle", which may be broken down to specific phases. This said" cycle" may either be long or short, in certain situation a company may not even go through all of the phases, during its "life". In general, the life cycle of a company may be described as follows:

A company begins its life with a formation – the signing and the acceptance of the legally prescribed formation documents. Subsequently, the company gains its legal subjectivity by its registration to the Business registry.[2]

After the phases of formation and incorporation of a company, the next step is the realization of the business plan of the company, for which purpose the company was initially incorporated. The duration of this phase varies from company to company. A company in the fulfilment of its business plan enters in a variety of contractual legal relations, from which a company derives certain rights, but also certain obligations.

Should a company be either unable to pay its debts on time, or be insolvent, or by the decision of the court, or in an event the partners in the company no longer have an interest in the functioning of the company[3], the company enters in its final phase of a life cycle – a phase of its winding up and its dissolution. However, before the company is dissolved, it must firstly settle its relations with the creditors. For such purposes the company, after the decision to be wound up, enters into liquidation. However, this only happens when there is a presumption that the conditions of the entry into liquidation are fulfilled – i.e. the company's assets are sufficient to cover the claims of all of its creditors, and that its capital is not transferred to the legal successor. Should a company fail to fulfil the condition on

[2] P. Kubíček, M. Mamojka, M. Patakyová, '*Commercial law*' (Obchodné právo) (1st edn. Comenius University in Bratislava, Faculty of Law, Publishing department 2007) 108
[3] Act No. 40/1964 Coll. Civil Code (Občiansky zákonník), [2019] Slovak Republic Article 20a

sufficient amount of assets, that would cover all of its debts, the company is said to be insolvent, and the insolvency proceeding begins. The main reason of the insolvency proceeding is similar to that of liquidation – settlement of creditors' claims.[4]

In the ideal business environment, the above-mentioned institutes of liquidation and insolvency would be the sufficient means of the protection of rights of the creditors in an event of company's winding up. In practice, however, the business activity is often exercised by individuals, who do not have the intentions to settle the company's debts. On the contrary, such individuals seek variety of forms of winding up of a company without its proper liquidation or insolvency proceeding respectively – i.e. they liquidate the company unfairly.

The term "unfair liquidation" itself was incorporated in the Slovak legal framework by the Act No. 264/2017 Coll., that amended the Commercial Code, and simultaneously amended and extended other laws.[5] Whereas the terms liquidation and bankruptcy portrait the legally approved forms of winding up of a company, that are connected with numerous legal conditions mainly for the purposes of the settlement of claims of the creditors, the unfair liquidation is the direct opposite of those actions – legally disapproved form of winding up of a company. For the sake of comprehension and better portrayal of the obligations that are being circumvented by an unfair liquidation, it is of importance to firstly explain the terms "liquidation", "bankruptcy" and "winding up without liquidation" as they are defined in the Slovak legal order.

1.1 Liquidation of a company

A liquidation is a legal consequence of a winding up of a company without a legal successor. Pursuant to Art. 68 Commercial Code, the winding up of a company may be:

[4] Ján Husár, '*Legal framework on the liquidation of the legal person in Slovakia and the Czech Republic*'(Úprava likvidácie právnickej osoby v SR a ČR) [2013] 65 Justice revue (Justičná revue) 220, 230
[5] Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes (Zákon č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Slovak Republic

1) Voluntary, i.e. from the will of the company, or its partners:

- expiration of time for which the company was incorporated;
- decision of its partners on its winding up.

2) Involuntary, i.e. forced winding up of a company:

- decision of the court of business registry;
- decision of the insolvency court.[6]

From the date of winding up of the company, the company *ex lege* enters into liquidation, unless other provisions of law provide otherwise (see below – winding up of company without liquidation).[7] The wound-up company still remains its legal subjectivity. It still exists as a legal person with the full legal capacity to be a part of judicial or other proceedings against other natural or legal persons, and also, such proceedings may be led against it.

Despite this fact, the legal subjectivity of the company is no longer absolute. The company may no longer continue in its business activities, for which it had been incorporated. Its conduct is limited only to acts leading to its liquidation and/or its winding up. As such, the company may conclude new contract only for the purposes of termination of unfinished businesses, if any.[8]

As the term liquidation is not legally defined in any statutory provision of the Slovak Republic, its definition shall for the purposes of presented Master thesis be derived from Kolaříková, who states: "*The liquidation of the company means a legally adjusted approach in out-of-court settlement of assets in the wound-up company, which capital had not been transferred to a legal successor, and which shall be dissolved by the erasure from the business registry without a legal successor."*[9] As such, the liquidation is conducted for the purposes of assessment of company's assets and subsequent settlement of company's commitments towards company's creditors – i.e. private creditors, or commitments towards state. In case a surplus is reached after all of the commitments and claims have been settled

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6 Act No. 513/1991 Coll. Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 68(3)

7 Milan Ďurica, '*Widing-up, liquidation and dissolution of a business company (Part 1)*' (Zrušenie, likvidácia a zánik obchodných spoločností (1. časť)) [2003] 55 Justice Revue (Justičná Revue) 1034, 1049

8 ibid.

9 L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 176

in a liquidation, such surplus shall be distributed amongst the company's partners in a ratio respective to their paid-up capital to the company's initial capital or alternatively distributed by a distribution rules provided by the Articles of Association.[10]

Based on the above-mentioned definition of the liquidation the following clear-cut conditions of the entry of a company to liquidation may be identified:

a) sufficient assets to settle all of the company's commitment in their full amount, and

b) inexistence of company's legal successor.

The stated conditions must be fulfilled cumulatively. The fact that the company has entered into liquidation is an information obligatory recorded in the business registry and such entry has a declaratory effect. The proposal for recording of entry into liquidation in the business registry shall be submitted to a court by a liquidator[11], to whom, after his appointment, the capacity to act on behalf of a company as its statutory organ has been transferred. The liquidator is also obliged to announce the entry into liquidation to all known creditors and also to publish such information in the Commercial Journal for the purposes of protection of creditors.[12]

After the liquidation – after the approval of financial statements, final report on the process of liquidation, and the proposal for distribution of the liquidation surplus – the liquidator shall within 90 days from the approval of above-mentioned documents submit a proposal for erasure of the company from the business registry.[13] From the date of the erasure of the company from the business registry the company definitely ceased to exist and loses its legal subjectivity.[14]

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[10] Act No. 513/1991 Coll. Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 153(2)

[11] A. Kolembus, '*The winding up and liquidation of a company from legal, economic and tax perspective*'(Zrušenie a likvidácia obchodnej spoločnosti z právneho, účtovného a daňového hľadiska) [2016]15 15 Tax and Accounting advisor of the businessman (Daňový a účtovný poradca podnikateľa) 105, 110

[12] Supra note 11, Article 73

[13] Supra note 11, Article 75(5)

[14] A. Polák, P. Kubala, 'Winding up of a legal person and extinction of receivable'(Zánik právnickej osoby a zánik pohľadávky) [2005] 57 Justice Revue (Justičná revue) 1440, 1444

1.2 Bankruptcy of a company

The specific situation occurs when in the course of the liquidation, the liquidator discovers, that the company has assets of certain value, however, such value would not suffice for the settlement of all of company's commitments, and as such, company is said to be insolvent.[15] The liquidator shall in such cases without undue delay submit a proposal for declaration of bankruptcy.[16] Kubíček in its publication defines insolvency proceeding as "*specific form of judicial proceedings, which aim is to align the assets of the debtor, who had become insolvent*."[17] Pospíšil defines the insolvency proceeding as "*liquidating judicial proceedings, in which a court settles the debtors insolvency by an encashment (liquidation) of its assets and the subsequent collective satisfaction of the creditors from the yield obtained from an encashment of the debtor's assets.*"[18]

In the cases when the liquidator does not fulfil its obligation and does not submit a proposal for declaration of bankruptcy, he shall be accountable for the damage occurred to the creditors, which has arisen as a result of failure to submit a proposal for declaration of bankruptcy, similarly to the accountability of the statutory organ of the company.[19] Despite the fact that such obligation is explicitly stated in Commercial Code[20] and also in Act on Bankruptcy[21], the violation of this obligation has also criminal aspect stated in Article 242 par. 1 letter a) of Penal Code in a form of criminal offence of obstruction of insolvency proceeding, which in itself embodies the state's interest in the protection of the creditors of a company which becomes insolvent.[22]

Shall a court declare a bankruptcy on the assets of the company in liquidation, the liquidation shall be estopped by the date of the declaration of bankruptcy until the date of

[15] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 73
[16] ibid. Article 75(5)
[17] P. Kubíček, et. al, '*Commercial Law*' (Obchodné právo) (1st edn. Vydavatelství a nakladatelství Aleš Čeněk s. r. o. 2016) 350
[18] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 558
[19] Z. Nevolná, A. Halušková, A. Škrinár, '*The fundamental questions of commercial law*' (Základné otázky obchodného práva) (1st edn. Typi Univesitatis Tyrnaviensis 2005) 66
[20] Supra note 16, Article 72(2)
[21] Act No. 7/205 on bankruptcy and restructuring (Zákon o konkurze a reštrukturalizácii) [2019] Slovak Republic Article 11(2)
[22] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 242(1)

cancelation of bankruptcy.[23] During the insolvency proceeding the liquidator exercises his capacity only to the extent that had not been transferred to the trustee. After the cancelation of the insolvency proceeding the liquidator continues to exercise his capacity to the full extent. Should a company remain without any assets after the insolvency proceedings, the liquidation is no longer necessary, and the next step is erasure of the company from the business registry and its subsequent dissolvement. Should there be any assets after the insolvency proceedings, the liquidator shall continue with the liquidation.[24]

Nota bene, the declaration of bankruptcy may be declared without company's prior entry to the liquidation. This is possible via submission of proposal for declaration of bankruptcy by either debtor, creditor or other authorized person. It is important to state the difference, that whilst in a case of a creditor such proposal it is his right to do so, in case of a debtor it is his obligation to submit a proposal for declaration of bankruptcy, if he finds himself insolvent.[25]

The condition for the creditor's proposal for declaration of bankruptcy is the provision of the proof of the insolvency of the debtor. The debtor shall be rendered insolvent if following cumulative conditions are met:

- delay of the debtor with payment of at least two of his debts of more than 30 days,
- existence of at least two creditors,
- existence of written notice for payment from at least one of the creditors.[26]

The debtor (its statutory organ) is obliged to submit a proposal for the declaration of bankruptcy within 30 days from the date when the statutory organ of the debtor knew, or with the due care should have known that the company is insolvent.[27] If the submitted proposal fulfils all the formal and substantive criteria prescribed by the respective statute,

[23]A. Kolembus, '*The winding up and liquidation of a company from legal, economic and tax perspective*'(Zrušenie a likvidácia obchodnej spoločnosti z právneho, účtovného a daňového hľadiska) [2016]15 15 Tax and Accounting advisor of the businessman (Daňový a účtovný poradca podnikateľa) 105, 108

[24] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 181

[25] P. Kubíček, et. al, '*Commercial Law*' (Obchodné právo) (1st edn. Vydavatelství a nakladatelství Aleš Čeněk s. r. o. 2016) 350

[26] Act No. 7/205 on bankruptcy and restructuring (Zákon o konkurze a reštrukturalizácii) [2019] Slovak Republic Article 11(3)

[27] Supra note 26 356

the court shall within 15 days from the date of delivery of such proposal issue a decision on the commencement of the insolvency proceedings. The bankruptcy itself, however, commences only after the bankruptcy is declared, i.e. from the publishing of the decision on the declaration of bankruptcy in the Commercial journal.[28] After the declaration of bankruptcy, the court establishes the trustee to whom the rights to dispose with debtor's assets are transferred, and the trustee is authorized to act on the matters in connection with such assets. Those authorizations are exercised on behalf on the debtor and on the account of debtor.[29] One of the main tasks of the trustee is to create the inventory of the debtor's assets and their subsequent encashment.

From the moment of the declaration of bankruptcy the phase of submission of creditors' claims commences. The creditor is obliged to submit its claim within 45 days from the date of the declaration of bankruptcy. Should the creditor submit its claim after the 45 days period, his right to be satisfied is not void, however, the diapason of his rights in the bankruptcy proceeding is narrowed.[30]

The assets that belong to the debtor in the time of the declaration of bankruptcy and the assets that are acquired by the debtor during the bankruptcy are a part of assets in bankruptcy/bankruptcy estate, which is further divided to general and separated parts. The separated part of the assets in bankruptcy is formed by assets that serve as a security for the secured creditors. The general part of the assets in bankruptcy is formed by assets that do not serve as a security for the secured creditors.[31]

For the purposes of assessment of the company's assets, the trustee produces an inventory of the debtor's assets for each part of the assets in bankruptcy, these are published in the Commercial journal.[32] Once the inventory of the assets in bankruptcy is created, the trustee is authorized to encash the assets in the bankruptcy either via auctions, public offers, procurements, etcetera. After the encashment of the assets in the bankruptcy, the trustee creates the final proposal of the distribution of yield of the encashment and then submits it to the creditors' committee for the approval. If the proposal is approved, the creditors are no

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[28] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 559

[29] Act No. 7/205 on bankruptcy and restructuring (Zákon o konkurze a reštrukturalizácii) [2019] Slovak Republic Article 44(1)

[30] P. Kubíček, et. al, '*Commercial Law*' (Obchodné právo) (1st edn. Vydavatelství a nakladatelství Aleš Čeněk s. r. o. 2016) 361

[31] Supra note 29 566

[32] Supra note 30 Article 76(1)

longer entitled to submit their claims in the bankruptcy proceedings.[33] The creditors are satisfied/remunerated based on the approved distribution of yield. After the fulfilment of the approved distribution of yield, upon the trustee's proposal, the insolvency court decides on the cancelation of the bankruptcy.[34]

It is the form and the extent of the creditors' satisfaction that is the main difference between the liquidation of the company and its bankruptcy. Whereas the company may not enter into liquidation only if the presumption of non-complete satisfaction of creditors exists, the bankruptcy proceeding, on the other hand, provides only limited satisfaction of the creditors from its early beginning due to the insolvency of the debtor/company.

1.3 Winding up of a company without its liquidation

If the company does not dispose with any assets – *de facto* there is nothing to liquidate, in such case a company is wound-up without liquidation.[35] The Commercial Code connects a winding up without liquidation also with certain decisions of the insolvency court, in particular:

a) dismissal of the proposal on the declaration of bankruptcy due to insufficiency of assets,
b) cancelation of bankruptcy due to insufficiency of assets, that would not cover remuneration of trustee,
c) cancelation of insolvency proceedings due to insufficiency of assets or cancelation of bankruptcy due to insufficiency of assets,
d) cancelation of bankruptcy after the fulfilment of decision on distribution of yield, should no assets remain after the distribution.[36]

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[33] P. Kubíček, et. al, '*Commercial Law*' (Obchodné právo) (1st edn. Vydavatelství a nakladatelství Aleš Čeněk s. r. o. 2016) 364
[34] Act No. 7/205 on bankruptcy and restructuring (Zákon o konkurze a reštrukturalizácii) [2019] Slovak Republic Article 102(3)
[35] Milan Ďurica, '*Widing-up, liquidation and dissolution of a business company (Part 1)*' (Zrušenie, likvidácia a zánik obchodných spoločností (1. časť)) [2003] 55 Justice Revue (Justičná Revue) 1034, 1038
[36] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 68(2)

The common feature of those decisions is, that each of them reflect certain unfavourable situation regarding the amount of assets in the company. The result of such decision is therefore a winding up of a company without liquidation. A winding up of a company without liquidation is not however, only connected with negative debt-to-assets ratio of the company.

Within the meaning of Art. 68 par. 2 of Commercial Code, the company is wound-up without liquidation also in the case, in which the company has a legal successor, who overtakes the company's capital and who continues to conduct the company's business. In such cases a liquidation is not necessary as the capital of the company, i.e. all of the assets and debts of the company are *ex lege* transferred to the legal successor. In those cases, the company is either acquired, merged or dissolved with another company, or it changes its legal form. The company is deemed to wound-up from the date of the entry of such change in the business registry.[37]

The definition of terms "winding up with liquidation", "bankruptcy", and "winding up without liquidation" at the beginning, served as a briefing to legally approved form of "liquidation" of a company, which is in line with the interest of protection of creditors. In the business environment, however, one often comes across a businessman who does not have an interest in a proper liquidation of a company and the subsequent satisfaction of its creditors. On the contrary, their interest is to obliviate their responsibility for the company's commitments and maximalization of their profit, alternatively, obtainment of other advantage for themselves. For such reason they lean towards illegal practices, the result of which is unfair or "factual" liquidation of the company and damage to its creditors.

1.4 Overview

As the chapter depicts, the legal framework of the Slovak Republic contains three scenarios that deal with termination of business activity of the company and ultimately with the winding up of a company and its dissolution. The differences in those forms are either in the financial situation of the company before its winding up and the subsequent dissolution, or in the results of their respective processes. Whereas the financially "healthy" company

[37] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 186

may either be wound-up voluntarily by its partners or be wound-up without liquidation via merger or acquisition, the same cannot be said when the company does not have sufficient amount of assets to compensate its creditors. In such situation, the company either enters bankruptcy which ultimately leads into its dissolution. Despite the differences that each process of winding-up of the company encompass, all of them have a few features in common, they are often lengthy and require fulfilment of legal obligations breach of which may lead into financial, administrative or criminal sanctions. Those shortcomings of the above-mentioned legally approved processes have the result of steering the partner away from legally approved forms of winding-up of company.

2 Unfair liquidation of a company and the forms of their realisation

An unfair liquidation is a new criminal offence, that has been introduced to the Penal Code via the amendment of the Commercial Code No. 254/2017 Coll. that has come into force on 1. January 2018 save for the parts that has come into force as early as 8. November 2017. The merits of the criminal offence of an unfair liquidation is pursuant to Article 251b Penal Code as follows:

" (1) Any person who with an intention to obstruct the cessation of conducting a business via liquidation seeks or mediates a person that only borrows his first and last name and its identity for the overtaking of rights and obligations to which it has no genuine interest, for the purposes of transfer of shares of a legal person to such person, or for the purposes of establishing such person as its statutory organ or a member of statutory organ of a legal person, shall be liable to a term of imprisonment to five years."

"(2) The same sentence as referred to in paragraph 1 shall be imposed to any person who with an intention to obstruct the cessation of conducting a business via liquidation transfers his shares of a legal person to a person, who only borrows his first name and last name and its identity for the overtaking of right and obligations to which it has not genuine interest."

"(3) The same sentence as referred to in paragraph 1 shall be imposed to any person who borrows its first and last name and its identity for the purposes of transferring the shares of a legal person or for the purposes establishing that person as a statutory organ of a legal person, although such person has no genuine interest on transferring the shares of a legal person or becoming a statutory organ of a legal person or a member of statutory organ of a legal person, knew and should have known that a person who transferred the shares of a legal person to a former or established a former person as a statutory organ or a member of statutory organ of a legal person, had the intention to obstruct the cessation of conducting a business of a legal person via liquidation."[38]

[38] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251b

The three above-mentioned merits of the criminal offence of unfair liquidation therefore tackle the action that consists of:

- **seeking** or **mediating** a person that acts as a "straw-man" with an intention to transfer shares of a legal person to that person or for the purposes of establishing such person as a statutory organ of a legal person or its member;
- **transfer** of shares of a legal person to a "straw man";
- **oneself becoming** a "straw man".[39]

The Commercial Code contains neither the legal definition nor the actual term of "unfair liquidation". Despite such fact, we are of the view that an unfair liquidation within the meaning of its commercial law aspects cannot be restricted only to the action delimitated in the merits of the criminal offence of unfair liquidation – i.e. intentional transfer of shares of a legal person to a "straw man".[40] The standardized and legal form of cancelation of business activity (liquidation of a company, bankruptcy proceeding) is often circumvented by a businessman via realization of unfair merger, that is often conducted with the same aim – circumventing the obligations arising out of proper cancelation of business activity.

Based on such hypothesis and for the purposes of the presented Master thesis, we shall differentiate between variety of forms of realisation of unfair liquidation, which shall be analysed in the following section.

2.1 Unfair liquidation by transfer of shares

The most common, and colloquially speaking, the "easiest" form of unfair liquidation is a transfer of 100% of shares of a legal person to a "straw-man". Despite the lack of a legal definition of the term "straw man" ("*biely kôň – a white horse*" in Slovak), it is a term that is often used whether it comes to legal practice or public. Heretik defines those "straw men" as "*people [that are] put as a fictitious persons to variety of financial and economic*

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[39] B. Hager, P. Štrbová Marková, '*Substantial amendment of the Slovak'Commercial Code or another try for an effective protection of rights of the creditors*'(Veľká novela slovenského Obchodného zákonníka alebo ďalší pokus o účinnú ochranu práv veriteľov) [2017] Yearbook of Slovak-Austrian Commercial Chamber (Ročenka Slovensko-Rakúskej obchodnej komory) 99

[40] J. Čenteš, '*Penal code - Commentary*' (Trestný zákon. Veľký komentár) (4th edn. Eurokódex 2018) 538-540

frauds".[41] Šanta adds that they are primarily *"people [who come from] asocial background, who for a negligible amount of money of their approximate amount of few hundred euros, acting on the directions of another person, often on the edge of criminal liability (commonly however unintentionally) perform only one or more illegal acts (e.g. transfer of shares in a private limited liability company on themselves, signing of documents, withdrawal of cash and realisation of bank transfers, transfer of shares to another person, etcetera)."* [42] Based on what has been stated, we can synthetize that a "straw man" is a person who, for a remuneration and/or alternatively under duress provides and borrows its identity for conducting an illegal economic activity, for the purposes of covering the real perpetrator, or alternatively a people who are gaining an advantage from such activity.

In the context of an actual transfer of shares, whether it is a sole partner in a company or it is a transfer of numerous parts of shares within one company, those are usually transferred to a one acquirer – a straw man, who becomes the sole partner and also a statutory organ of a company. The transfer of 100% of shares of a company to a one partner is naturally the most common form of transfer, primarily from the perspective of the transfer itself (seeking for a straw man), and from the economic perspective (remuneration for a straw man), and also from the perspective of actual managing of a company – a company takes its decision based on a decision of a sole partner, and there is no need to convene a shareholder meeting as it would be the case with more than one partner in a company.

Despite the fact that a person acting as a straw man is often an insolvent and homeless person, in practice we often come across a situation in which a straw man is a person from abroad, which complicates the successful investigation and subsequent penalization of those persons as they are difficult to track down.

Moreover, based on the current legal framework of the Slovak Republic, an entry of an appointment of a new statutory organ in a Business registry has only a declaratory nature.[43] Such legal framework may be abused in an unfair liquidation of a company, when an entry in a business registry shows earlier date of appointment of such person as a statutory organ

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[41] A. Heretik, '*Herd of white horses – an attempt for forensic-psychological analyses of a marginalized group*' (Stádo bielých koní – pokus o forenzne psychologickú analýzu marginalizovanej skupiny) [2010] 106 Czech and Slovak psychiatry (Česká a slovenská psychiatrie) 318, 320

[42] J. Šanta, '*Criminal liability of tax advisor*' (Trestná zodpovednosť daňového poradcu) [2015] 67 Justice Revue (Justičná revue) 518, 525

[43] T. Čentík, '*The Business registry and few "problematic" questions*' (Obchodný register a zopár „problémových otázok") [2017] Ulpianus <http://www.ulpianus.sk/blog/obchodny-register-a-zopar-problemovych-otazok/> accessed 15 May 2019

compared to a date on which a decision of its appointment was taken by a partner in a company. This argument is supported by the Decision of District Court Bratislava I issued on 06.06.2014, in which the Court stated following: *"A statutory organ of a company is appointed and called off by a shareholder meeting and an entry in a Business registry in that matter has only a declaratory nature, as the function of a statutory organ is established on a date of the decision at the meeting of shareholders [...] the authenticity of a signature of one of the partners on such decision shall be authorized by a notary. The date of the authorization of a signature however, is not a date of the decision of the partner or of a meeting of a shareholders, as decision of a partner or partners is not a legal act which requires a signature to be authorized by a notary, this is of a different legal fact. The mentioned authorization of a signature of the sole partner is a procedural requirement and shall be used only to verify a person that has taken such decision and as such support the fact that such decision was taken by the authorized person."*[44] Pursuant to this decision, the law allows for the decision of a sole partner to be anti-dated, and as such offers the former statutory organ the possibility of circumventing the criminal liability for a criminal offence of obstructing of insolvency proceeding and also any commercial-law liability i.e. disqualification of a statutory organ.

We shall illustrate this statement on the following example:

The sole partner of the company, which is as of 12.07.2018 *de facto* insolvent, with an intention to obliviate him from the criminal liability for obstructing of insolvency proceeding decides on 12.11.2018 to change a statutory organ of the company as of 12.06.2018. The sole partner creates a decision of a sole partner of the company on such change in statutory organ, in which he sets as a date of a decision 12.06.2018 and within the meaning of Art. 125 par. 1 letter f) in conjunction with Art. 132 par. 1 Commercial Code[45] he authorizes his signature on the decision on 12.11.2018. Subsequently the sole partner submits a proposal for an entry of the subjected change in the Business registry. Within the meaning of the above-mentioned Decision, regardless of the date of the authorization of a signature on the decision, the new statutory organ of a company will be appointed as of 12.06.2018.

[44] Case *Lactalis Slovakia, s. r. o.*, decision of the District Court Bratislava I issued on 06.06.2014, ref. no. 34Nsre/59/2014 ECLI:SK:OSBA1:2014:1114908965.1

[45] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Articles 125(1)(f) and 132(1)

Currently, the only limiting factor for such action, besides the newly introduced criminal offence of unfair liquidation, is a competence of a registry court to impose a fine up to 3.310, - EUR due to failure to comply with a requirement to notify the court on any decision of the sole partner within 30 days from the date of such decision. However, such fine is pursuant to Art. 11 par. 1 letter a) Act on Business Registry imposed to a new statutory organ[46] – a straw man, which makes the fine imposed ultimately irrecoverable. Moreover, such fines are imposed rarely in practice.

2.2 Unfair liquidation by unfair M&A (merger, acquisition)

We often come across an unfair or "*de facto* liquidation" of a company via "services" of a straw man by means of unfair merger or acquisition.

The problematic of merger and acquisition is generally administered by Art. 69 and 69a Commercial Code[47], whilst a specific for each legal form of a company merger is described in dedicated part of Commercial Code. In a case of a private limited liability company, mergers and acquisitions are administered by Article 152a Commercial Code[48], with Articles 218a to 218k Commercial Code on merger and acquisition of joint-stock company used accordingly.[49]

Acquisition of a company may be defined as *"process, in which, based on a winding up of a company without liquidation a company is wound-up whilst the capital of the wound-up company is transferred to the already existing company, which by the virtue of such transfer becomes the legal successor of a wound-up company."*[50]

Example:

Company A		**Company B**		**Company A**
(one who takes	+	(wound-up, which	=	(Company A with
over the capital)		capital is transferred)		Company B)

[46] Act No. 530/2003 Coll. on Business Registry (Zákon o obchodnom registry) [2019] Slovak Republic Article 11(1)(a)
[47] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Articles 69 and 69a
[48] ibid. Article 152a
[49] ibid. Articles 218a-218k
[50] V. Keletová, *'Mergers, acquisitions and divisions of companies'* (Zlúčenie, splynutie, rozdelenie obchodných spoločností) [2007] 15 Tax and Accounting advisor of the businessman (Daňový a účtovný poradca podnikateľa) 58, 62

*“**Merger** is a process, in which based on a winding up of a company without liquidation one or more companies are wound-up, whilst the capital of the wound-up company/companies is transferred to a newly incorporated company, which by virtue of such transfer becomes the legal successor of a wound-up company/companies.”*[51]

Example:

Company A		**Company B**		**Company C**
(company wound-up without liquidation)	+	(company wound-up without liquidation)	=	(newly incorporated company)

Based on the above-mentioned definitions we can observe the main differences between the two forms of transfers in the company. Whereas in a case of acquisition of a company, one or more companies are wound-up without liquidation and their capital is by the date of their liquidation transferred to the already existing company, on the other hand, the result of a merger is a newly incorporated company, to which a capital of wound-up companies is transferred.

When it comes to a process of actual unfair acquisition, at the beginning of the process is a company which is insolvent, and such insolvency may not only be the result of objective economic causes such as secondary insolvency (insolvency caused by a default of business partners/customers).[52] The insolvency, as is often a case in unfair liquidation, is the result of intentional circumvention of commitments for the purposes of maximalization of profit from the company to the partner of the company. Instead of legal forms of winding up of such company via either winding up with liquidation (if the capital-debt ratio of the company is higher than 1) or via the declaration of bankruptcy, in which at least a partial repayment of creditors’ claims is possible, the partners decides for winding up of the company without

[51] V. Keletová, *‘Mergers, acquisitions and divisions of companies’* (Zlúčenie, splynutie, rozdelenie obchodných spoločností) [2007] 15 15 Tax and Accounting advisor of the businessman (Daňový a účtovný poradca podnikateľa) 58, 63

[52] H. Majdúchová, *‘The insolvency of construction companies in Slovakia and the possibilities of its solution*’(Platobná neschopnosť podnikov stavebníctva v SR a možnosti jej riešenia) [2013] (Economic University in Bratislava, Faculty of company management)

liquidation vie legal successor – a company with a straw-man as a sole partner and statutory organ. One of the main motives of such action is a fact, that the business activities of insolvent company had often signs of economic criminal activity.

Despite the fact, that the new company is a universal legal successor, meaning that all of the right and obligations of the company that is wound-up without liquidation are transferred *ex lege* to the new company, any recovery of claims against such company is practically impossible. The main factor for nonrecovery of claims is that in a text of merger agreement or acquisition agreement, the partners of the company that will be wound-up without liquidation may decide, that some or all of them would not become the new partners in a legal successor.[53] Moreover, a legal successor is, in a case of merger, a newly incorporated company, without any real capital (initial capital is often not paid up) and a straw man as the sole partner and the sole statutory organ of such company.

The stated nonrecovery of claims is often "strengthen" by a "chain of mergers" of companies, i.e. the companies are repeatedly merged, with the last link of the chain being either a company in which the sole partner and the sole statutory organ is a straw-man, or such company transfer 100% of its shares to a straw-man (so-called "multi-mergers").[54]

The unfair liquidations of companies are also realized on multi-national level via cross-border mergers and acquisitions. A cross-border merger is defined as process, in which two companies with their seats in different jurisdictions are merged.[55] The promulgation of the Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies (hereafter as "Cross-border Merger Directive")[56], amended and subsequently repealed by the Directive 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law[57], facilitated the process of cross-border mergers within the EU.[58] The Cross-border Merger Directive has been implemented in the Slovak legal order via Article 69aa

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[53] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 69(8)
[54] Š. Bröstl, *'Amendment to the Commercial Code: Mergers (acquisition, division) of companies'*(Novela Obchodného zákonníka: Zlúčenie (splynutie, rozdelenie) obchodných spoločností) [2017] Ulpianus <http://www.ulpianus.sk/legislativa/novela-obchodneho-zakonnika-1.-zlucenie-splynutie-rozdelenie-obchodnych-spolocnosti/> accessed 21 May 2019
[55] Supra note 54 Article 69aa(1)
[56] Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies, [2005] OJ L310/1
[57] Directive 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law [2017] OJ L169/46
[58] T. Biermeyer, M. Meyer, *'Corporate Mobility in Europe: An Empirical Perspective'* [2018] 15 European Company Law 64, 65

Commercial Code and is only applied to a cross-border mergers of companies with their registered seats within EU and countries of EEA.[59] The Cross-border Merger Directive has liberalised the process of cross-border mergers. Prior to its promulgation, some of the member states had not even allowed for cross-border mergers (see ECJ case Sevic C-411/03).[60] The liberalisation brought by the Cross-border Merger Directive, however, allows also for unfair merger and acquisition that worsens the position of the creditors vis-à-vis the insolvent company.

2.3 Commercial aspects of an unfair liquidation

One of the main pillars that regulate the commitments arising out of commercial law are basic principles, that are the expressions of basic values which serve as the foundation for the commercial contract law.[61] Among those basic principles for the commitments arising out of commercial law is the principle of *pacta sunt servanda*, which is an expression of legislators' interest for fulfilment of commitments, in which a breach to a contract is viewed as a breach to the law.[62] Another basic principles are, *inter alia*, principle of good manners, and principle of fair dealing that serves as guarantees of morality, i.e. type of behaviour that is accepted by society.[63] Those abovementioned key principle of commercial law are most frequently breached in the unfair liquidation.

Whether it is a liquidation of a company without liquidation via merger or via acquisition, both of those action are based on *ex lege* transfer of commitments and as such, in legal terms it is not a change in commitment, *ergo* approvals of the creditors are not required.[64] The same applies to transfer of shares in a company to a straw, as there is no change of the commitment, as the debtor remains the same person. The debtor (company) remains the same, the change only happens in the persons acting as a partner in the company and a statutory organ of the company. Stemming from that, a debtor – in our case the

[59] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 69aa
[60] Case 411/03 SEVIC Systems AG [2005] ECR I-10825
[61] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 33-34
[62] B. Lurger, '*The Future of European Contract Law between Freedom of Contract, Social Justice, and Market Rationality*' [2005] 1 European Review of Contract Law 4, 442, 452
[63] O. Lando, H. Beale, '*Principles of European Contract Law: Parts I and II*' (1st edn. Kluwer Law International 2000) 115
[64] Act No. 40/1964 Coll. Civil Code (Občianský zákonník) [2019] Slovak Republic Article 531(1)

company, that is unfairly liquidated, is able to without any notification to its creditors weaken the recoverability of creditors' claims or in certain cases render such recovery impossible, as the debtor is now a company whose sole partner and a statutory organ is a straw man. It is a creditor who is the most harmed party in the unfair liquidation as they are often left with nonrecoverable claims.

For the purposes of better comprehension and portrayal of the impact of unfair liquidation on the creditors, we divide the creditors and their claims respectively in two categories:

1) claims arising out of commercial contracts – e.g. agreement on sale of goods, build contracts, etcetera[65];

2) state's claims arising out of tax obligations, payroll transfers to social and health insurance, etcetera;[66]

2.4 Overview

This chapter was dedicated to analyses of the actual process of unfair liquidation and its subsequent practical implications on the creditors and their respective claims. The unfair liquidation is conducted in two different forms. The first form consists of transfer of shares to a contactless person – straw man, with simultaneous appointment of such person as a statutory organ of the company. The second form is realized via merger or acquisition of the unfairly liquidated company with another company result of which is the legal successor who takes over debts and liabilities of the company that is unfairly liquidated. Furthermore, the sole partner and the statutory organ in the legal successor is a contactless straw-man.

The resulting unfair liquidation of the company has variety of negative aspect ranging from criminal liability of people engaged in unfair liquidation up to economic aspects such as non- recoverability of claims of the creditors of the unfairly liquidated company. The

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[65] R. Šlosár, A. Šlosárová, '*Balance-sheet accounting for companies*' (Podvojné účtovníctvo pre podnikateľov)(1st edn. Bratislava:Ekonómia 2005)
[66] Z. Švecová, '*Receivables*'(Pohľadávky), [2016] 10 Taxes and Accounting (Dane a účtovníctvo) 35, 38

main creditors that are affected by the unfair liquidation may be distinguished into two broad categories based on the types of their claims against unfairly liquidated company. The first category is made up by business partners who had entered into economic and legal relations with the company prior to its unfair liquidation. The second category represent state authorities who may have variety of claims against the unfairly liquidated company such as claims arising out of existing tax arrears, penalties, fines, etcetera.

In the following chapter we assess the legal instruments available to the creditors pursuant to Slovak legal order, based on their previous differentiation. The particular focus shall lie on the forms of the recovery of their claims.

3 Current legal framework of the Slovak Republic in protection of creditors vs. Piercing the corporate veil

The chapter discusses and analyses different legal forms of creditors' claim recovery based on their differentiation in the previous chapter. The first part analyses the specific forms of recovery of claims within the meaning of Commercial Code. The second part discusses the latest amendment of the Commercial Code aimed against the unfair liquidation. The third part then subsequently introduces the doctrine of piercing the corporate veil in general and compares it to the instruments available to the creditors in Slovak legal order.

3.1 Instruments for protection of creditors

The claims arising out of commercial contracts are most commonly based on the vendor-client relationships to which company enters in the process of conducting its business activity. It is the most frequent form of receivable/claim, as the business activity is often based on such commitments.[67]

In the case of a solvent company that has non-fulfilled claim against its creditor, the creditor may bring a case to the court for repayment of the receivable, and subsequently enforce the decision of the court via bailiff.[68] Moreover, the creditor is authorized to submit a proposal for declaration of bankruptcy of the debtor, provided that legal procedural and material criteria are met.[69] Mentioned forms of protection of creditor however become useless in a case of unfairly liquidated company. Despite the fact that the creditor successfully claims its right at the court whether it is a money decree or execution order or declaration of bankruptcy, the unfairly liquidated company does no longer have any assets. Moreover, the sole partner of the company and also its statutory organ is a person who is impossible to reach – a straw man. In such cases there is a possibility of criminal

[67] R. Šlosár, A. Šlosárová, '*Balance-sheet accounting for companies*' (Podvojné účtovníctvo pre podnikateľov)(1st edn. Bratislava:Ekonómia 2005)
[68] M. Buznová, M. Magyar, '*Act on consumer loans and its applicability in practice in the field of assignment of claims out of consumer loans*' (Zákon o spotrebiteľských úveroch a jeho aplikačná prax v oblasti postupovania pohľadávok zo spotrebiteľských úverov) [2016] 24 Regulation of financial market (Regulácia finančého trhu) 5, 30, 32
[69] M. Ďurica, J. Husár, '*A guide to insolvency law*' (Sprievodca konkurzným právom) (1st edn. Ministry of Justice of the Slovak Republic 2008) 13

repercussions of the former partner, i.e. the partner who transferred the shares to a straw-man and caused the insolvency of the debtor, in form of charging that person with criminal offence of obstructing insolvency proceedings,[70] harm done to a creditor,[71] fraud[72], tax and insurance evasion[73], and currently also a criminal offence of unfair liquidation[74]. Although by means of criminal repercussion the state exercises the general prevention from such actions, however, the criminal liability (save for the exception, e.g. seizure of the assets) does not satisfy the creditors' claims. We are of the view, that even the commercial law should provide norms, based on which it would be possible to held liable a person who transfers his shares for the purposes of unfair liquidation.

The said liability in commercial law would be presumably possible, if (1) the creditor could successfully contest the validity of the agreement on transfer of shares, and simultaneously (2) the liability of a partner in the company for the debts of the company would be extended, if it was proven that in the process of managing the company such partner did not proceed with professional care.

Regarding the contesting of the validity of the agreement on transfer of shares it is important to state that pursuant to Article 137 par. c) Civil Procedure Regulation[75] it is action of determination, that a person with imperative legal interest may file. The Supreme Court of the Slovak Republic in its decision states, that the imperative legal interest must *"[...] be imperative within the meaning that the plaintiff in the subjected legal relationship may with the proposed determination achieve the abolition of ambiguity and protection of its rights and legitimate interest."*[76] In other judgment the Supreme Court of the Slovak Republic states that *"the imperative legal interest for determination is present when there is an actual case of objective legal uncertainty between the plaintiff and the defender, that endangers the plaintiffs' legal position and that may be abolished via this legal instrument [...] regardless of the source of such uncertainty."*[77] Stemming from the stated interpretation of the term "imperative legal interest" it may be concluded that in the context of transfer of shares to a straw-man there is a situation in which the creditor enters in legal uncertainty, as he cannot

[70] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 242
[71] ibid. Article 239
[72] ibid. Article 221
[73] ibid. Article 276
[74] ibid. Article 251b
[75] Act No. 160/2015 Coll. Civil Procedure Regulation (Civilný sporový poriadok) [2019] Slovak Republic Article 137(c)
[76] Decision of the Supreme Court of the Slovak Republic issued on 16.11.2017, ref. no. 3Cdo/197/2016
[77] Judgement of the Supreme Court of the Slovak Republic issued on 26.03.2013, ref. no. 4Obo/79/2011

claim its rights, and also, that with the determination of invalidity of the agreement on transfer of shares it would be possible to achieve the protection of creditors' rights.

Based on the above-mentioned we are of the view, that in such cases there would be imperative legal interest on the side of the creditor on determination of invalidity of the agreement on transfer of shares, ergo the creditor would have active legitimation for submitting the claim on contesting the validity of the said agreement.

Regarding the actual reasons for invalidity of agreement on transfer of shares, one can operate with qualifying the action of the former partner of transferring the shares of the company to a straw man either in accordance with Article 256 Commercial Code[78], i.e. exercise of rights that is in conflict with principles of fair dealing or in accordance with Article 39 Civil Code administering the absolute invalidity of legal act, which content or aim conflicts the law, circumvents it or is against the good manner, which could be used as *lex generalis* in the presented case.[79] The two terms fair dealing, and good manners cannot be used interchangeably. The term fair dealing is a term with narrower content than term good manners. Their effect is also significantly different. Whereas the action in conflict with good manners establishes the absolute invalidity of legal act[80], the exercise of right in conflict with principle of fair dealing is "only" legally unprotected[81] and, as such, based on such action it would be impossible to render the agreement on transfer of shares invalid.[82]

The Constitutional Court in its finding states that *"[the] principles of fair dealing are the expression of concretization of general moral principles [...] it is a concretization of norm of moral in the field of application of specific social relations, of which [parts] are commercial contract relations."*[83] The two institutes are, however, interestingly differentiated by the Supreme Court of the Czech Republic, which in one of its decision states, that *"in conflict with the principles of fair dealing may only be the exercise of rights*

[78] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 256
[79] Act No. 40/1964 Coll. Civil Code (Občiansky zákonník) [2019] Slovak Republic Article 39
[80] L. Žitňanská, O. Ovečková, et. al., 'Commercial law, companies'(Obchodné právo, obchodné spoločnosti) (2nd edn. IURIS LIBRI 2013) 28-30
[81] M. Patakyová, et. al., 'Commercial Code, Commentary' (Obchodný zákonník, Komentár) (3rd edn. C.H. Beck 2010) 753
[82] P. Kubíček, et. al, '*Commercial Law*' (Obchodné právo) (1st edn. Vydavatelství a nakladatelství Aleš Čeněk s. r. o. 2016) 222
[83] Decision of the Constitutional Court of the Slovak Republic issued on 09.06.2010, ref. no. I. ÚS 221/2010

not the legal act itself […] it is the presumption of application of Article 265 Commercial Code the valid legal act, and from such legal act the right is claimed."[84]

Based on the difference defined by the Supreme Court of the Czech Republic between the terms "fair dealing" and "good manners" a conclusion may be drawn, that whereas the agreement on transfer of shares to a straw man is a legal act, and simultaneously it is a form of circumvention of obligations arising out of specific statutes, by virtue of which the harm is done to the creditors, it is an act in conflict with good manners. Stemming from that, we are of the view that the said action of the partner (transfer of shares) falls within the application ambit of Article 39 Civil Code.[85] The stated argument is based on the judgment of the Regional Court Košice, that has also adjudicated the validity of agreement on transfer of shares in the context of its conformity with good manners within the meaning of Article 39 Civil Code.[86]

Regarding the actual probation of incompatibility of the act of the partner with good manners, this would be in every case attested individually, based on the concrete circumstances of each case.[87] Should the court based on the probation of evidence come to the conclusion, that the agreement on transfer of shares, upon which the former partner had transferred the shares to the straw-man, is in conflict with good manner, and such legal act is pursuant to Article 39 Civil Code rendered absolutely invalid *ex tunc,* the former partner is then reintroduced back as to the position of partner.[88]

With the court's decision on invalidity of agreement on transfer of shares a gap for the application of newly introduced Article 66aa Commercial Code appears.[89] This Article administers the liability of controlling person for a harm that is done to the creditors of the controlled person, if the actions of the controlling person contributed to the insolvency of the controlled person. The term, controlled person, could be understood as *"a person, in which a specific person holds majority of voting rights.*"[90] Stemming from the stated

[84] Decision of the Supreme Court of the Czech Republic issued on 07.12.2011, ref. no. 32 Cdo 542/2010
[85] Act No. 40/1964 Coll. Civil Code (Občianský zákonník) [2019] Slovak Republic Article 39
[86] Judgment of the Regional Court Košice issued on 09.03.2017, ref. no. 9Co/328/2016
[87] Judgment of the Supreme Court of the Slovak Republic issued on 26.03.2013, ref. no. 4 Obo/44/2012
[88] J. Lazar, et. al., '*Civil law – substantive part, 1st volume*' (Občianské právo hmotné 1. zväzok) (2nd edn. IURIS LIBRI 2014) 130
[89] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 66aa(1)
[90] ibid. Article 66aa

definition, the controlling person could be a natural person in the position of the partner of the company.[91]

Pursuant to Article 66aa Commercial Code the partners in the company are obliged to adhere *"[to] corporate loyalty and, cannot abuse their position in the company and shall be liable for the harm occurred due to their behaviour, mainly in the regime of general liability for harm (primarily the liability for harm done by intentional action against good manners pursuant to Civil Code)."*[92] The consequence of introduction of Article 66aa Commercial Code is that the loyalty principle is for the first time explicitly applied on the action of the partner in the Slovak legal order. Prior to introduction of Article 66aa Commercial Code, the loyalty principle was explicitly applied to the action of statutory organ, whilst the obligations and liabilities of the partners were narrower concept.[93] The loyalty obligation regarding the partners in the company was not explicitly stated. Such obligation could have only been deduced by extensive interpretation of Commercial Code (e.g. Article 56 Commercial Code).[94]

According to the newly amended legal framework a partner in the company may be held liable for the harm to the creditors as a result of insolvency of the company, if the partner *"[with his actions] significantly contributed to the insolvency of the controlled person."*[95] whilst his actions does not need to be the main or even the only cause of insolvency.[96] Pursuant to the explanatory memorandum to the amendment of Commercial Code, such action may consist in any binding or non-binding instruction to the statutory organ.[97] The partner will not however be held liable for any incorrect business decision.

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[91] Š. Bröstl, *'Amendment to the Commercial Code: Mergers (acquisition, division) of companies'*(Novela Obchodného zákonníka: Zlúčenie (splynutie, rozdelenie) obchodných spoločností) [2017] Ulpianus <http://www.ulpianus.sk/legislativa/novela-obchodneho-zakonnika-1.-zlucenie-splynutie-rozdelenie-obchodnych-spolocnosti/> accessed 21 May 2019

[92] National Parliament of the Slovak Republic, '*Explanatory memorandum to Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes*' (Dôvodová správa k zákonu č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Publishing department of the National Parliament of the Slovak Republic, p. 21

[93] ibid. p. 21

[94] University of Pavol Jozef Šafarik in Košice, 'Legal position of a partner in the company' (Právne postavenie spoločníka v obchodnej spoločnosti) [2017] 1 Directory of Articles from IV. study symposium on company law (Zborník príspevkov zo IV. študentského sympózia z práva obchodných spoločností) 77, 78

[95] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 66aa(1)

[96] Supra note 93, p. 22

[97] ibid. p. 22

For the partner to be held liable a proof of intentional action of the partner to the assets of the company would be needed.[98] Simultaneously, the law allows for release of partner from liability it its shown that the partner *"proceeded on an informed basis, in good faith, and that he acted for the benefit of the controlled person"*, with the burden of proof being on the partner.[99]

Stemming from that, we can draw a following conclusion: should the court rule on the invalidity of the agreement on transfer of shares by virtue of conflict of the said legal action of the former partner with good manner in conjunction with Article 66aa Commercial Code, the result could lead in the liability of the former partner for the harm done to the creditors. On the other hand, it is important to note that this would not be a matter of short time. Also, the invalidity of the agreement on transfer of shares in itself would need to be adjudicated in light with protection of property rights and the right to dispose with one's property, as shares are within the meaning of Commercial Code considered other form of property.

It is important to state that the application of such steps is currently only a theory, and although there have been decisions of the Slovak courts on invalidity of the agreement on transfer of shares, none of them were taken in the cases regarding unfair liquidation and the subsequent liability of the partner within the meaning of Article 66aa Commercial Code.[100] Hypothetically, the possibility to rule out validity of the agreement on transfer of shares could be used also to determine the validity of either merger agreement or acquisition agreement *mutatis mutandis*. However, the amendment to the Commercial Code introduced the new methods of tackling the infamous forms of unfair mergers and acquisitions, which shall be analysed in the following part.[101]

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[98] [98] Š. Bröstl, *'Amendment to the Commercial Code: Mergers (acquisition, division) of companies'*(Novela Obchodného zákonníka: Zlúčenie (splynutie, rozdelenie) obchodných spoločností) [2017] Ulpianus <http://www.ulpianus.sk/legislativa/novela-obchodneho-zakonnika-1.-zlucenie-splynutie-rozdelenie-obchodnych-spolocnosti/> accessed 21 May 2019

[99] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 66aa(1)

[100] ibid. Article 66aa

[101] Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes (Zákon č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Slovak Republic

3.2 Amendment to the Commercial Code

On 12.10.2017 the Slovak National Council promulgated Act no. 264/2017 Coll. by which it significantly amended Commercial Code.[102] The aim of the amendment could be described as three-fold. The first aim is to tackle unfair liquidation via transfer of shares to a straw man, the second aim is to tackle unfair liquidation via unfair merger or acquisition and the third aim is the extension of liability of statutory organs of the company. This subchapter analyses each of the aims based on their specific instruments, with the particular importance being placed on the practical implications of each instrument.

3.2.1 Instruments against unfair liquidation via transfer of shares

The main instrument chosen by the legislator to tackle the unfair liquidation via transfer of shares is the introduction of a criminal offence of unfair liquidation to the Slovak' Penal Code. As mentioned early, the newly introduced criminal offence operates on three planes, it penalizes people who mediate, act as or transfer their shares to a straw man.[103] Based on the legal wording of the criminal offence of unfair liquidation, there are several shortcomings than may render the application of this *prima facie* effective instrument challenging.

At first, it is the problematic notion of definition of a straw-man. The Penal Code does not use the term straw-man itself, instead it uses the term: *"a person, who only borrows his first name and surname and its identity for the purposes of overtaking rights and obligations of which it has no genuine interest to act upon*"[104], however, the commentary to the Penal Code uses the term straw-man.[105] Despite the fact that term itself has its defined meaning, it is possible that the practical usage of this term and eventual labelling of the

[102] Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes (Zákon č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Slovak Republic

[103] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251b

[104] ibid. Article 251a

[105] J. Čenteš, '*Penal Code, Commentary*' (Tresný zákon. Veľký komentár) (4th edn. Eurokódex 2018) 538-540

person as a straw-man may be difficult to prove. We are of the view that the "genuine interest to act upon [overtaken rights and obligations]" would be rather challenging to prove.

At second, as we already mentioned in Chapter 2, another shortcoming of the newly introduced criminal offence of unfair liquidation is the limited scope of application of the criminal offence. It stems from the wording of the criminal offence of unfair liquidation, that the said criminal offence only encompasses actions regarding transfer of shares and does not apply to the unfair mergers or acquisitions.[106] Our argument is further supported by the commentary to the Penal Code which states that in the cases concerning private limited liability companies the transfer in control over the company is predominantly realized via transfer of shares.[107] However, the term unfair liquidation is on the same page of the commentary defined as *"action, that de facto aims at the termination of control of certain person over the company, however, such termination is realized by unwanted manner [...] it does not concern acts, which could be interpreted as act done in legal winding up of a company.*"[108] As we stated early, action by which a proper winding up of a company is circumvented is not only realized via transfer of shares. The unfair liquidation is also done via unfair merger or via unfair acquisition. Stemming from that, it is baffling why the legislator does not tackle also other forms of unfair liquidation in within the scope of criminal offence of unfair liquidation. In the commentary to the Penal Code prof. Čenteš, mentions that in the case of the private limited liability company is "predominantly" transfer of shares as a form of unfair liquidation, he does not elaborate his interpretation to other examples of unfair liquidation.[109]

At third, in connection with the scope of application of the criminal offence of unfair liquidation is important to refer to the fact that the said criminal offence does not apply to all persons mediating a transfer to a straw-man. As Šamko states, it is not clear why with the amendment of the Penal code the legislator also did not extended the criminal liability also to a legal person, as it is often the case that such transfer is mediated via legal person in the scope of their business activity.[110] The result of the lack of extended liability of legal person is the fact, that those legal persons may continue to mediate the transfer of shares to a straw-

[106] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251
[107] J. Čenteš, '*Penal Code, Commentary*' (Tresný zákon. Veľký komentár) (4th edn. Eurokódex 2018) 539
[108] ibid. 539
[109] ibid. 539
[110] P. Šamko, '*The proposal for the introduction of the new criminal offence of unfair liquidation and amendments to the obstructing of insolvency proceedings*' (Návrh na zavedenie nového trestného činu nekalej likvidácia a zmeny v marení konkurzného konania) [2017] 04 Legal letter (Právne listy), 10, 12

man without any criminal liability, by virtue of which the newly introduced criminal offence is partially ineffective.

Furthermore, it is important to state, that whilst the introduction of a new criminal offence is a step forward towards tackling unfair liquidation, it is still only preventive instrument that either deter the prospective perpetrators or imposes a penalty on the perpetrator. It does not however tackle the commercial aspect of unfair liquidation – financial harm done to the creditors. Moreover, the scope of the application and the wording of the newly introduced criminal offence of unfair liquidation may prove the application in practice difficult, due to the nature of the criminal offence – intentional criminal offence, and as such, intention to either obliviate the obligations or intentions act as a straw-man may be difficult to prove.

Lastly, as many experts on criminal law in Slovak Republic has repeatedly stated, even prior to the introduction of the criminal offence of unfair liquidation, the Slovak Penal Code offered other forms of criminal repercussion for unfair liquidation such as criminal offences of tax and insurance evasions, obstructing bankruptcy proceedings, or other economic criminal offences.[111] As such, the criminal offence of unfair liquidation may seem redundant and may not even fulfil one of the basic principles of criminal law – *ultima ratio*.[112]

3.2.2 Instruments against unfair liquidation via unfair merger or acquisition

The processes of merger and acquisition were significantly restricted to provide better protection against unfair merger and liquidation. The wording of Article 69 Commercial Code that administers the winding up of a company without liquidation was extended by five new paragraphs, whose aim is *"enhancement of protection of creditors' right and rights of the partners in companies engaged in merger, acquisition or dissolvement of companies and the prevention of illegal practices in those mergers, acquisitions and*

[111] P. Šamko, '*The proposal for the introduction of the new criminal offence of unfair liquidation and amendments to the obstructing of insolvency proceedings*' (Návrh na zavedenie nového trestného činu nekalej likvidácia a zmeny v marení konkurzného konania) [2017] 04 Legal letter (Právne listy), 10, 12

[112] J. Strémy, '*Quo vadis liquidation of the company*' (Quo vadis likvidácia obchodnej spoločnosti) in '*Mutations and innovations of concept of capital companies in conditions of globalization*' (Premeny a inovácie konceptu kapitálových spoločností v podmienkach globalizácie) (1st edn. Comenius University in Bratislava 2017) 3

dissolvements [realized] with the aim of obliviating obligations in winding up of a company or in insolvency proceedings."[113] The stated aim shall be fulfilled via introduction of following conditions imposed on mergers/acquisitions of companies:

i. the capital-debt ratio of the legal successor must be higher than 1;[114]
ii. wound-up company and/or its legal successor shall not be in liquidation;[115]
iii. wound-up company and/or its legal successor shall not be in bankruptcy or restructuring;[116]
iv. wound-up company and/or its legal successor cannot be in proceedings regarding its winding-up;[117]
v. if the company does not fulfil the criteria mentioned in points i – v its organs shall not proceed with either merger or acquisition, under the threat of liability for harm done to the creditors due to breach of this condition;[118]
vi. the company shall notify the tax authority that the agreement on merger/acquisition has been drafted 60 days prior to the meeting of the shareholders that shall vote on the proposed merger/acquisition;[119]
vii. after the shareholders'[120]' approval of agreement on merger/acquisition a report of the auditor shall be made to authorize the company's compliance with point i.;[121]
viii. condition to set the decisive day from which the action of companies shall be considered as the action of the legal successor (from the economic perspective).

[113] National Parliament of the Slovak Republic, '*Explanatory memorandum to Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes*' (Dôvodová správa k zákonu č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Publishing department of the National Parliament of the Slovak Republic, p. 24
[114] Act No. 513/1991 Commercial Code (Obchodný zákonník) [2019] Slovak Republic Article 69(11)
[115] ibid. Article 69(12)
[116] ibid. Article 69(12)
[117] ibid. Article 69(12)
[118] ibid. Article 69(13)
[119] ibid. Article 69(13)
[120] ibid. Article 69(14)
[121] ibid. Article 69(14)

Commentary to points i. – iv.

Within the meaning of the explanatory memorandum to the amendment, the promulgated conditions shall secure that the legal successor is in "good condition".[122] We are of the view that the selected provisions are directly aimed at the protection of creditors as the legal successor *ex lege* overtakes the commitments of the wound-up company. Moreover, application of those conditions does not preclude economically motivated merger/acquisition, as company with capital-debt ratio below 1 may be merged/acquired provided that its legal successor will have capital-debt ratio higher than 1.

Commentary to point v.

The stated condition primarily protects the creditors by granting them damages for the harm in the case that organ of the company take steps leading to merger/acquisition despite the nonfulfillment of legally prescribed conditions.[123] In our view, the stated condition has also a secondary function – preventive as it deters organs of the company to proceed with such steps, under specific circumstances.

Commentary to point vi.

The aim of this provision is the effort of the state to stop those mergers/acquisitions that resemble signs of fiction, or mergers/acquisitions without real meaning. The tax authority shall probate the agreement on merger/acquisition.[124] The introduction of this condition prolongs the process of merger/acquisition, as the draft of the agreement on merger/acquisition must be delivered to the tax authority at least 60 days before its approval on the meeting of shareholders.

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[122] National Parliament of the Slovak Republic, '*Explanatory memorandum to Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes*' (Dôvodová správa k zákonu č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Publishing department of the National Parliament of the Slovak Republic, p. 24

[123] J. Beracka, '*New interference in merging of the companies and their regulation is a reality*' (Nový zásah do zlučovania obchodných spoločností a ich pravidiel je realitou) [2018] 4 Tax and Accounting advisor of the businessman (Daňový a účtovný poradca podnikateľa) 25, 28

[124] ibid. 28

Commentary to point vii.

The auditor, in this case, fulfils the function of controller, and as such shall attest whether the conditions for realization of merger/acquisition are met.[125] The specific auditor that prepares such report is chosen by parties engaged in merger/acquisition. This form of party autonomy could theoretically lead in to picking of the auditor that would be "willing to cover" the non-fulfilment of conditions needed for merger/acquisition. The auditor, however, is in the case of tempering with financial and economic information about the companies exposed to recourses in form of licence withdrawal and also risk of damage to his reputation.[126]

Commentary to point viii.

The obligation of setting the decisive date of the merger/acquisition was promulgated primarily with the aim of increasing the financial transparency of merger/acquisition of the companies.[127]

The newly introduced instrument tackling the realization of unfair mergers/acquisitions are viewed as effective, as from the date of effect of the said instruments there has been a significant decline in number of mergers/acquisitions, which has also been confirmed by the court clerk working at the Business registry court in Nitra. The question remains, whether these rigid limitations do not also impede legitimate mergers/acquisition, i.e. whether they do not impose unnecessary administrative/legal/economic burden on the companies.

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[125] J. Čarnogurský, '*Amendment to the Commercial Code*' (Novela obchodného zákonníka) [2018] 18 Pro Bono 3, 4

[126] L. Hmírová, '*The approved amendmendts to the Commercial Code, Penal Code and other statutes effective from 01. January 2018'* (Schválené zmeny Obchodného zákonníka, Trestného zákona a iných predpisov k 1. januáru 2018) [2017] 3 Personal and wage advisor for the businessman (Personálny a mzdový poradca podnikateľa) 12, 15

[127] National Parliament of the Slovak Republic, '*Explanatory memorandum to Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes*' (Dôvodová správa k zákonu č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Publishing department of the National Parliament of the Slovak Republic, p. 24

3.2.3 Instruments extending liabilities of statutory organs of the company – disqualification of a statutory organ

The possibility of disqualification of a statutory organ of a company has been introduced to the Slovak legal order via Act No. 87/2015 Coll. with the entry into force on 01.01.2016.[128] Besides the member of a statutory organ, it was possible to disqualify also a member of the supervisory organ of a company, head of a branch of a legal person, the holder of the procuration, etc.[129] From the date of the legal validity of the decision on disqualification of the person as the statutory organ, that person ceased to be the member of statutory organ and/or supervisory organs in all Slovak companies.[130] The disqualification itself was the exclusive competence of the courts, with two different types of disqualification decisions. The first type of disqualification decision was the decision in which the court imposed the ban on being a statutory organ on such person.[131] The second type of disqualification decision was the decision of insolvency court based on which the court imposed a contractual fine based on the breach of the obligation to submit a proposal on declaration of bankruptcy on time by a person who has such obligation pursuant to specific legal provision.[132]

Pursuant to the amendment of the legal framework on disqualification, a statutory organ may be disqualified *"[by] the decision of the court, or by the decision of other organ, [provide that such decision] is reviewable by the court, if established by specific provision."*[133] The explanatory memorandum uses as an example of other organ that can disqualify a statutory organ a tax authority or administrative organ.

[128] Act No. 87/2015 Coll. amending and extending Act No. 513/1991 Coll. Commercial Code as amended and amending and extending other statutes (Zákon č. 87/2015 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2015] Slovak Republic

[129] O. Beracka, '*Changes in legal framework of companies connected with insolvency and restructuring*' (Zmeny v právnej úprave obchodných spoločností spojené s konkurzom a reštrukturalizáciou) [2015] 15 EPI Scholarly Articles (EPI Odborné články)

[130] Z. Bartlová, '*Commentary to the Act No. 513/1991 Coll.*' (Komentár zákona č. 513/1991 Zb.) (1st edn. EPI 2016) 56

[131] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 31(10)

[132] Act No. 7/205 on bankruptcy and restructuring (Zákon o konkurze a reštrukturalizácii) [2019] Slovak Republic Article 74a(6)

[133] National Parliament of the Slovak Republic, '*Explanatory memorandum to Act No. 264/2017 Coll. that amends and extends the Act No. 513/1991 Coll. Commercial Code as amended and amends and extends other statutes*' (Dôvodová správa k zákonu č. 264/2017 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2017] Publishing department of the National Parliament of the Slovak Republic, p. 15

The abovementioned instruments may be for the purposes of the presented thesis, in accordance with their application also distinguished in two broad categories. The first category is actively protective measures, which are the measure that are readily available for the creditors and grant them on one hand rights and on the other instrument via which they can protect their rights. The second category composes of passively protective measures such as introduction of criminal offence which primarily serves as a deterrent for unfair liquidation. As such it is important to state that both of those forms of instrument are available for private creditors (other companies) and public creditor (the state), however a distinction must be made regarding two categories of creditors.

Whereas instruments, as stated early, are available to both of those creditors, and so is the probability of recovery of their claims, the difference is on the effect of non-recovery of the said claim by those creditors. The non-recovery of claims by the state only creates the difference in state's budget and does not pose an existential threat for the state itself. However, should a private creditor fail to recover his receivables against the company, it may in certain situation pose a real threat for the financial and ultimately to the existential situation of the company. Stemming from that, it is important for the creditors to have instrument for protection of their interest and claims that would not either lead to long-lasting lawsuits and would enhance their legal certainty.

3.3 Piercing the corporate veil

One of the doctrines offering the protection of creditors in cases of unfairly liquidated company could be the doctrine of piercing the corporate veil. Before the assessment of the applicability of the said doctrine to unfairly liquidated companies, one must analyse the doctrine itself, evaluate its pros and cons and, and to discuss its impact on the doctrine of separate legal entity, that forms a cornerstone of principles of limited liability companies.[134]

[134] D.K. Millon, '*Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability*' [2007] 56 Emory Law Journal 5, 1309 1312

3.3.1 Doctrine of separate legal entity and reasons for limited liability company

The doctrine of separate legal entity states, in the case of the private limited liability company, that the company is a different person from its partners/shareholders. The justification of such doctrine may be summarized with 2 major advantages.

a) Efficiency[135]

The efficiency of limited liability doctrine towards economy at large operates on the theorem that limiting liability of shareholders for the action of the company increases their drive to invest. Business efficiency is also supported by time efficiency, in which shareholders do not need to invest much time in actively participating in control over the company's action to protect themselves from the risk of company's failure.[136] The limited liability also promotes independence of each shareholder as there is no need to for one shareholder to control the others.[137] The abovementioned efficiency-based reasons would if not present incur significant cost on each shareholder and as such, would ultimately lead in limiting the shareholder's active investment radius to fewer companies, which would eventually lead in fewer investments and worse economic situation. This efficiency is not limited only to companies with several shareholders, it also applies to sole shareholders of smaller companies as limiting their liability for the potential insolvency of the company motivates them to invest their time and resources despite the potential downfall, is such downfall would not directly affect their personal assets.

b) Risk reallocation

The other important aspect that adds to the economic benefit of the doctrine of separate legal entity lies in the transfer of risk from investors to creditors.[138] The shift in the risk allocation allows for investors to invest more and offers them business incentive. Such incentives are then translated in to creation of new jobs, tax revenues and ultimately it benefits the general public.

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[135] S.E. Woodward, '*Limited Liability in the Theory of the Firm*' [1985] 141 J. INSTITUTIONAL & THEORETICAL ECON. 601, 602

[136] F. H. Easterbrook, D.R. Fischel, '*The Economic Structure of Corporate Law*' (1st edn. Harvard University Press 1991) 41-42

[137] P. Halpern, M. Trebilcock, S. Turnbull, '*An Economic Analysis of Limited Liability in Corporate Law*' [1980] 30 University of Toronto Law Journal, 117, 123-124

[138] Supra note 136, 602

This short summary sums up the advantages and benefits of the doctrine of separate legal entity and the subsequent limited liability of shareholders for the debts of the company. However, there are other important aspect that are worth mentioning. One of the factors that undermines the necessity of separate legal entity is a fact that certain creditors such as banks, require of shareholder to be the personal guarantor for the loan, or they secure the provided loan by immovable property as a security. In such cases, the need for the limited liability may seem redundant. Despite such option, as not every creditor is in the position that allows him for requirement of other guarantee by the debtor. In the ideal business environment such shortcoming would not pose any threat to neither secured and ordinary creditors. However, as we discuss in the presented thesis, in the situation such as unfair liquidation of a company, the effect of the limited liability and the doctrine of separate legal entity is the direct opposite of what its initial effect.

Stemming from that, there is a need to limit the usage and the scope of limited liability. This could be done via the doctrine of piercing the corporate veil.

3.3.2 Doctrine of piercing the corporate veil

As mentioned above, the doctrine of separate legal entity and the subsequent limited liability of shareholders is a desired instrument for promotion of economy and ultimately a general welfare.[139] However, there may be situation in which there is need for intervention to the "unlimited" limited liability of the shareholders for the same reason as the reason of its creation – general welfare and promotion of economy. This argument is supported by so-called domino effect based on which if we allow for "unlimited" limited liability and such limited liability is abused, there would be no desire of creditors to conduct a business with limited liability companies, as they tend to abuse their limited liability.[140] However, the counter-argument could be the "invisible hand" of the market,[141] and that the market would eradicate the "businessmen" abusing the limited liability. That might be the theoretical approach, however, such *ex-post* adjustment of the market leaves behind many creditors with non-recovered claims.

[139] D.K. Millon, '*Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability*' [2007] 56 Emory Law Journal 5, 1309 1317
[140] W.P. Hackney, T.G. Benson, '*Shareholder Liability for Inadequate Capital*' [1982] 43 University of Pittsburgh Law Review, 837, 898
[141] W.A. Klein, J.C.Coffee Jr., 'Business organization and finance' (8th edn. Foundation Pr 2002) 242-246

Stemming from that, it is of vital importance that an instrument is used that can offer effective protection for each creditor that is defrauded by the action of illegitimate businessman abusing limited liability.

The doctrine of piercing the corporate veil (hereafter as the "*Piercing*") with its concept of holding a shareholder liable for the liabilities/debts of the company by virtue of which it completely overturns the principle of limited liability by virtue of which it offers the creditors the possibility to be satisfied from the assets of the shareholder.[142]

The Piercing has its roots in common law countries which stems from the fact that the common law countries are more flexible in terms of their decision making and are not bound only by statutes and/or other ex-ante forms of legal sources. Despite its abundance in the common law legal system, the Piercing is rarely used by the courts, due to its impact on the principles of separate legal entity and the doctrine of limited liability of the shareholders. As such, it is often view as *ultima ratio*.[143] However, if used, it has proven to be the effective form of the protection of creditors' interest. The underlying reasons for application of the Piercing and the limitation of doctrine of limited liability may be found in the relevant jurisprudence and argument of scholars.

At first, it must be stated that the limited liability of shareholders in English common law is granted by the statutory provision, and as an English judge, Willes J, stated, the legal provision shall be interpreted *as "whatever the language used necessarily or even naturally implies."*[144] Even in the famous *Salomon* case that is an epitome of confirmation of doctrine of separate legal entity and limited liability, the court stated that: *"[In] a Court of Law or Equity, what the Legislature intended to be done or not to be done can only be legitimately ascertained from that which it has chosen to enact, either in express words or by reasonable and necessary implication."*[145]

In other case of *Sanders* the court continued and stated that *"[Accordingly] separate personality cannot be extended to a point beyond its reason and policy, and will be disregarded when this occurs."*[146] Stemming from that, the legislator's intentions were to

142 F.H. Easterbrook, D. R. Fischel, '*Limited Liability and the Corporation*' [1985] 52 The University of Chicago Law Review 89, 95
143 C. Alting, '*Piercing the Corporate Veil in American and German Law – Liability of Individuals and Entities: A Comparative View*'[1994] 2 Tulsa Journal of Comparative & International law 187, 197
144 *Charlton v. Lings,* [1868] L.R. 4 C.P. 374 (Ct. Common Pleas) 387
145 *Salomon v. A. Salomon & Co. Ltd.,*[1897] A.C. 22 (H.L.) 38
146 *William H. Sanders v. Roselawn Memorial Gardens, Inc.,* [1968] 159 S.E.2d 784, 800

provide the limited liability of shareholders towards their company so as to facilitate the economy, their desire was not to create a loophole in which it would be possible to harm either creditors or other persons engaged with the company.

Despite these elaborate reasons that justify the utilization of the Piercing, the said doctrine is used rarely in practice by the courts.[147] However, as English jurisprudence suggests, the Piercing may be used in order to prevent the abuse of corporate legal personality.[148] This is supported by the US court which in the *Glazer* case stated that *"[a court may] pierce the corporate veil when the established norm of corporateness has been so abused in conducting a business that the venture's status as a separate entity has not been preserved."*[149] This however, opens a wide array of possibilities in which the Piercing could be used, and as such it may deter shareholders to start new ventures using limited liability companies. This is one of the reasons why some of the advocates for the Piercing opt for the narrow applicability.[150] The other reason for narrow applicability and/or the redundancy of the Piercing is the fact, that in the cases where there are enough reasons to pierce the corporate veil, there is an overlap with other existing instruments for protection of creditors that do not stomp over the limited liability doctrine.[151] This however, shall be tested based on the relevant legislation in particular jurisdiction. Pursuant to the jurisprudence of USA, the Piercing is used on closely held corporations[152] – i.e. companies controlled by small amount shareholders that has acted in conflict with good manners or committed illegal acts.[153] Stemming from that, we are of the view that the Piercing, if drafted in accordance with current legal framework of the Slovak Republic could be potentially used as an effective instrument for protection of creditors in unfair liquidation of a company, however, this is closely discussed in Chapter 5 of the presented Thesis.

[147] D. Cabrelli, M. Siems, '*Comparative Company law – A Case-Based Approach*' (2nd edn. Hart Publishing 2018) 219

[148] *VTB Capital Plc v Nutritek International Corp,* [2012] EWCA (Civ) 808, 2 C.L.C. 431, 460

[149] *Glazer v Comission on Ehtics for Public Employees,* [1983] 431 So. 2d 752, 757

[150] T.K. Cheng, '*Form and substance of the doctrine of piercing the corporate veil*' [2010] 80 Mississippi Law Journal 497, 510

[151] *Mentmore Manufacturing Co. v National Merchandise Manufacturing Co,* [1978] 89 DLR (3d) 195, par. 23

[152] J.K. Vandervoort, '*Piercing the Veil of Limited Liability Companies: The Need for a Better Standard*' [2004] 3 DePaul Business and Commercial Law Journal 51, 57

[153] ibid. 58

3.4 Overview

The aim of the chapter was to analyse the instruments available to the creditors of unfairly liquidated company within the legal framework of the Slovak Republic. The examination of the current legal framework in conjunction with the relevant jurisprudence has shown, that the creditors may protect their claim by contesting the validity of the agreement on transfer of shares between the transferor (person controlling the company) and the transferee (straw-man), which may ultimately lead into reinstitution of the transferor back to the position of the partner in the company. However, due to the scarcity of the jurisprudence on this particular matter it is analytically impossible to address the successfulness of such action regarding the protection of creditors' claims and as such, the possible contest of validity is theoretical approach.

The next part of the chapter was dedicated to the analyses of the amendment to the Commercial Code effective as of 01.01.2018 and its practical implications on the protection of creditors in the event of an unfair liquidation of the company. The amendment in itself tackles the unfair liquidation from two perspectives based on the manner in which they are executed.

At first, it tackles the unfair liquidation realized via transfer of shares of the company to a straw-man. For such cases, the amendment introduces criminal liability for persons engaged either directly (by acting as a straw-man) or indirectly (by facilitating the transfer of shares) in unfair liquidation via transfer of shares.

At second it tackled the unfair liquidation via merger/acquisition. It does so by introduction of mandatory requirements which companies shall fulfil prior to their merger/acquisition. Such imposition of requirements creates a situation in which it is technically impossible to conduct an unfair liquidation via merger/acquisition without breaching pre-conditions laid down by the amendment. The question however remains, whether such conditions, that are applied to all mergers/acquisition fulfil proportionality test and do not go beyond what is necessary to achieve the aim. In other words, whereas their initial aim is to improve the business environment, their impact may in some cases be completely the opposite, as businesses are reluctant to accept increased bureaucracy.

Lastly, the amendment enhances the liability of statutory organs of the company by extending the authorities and grounds upon a statutory organ may be disqualified.

The chapter also contemplates and introduces the doctrine of piercing the corporate veil as the possible instrument in protection of creditors in an event of unfair liquidation of the company. The doctrine having its roots in common law jurisdictions offers a possibility of disregarding the basic principles of commercial law such as separate legal entity and limited liability and holding a partner/shareholder of the company directly liable for the debts of the company towards its creditors. However, due to the impact of the doctrine of piercing the corporate veil on the basic principles of commercial law, it must be carefully analysed whether such introduction of the doctrine is viable in the conditions of the Slovak Republic. As such, the comparative assessment of the implementation of the said doctrine in different jurisdiction is conducted in the following chapter.

4 Piercing the corporate veil in selected jurisdictions

The following chapter analyses the implementation and/or mutation of the doctrine of piercing the corporate veil in selected jurisdictions, with the aim of comparing their implementation and assessment of their usefulness and prospective utilization in the Slovak legal order. The jurisdictions chosen are as follows:

The idea of choosing the Czech Republic is based on the three main pillars. First of all, the circumvention of variety of legal obligations via usage of straw-man is similar problem as in the Slovak Republic. Second of all, both the Slovak Republic and the Czech Republic have similar socio-economic-legal roots which stems from their mutual history as then Czechoslovakia.[154] Third of all, the factor common to all selected jurisdictions, the Czech Republic is a member state of the European Union and as such, its legal framework shall be in line with the law of the European Union.[155]

The Republic of Austria is chosen for another three reasons. At first, it is also a member state of the European Union.[156] At second, it is a civil law country and thus has similarities to the legal framework of the Slovak Republic.[157] At third, the Austrian legal framework is a dynamic, complex and adaptable which is often used as an example in amendments of the Slovak legal system.

The United Kingdom is chosen due to following facts. It is (in time of writing this thesis still) a member of the European Union.[158] It is a common law country which invented and perfected the doctrine of piercing the corporate veil.[159]

Stemming from the factors that have been taken in selection of the compared jurisdictions, this chapter assess their implementation and practical implications in terms of protection of creditors in unfair liquidation of the company.

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[154] A. J. Innes, 'The Partition of Czechoslovakia' (1st edn. ProQuest LLC 2014) 105
[155] A. Zhelyazkova, C. Kaya, R. Schrama, '*Decoupling practical and legal compliance: Analysis of member states' implementation of EU policy*' [2016] 55 European Journal of Political Research 827, 832
[156] J. Greenwood, '*Interest Representation in the European Union*' (4th edn. PALGRAVE 2017) 175
[157] G. Palumbo, G. Giupponi, L. Nunziata, J. Mora-Sanguinetti, '*Judicial performance and its determinants: a cross-country perspective*' [2013] 5 OECD Economic Policy Papers 6, 8
[158] Supra note 156, 833
[159] C-H. Tan, J. Wang, C.Hofman, '*Piercing the Corporate Veil: Historical, Theoretical & Comparative Perspectives*' [2019] 16 Berkeley Business Law Journal 140, 145

4.1 The Czech Republic

Similarly to the Slovak Republic, the unfair liquidation in the Czech Republic is engaged either via transfer of shares to the straw-man, or via the unfair liquidation by merger/acquisition of the company. The first part of the chapter is dedicated to the unfair liquidation via transfer of shares, whilst the latter focuses on unfair merger/acquisition.

One of the basic principles, that are applied in the field of commercial law in the Czech Republic is the principle of loyalty.[160] The said principles serve as an interpretational guide for definition of particular obligations of the partner towards the company. Stemming from that, in the cases of transfer of shares of the company the transferor shall act in accordance with the principles of loyalty, and as such shall act in loyalty towards the company and also towards to other partners. It follows that in the process of transfer of shares of the company the transferor shall also take into account the interest of company itself. This has been confirmed by the Supreme Court of the Czech Republic, which in its decision states: *"[by] the usage of the principle of loyalty it is then possible to deduct, that one of the obligations of the partner in the process of transfer of shares is, that such transfer of shares shall not disproportionally and unreasonably endanger further functioning and the existence of the company, or [the transferor] shall not abuse the transfer of shares for the purposes of circumventing the obligations that would otherwise arise in prospective liquidation or bankruptcy of the company".*[161]

The breach of the principle of loyalty is a reason for submitting a claim for determination of validity of the agreement on transfer of shares, which is a one of the tools for protection of creditors in the Czech legal framework in the events of unfair liquidation. The said statement is further supported by the Judgment of the Supreme Court of the Czech Republic dated 26.06.2007, in which the Supreme Court decided the case as the highest appeal court. The plaintiff, in this case the creditor of the company whose shares had been transferred to a new partner, contested the validity of the agreement on transfer of shares, based on the merits that the agreement on transfer of shares was concluded by the former partner for the purposes of circumventing his obligations as the company has found itself in financial problems. The plaintiff sought the legal protection at the highest appeal court after the appeal

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[160] S. Černá, '*Commercial law – Joint-stock corporation III.*' (Obchodní právo. Akciová společnost III.) (1st. edn. ASPI 2006) 185

[161] Judgment of the Supreme Court of the Czech Republic issued on 26.06.2007, ref. no. 29 Odo 387/2006

court has confirmed the decision of the court of first instance which refused the plaintiff's submission claiming that the plaintiff is not a party to the agreement on transfer of shares and that it lacks the imperative legal interest in the presented case. The plaintiff as the appellant in front of the Highest Appeal Court states that despite the fact that she is not a party to the agreement on transfer of shares, such transfer is paramount to her interest as by the transfer of shares to a person with unknown address the transferor had breached the principle of fair dealing. She further states, that by such action of the partner and the statutory organ of the company, when by transfer of shares the new sole partner of the company becomes a person without genuine interest to continue in the business activity, such action has an impact on all of the creditors of the company, as their legal claims against the company become practically nonrecoverable. According to the plaintiff's opinion, the agreement on transfer of shares was clearly concluded with unfair intentions to circumvent the problems with insolvent company, and as such, it is pursuant to Article 39 of Civil Code of the Czech Republic absolutely invalid as it contradicts the good manners.[162]

The Highest Appeal Court firstly dealt with the question of whether the plaintiff has the imperative legal interest in the presented case. The Highest Appeal Court in its reasoning, *inter alia*, states that the Appeal Court, when addressing the plaintiff's imperative legal interest, did not take into account that the manners in which the company is managed have a direct impact on the plaintiff's legal standing. *"In order to assess the existence of the imperative legal interest of the plaintiff ,it is substantial to attest whether the claims of the plaintiff that the former partner intentionally (gratuitously) transferred 100% of shares of the company to the person that was not capable and/or willing to act as a partner in the company and to manage such company [...]. [Moreover] if it is shown that the former partner transferred his shares under such circumstances in order to circumvent the obligations that [the former partner] would have from prospective liquidation or bankruptcy of the company."*[163] The Highest Appeal Court then in its decision applies the above-mentioned principle of loyalty in light of which the actions of the partner shall be considered. This legal opinion is further supported by Article 66 par. 6 Commercial Code of the Czech Republic[164], by virtue of which the articles of legal statutes on the liability and the guarantee of the organs and the members of the organs of the company are extended also to the persons,

[162] Act No. 89/2012 Coll. Civil Code (Občanský zákoník) [2019] Czech Republic Article 39
[163] Judgment of the Supreme Court of the Czech Republic issued on 26.06.2007, ref. no.:29 Odo 387/2006
[164] Act No. 513/1991 Coll. Commercial Code (Obchodní zákoník) Czech Republic Article 66(6)

who either based on the agreement, their share in the company, or other actuality significantly affect the functioning of the company, regardless of their relation with that company. The Highest Appeal Court considers the sole partner of the company to be such person. Based on that, the Highest Appeal Court came to a conclusion, that based on the particular circumstances of the case, i.e. when the unfair intentions of the transferee to circumvent the obligations stemming from the prospective liquidation and/or bankruptcy, shall be liable for the commitments of the company pursuant to Article 194 par. 5 and 6 of Commercial Code of the Czech Republic[165], which shall be accordingly applied also to the statutory organ of the company.[166]

In light of the above-mentioned legal assessment it may seem that the Highest Appeal Court of the Czech Republic induced to the doctrine of piercing the corporate veil, which could in other words, lead into requalification of the action of the company to be the action of its partners. However, as Lokajíček states, this decision of the Supreme Court of the Czech Republic is only a cautious step of the Czech judiciary towards the doctrine of piercing the corporate veil.[167] He supports his statement by the fact that the application of the doctrine of piercing the corporate veil would only be possible if the Court of first instance (as the Highest Appeal Court returned the case to the Court of first instance for another proceedings) decided, that the partner is directly responsible for the commitments of the company based on the unfair intentions of the partner.[168] On the other hand, should the court decide "only" on the invalidity of the agreement on transfer of shares without transferring the direct liability for the commitments of the company to the partner, the situation would only resemble the doctrine of piercing the corporate veil.

The conclusion of the Supreme Court of the Czech Republic was later utilized by the Higher Court in Prague in its decision dated 08.06.2015.[169] The merits of the case were similar to the former case – the partner in the company, which was in bad economic situation, and which not fulfilled its obligations towards its creditors, transferred his shares to a third parson. The creditor in the presented case also filed a lawsuit claiming the invalidity of the

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[165] Act No. 513/1991 Coll. Commercial Code (Obchodní zákoník) Czech Republic Article 194(5)-194(6)
[166] ibid. Article 135(2)
[167] J. Lokajíček, '*The Doctrine of Piercing the corporate Veil or breaking of doctrine of limited liability of legal person and their options in Commercial Law of the Czech Republic'* (Doktrina Piercing the corporate Veil neboli prolomení majetkové samostatnosti právnické osoby a její možnosti v českém obchodním právu) [2011] 12 Legal review (Právni rozhledy) 105, 110
[168] ibid.
[169] Judgment of the Higher Court in Prague issued on 08.06.2015, ref. no.: 14 Cmo 524/2013

agreement on transfer of shares. The Higher Court in Prague has in the process of assessment of the active legitimation of the creditor referred to the decision analysed above, and as such, approved the existence of the imperative legal interest of the creditor in the presented case.[170] Simultaneously, however, the Higher Court in Prague stated, that in reference to the Supreme Court of the Czech Republic, the presented claim shall be formulated as an action on determination of the ownership rights to the particular shares, whilst the validity of the agreement on transfer of shares shall be treated as prejudicial question.[171] In connection with this case it is important to note, that the principle of loyalty was at the time of the decision explicitly incorporated in Article 212 (1) of Civil Code.[172]

Another interesting institute applied in the Czech commercial law is the institute of personal guarantee of transferor for the debts, that had been transferred with the shares from transferor to transferee.[173] The aim of this institute is to secure that the transfer of shares is not abused for circumvention of obligatory approval of the creditor that is otherwise required when the change in the person of debtor occurs, and as such, it prevents the deterioration of the position of the creditor.

Furthermore, similarly to the Slovak legal order, the action of transferring the shares to a straw-man has also a criminal law recourse as transferor may be charged with a criminal offence of harm done to a creditor[174], and/or fraud respectively[175], which may be in conjunction with the criminal offence of distortion of data in financial and commercial records.[176]

When it comes to unfair liquidation via merger or acquisition, the legal order of the Czech Republic protects the creditors in twofold manner, which can be divided into *ex ante* and *ex post* protection of creditors. First of all, ex ante protection of creditors in the process of the merger or acquisitions imposes notification obligation upon the parties engaged in the merger/acquisition.[177] This serves as a protection of creditors for the creditors may be informed on the proposed and prepared merger/acquisition and actively engage in it. Second

[170] Judgment of the Supreme Court of the Czech Republic issued on 29.04.2003, ref. no.: 21 Cdo 58/2003
[171] Judgment of the Higher Court in Prague issued on 08.06.2015, ref. no.: 14 Cmo 524/2013
[172] Act No. 89/2012 Coll. Civil Code (Občanský zákoník) [2019] Czech Republic Article 212(1)
[173] Act No. 90/2012 Coll. on corporations and cooperatives (Zákon o obchodních společnostech) [2019] Czech Republic Article 209
[174] Act No. 40/2009 Coll. Penal Code (Trestní zákoník) [2019] Czech Republic Article 256
[175] ibid. Article 209
[176] Decision of the Supreme Court of the Czech Republic issued on 22.07.2015, ref. no.: 8Tdo/617/2015
[177] Act No. 125/2008 Coll. on transfer of corporations and cooperation (Zákon o proměnách obchodních společnosti a družstev) [2019] Czech Republic Article 33(1)(a)

of all, the *ex post* protection of creditors comprises of the possibility of statutory organs, members of the supervisory boards and experts who had engaged in the merger/acquisition to be held liable for the harm done to the creditors.[178] However, such liability is not absolute, the law allows for liberation from the liability. Those persons may be liberated from the liability for the harm, if they prove that they had acted in accordance with legally prescribed care.[179] For instance, the legally prescribed care of statutory organ may be understood as "*care of the good manager*".[180] The right of the creditor to seek redress for the damages occurred is time-barred within 5 years from the date when the recording of the merger/acquisition became effective against third parties.[181]

Based on the abovementioned analysis of the Czech Republic's legal framework on protection of creditors in the process of unfair liquidation, we can deduct following notions.

At first, in the process of transfer of shares, the Czech Republic's legal framework operates with the principle of loyalty. This principle allows for possibility of invalidity of agreement on transfer of shares and ultimately leads into liability of former shareholder for the debts of the company. However, this as Lokajíček states, merely resembles the doctrine of piercing the corporate veil, although we observe it as a step forward in the process of protection of creditors.[182]

At second, in regard to unfair liquidation via merger/acquisition, the Czech Republic's legal framework offers a two-step protection which consists of ex ante notification obligation and subsequently of ex post right of creditors to seek the remedy for the damages occurred by merger/acquisition.

The Czech Republic's legal framework in protection of creditors in unfair liquidation uses a mutation of the doctrine of piercing the corporate veil, which on one hand offers a higher flexibility for shareholders/partners in the company to conduct their transfer of shares and/or merger/acquisition than in the Slovak Republic. However, such flexibility in

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[178] Act No. 125/2008 Coll. on transfer of corporations and cooperation (Zákon o přeměnách obchodních společnosti a družstev) [2019] Czech Republic Article 50
[179] ibid. Article 50(2)
[180] P. Kuhn et.al., '*Act on transfer of corporation and cooperation. Commentary'* (Zákon o přeměnách obchodních spolčností a družstev. Komentář) (1st edn. C.H. Beck Prague 2010) 101
[181] Supra note 179 Article 50(4)
[182] J. Lokajíček, '*The Doctrine of Piercing the corporate Veil or breaking of doctrine of limited liability of legal person and their options in Commercial Law of the Czech Republic'* (Doktrina Piercing the corporate Veil neboli prolomení majetkové samostatnosti právnické osoby a její možnosti v českém obchodním právu) [2011] 12 Legal review (Právni rozhledy) 105,108

comparison to Slovak' rigidness brings about higher liability of partners for abusing the rules concerning transfer of shares and/or merger/acquisition.

4.2 The Republic of Austria

The Republic of Austria is a civil law country which readily utilizes the doctrine of piercing the corporate veil and as such, it is an ideal comparatist country for the analysis of the applicability of the doctrine. The doctrine of piercing the corporate veil (Durchgriffshaftung) is widely recognized by Austrian judiciary, as the Austrian Oberster Gerichtshof has held: *"[...] the underlying principle of piercing the corporate veil is that no one may use a legal entity in order to damage a third party, or in order to evade the law."*[183] Such position is supported by P. Jabornegg who reasons that: *"[...] the aspect of an abuse of law must be taken into account because, in any context, the legal system will oppose to an abusive behaviour, particularly through liabilities. One would virtually have to invent reasons why, in the context of corporate veil piercing, this not be the case."*[184]

Building on that, the doctrine of piercing the corporate veil is well established in Austrian judiciary and as such is used in specific situations which can be divided into 7 distinct categories.

The first category for application of the doctrine of piercing the corporate veil arise in the situation when there is no separation between the assets of the company and the assets of the partner of the company (Vermögens – oder Sphärenvermischung)[185]. The reasoning for differentiation between the assets of the company and those of the partner is simple – one must determine whether the partner did not enrich himself for the determent of the company.[186]

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[183] OGH, 26 April 2006, Ref. no.: 7 Ob 236/05i

[184] P. Jabornegg, '*Studies from excurse in law of the capital companies*' (Die Lehre vom Durchgriff im Recht der Kapitalgesellchaften) (1st edn. WBI 1989) 25

[185] F. Wünscher, '*Piercing the corporate veil because of commingling of assets in German and Austrian limited liability company-law*' (Die Durchgriffshaftung wegen Sphärenvermischung im deutschen und österreichischen GmbH-Recht) (University of Graz 2014) 24

[186] ibid. 25

The second category encompasses situations in which the company is not capitalized sufficiently (Qualifizierte Unterkapitalisierung)[187], in such assessment the court would address the purpose of the company, its capitalization and the likelihood of creditors' loss.[188]

The third category consists of situation in which a shareholder acts towards the third parties as the director of the company without being officially appointed as director (Faktische Geschäftsführung).[189] In such situations the shareholder shall be held liable under the similar circumstances as if he was appointed as director.[190]

The fourth category comprises of situations in which a shareholder causes a negative ratio between company's assets and liabilities and as such causes shortage of funds (Existenzvernichtung).[191]

The fifth category is one of the most frequently used and encompasses the abuse of corporate structure (Rechtsformmissbrauch).[192] This consists of action of a shareholder who abuses the corporate structure and its limited liability to harm creditors or circumvent statutory provisions and/or gain unfair advantage.[193]

The sixth and seventh category concern the issue of insolvency and encompass situations in which the shareholders ignore the need for reorganisation (Ignorieren von Reorganisationsbedarf)[194] and when the shareholders instruct directors to postpone and/or refrain from filing a proposal for insolvency proceedings (Insolvenzverschleppung).[195]

All of these categories may lead into application of doctrine of piercing the corporate veil and as a result, the shareholder or the partner in the company may be held personally

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[187] L. Fantur, '*Piercing the corporate veil in a private limited liability company'* (Zur Durchgriffshaftung bei der GmbH) [2005] 1 Gesselschaftsrecht 19, 19

[188] D.P. Halmer, '*Shareholder Loans and Piercing the Corporate Veil. On the Legal Economics of Limited Liability under Undercapitalization'* (Gesellschafterdarlehen und Haftungsdurchgriff Zur Rechtsökonomik beschränkter Haftung bei Unterkapitalisierung) (1st edn. Mohr Siebeck 2013) 53

[189] Supra note 188

[190] DLA Piper, '*Corporate Personality: International Perspectives Part I*' (1st edn. DLA Piper 2018) 9

[191] P. Graf, '*The liability of the sole shareholder for existence-damaging interventions in private limited liability company*' (Die Haftung des Alleingesellschafters für existenzvernichtende Eingriffe in die GmbH) (1st edn. dipom.de 2012) 17

[192] Supra note 188

[193] R. Stark, '*Liability of the registered association*' (Die Haftung des eingetragenen Vereins) (1st edn. Dr. Stark, Niedeggen & Kollegen 2008) 4

[194] Federal Act No. 114/1997 on the Reorganization of Enterprises (Bundesgesetz über die Reorganisation von Unternehmen (Unternehmensreorganisationsgesetz - URG)) [2019] The Republic of Austria Article 22(4)

[195] Federal Act No. 337/1914 on Insolvency Proceedings (Bundesgesetz über das Insolvenzverfahren (Insolvenzordnung – IO)) [2019] The Republic of Austria Article 69

liable for the harm done to the creditors. The actual claim for piercing the corporate veil may be either brought by an aggrieved creditor or by a liquidator in an insolvency proceeding.[196]

It must be however added, that despite the existence of numerous categories/situations in which the doctrine of piercing the corporate veil may be used and the shareholder/partner in the company may be held liable for the damages, this is not a common approach of the Austrian courts. The reasons for the reluctancy are twofold, first of all, the action of the shareholder/partner of the company must be intentional or negligent act or omission which must be proven to the shareholder/partner of the company.[197] The second reason for the reluctancy is the fact that has been mentioned previously in the thesis – the doctrine of piercing the corporate veil completely reverses the cornerstone of the limited liability companies – limited liability of partners/shareholders.[198] Stemming from that, there is rather low risk that the Austrian court would effectively apply the doctrine of piercing the corporate veil and hold shareholder/partner liable either towards the company itself or towards the creditors of that company.[199]

The analyses of the Austrian legal framework on piercing the corporate veil has shown, that the Austrian judiciary does have the doctrine on piercing the corporate veil at their disposal, with the usage being limited to the categories mentioned above. However, as the actual application of the doctrine, due to its impact on the traditional separate legal personality doctrine of limited liability companies, is restricted and limited, we do not see often its practical usage. Therefore, we are of the view, that in the cases such in Austria, the existence of the doctrine of piercing the corporate veil has rather preventive function of deterring possible abuses of limited liability of the shareholders in the company.

[196] DLA Piper, '*Corporate Personality: International Perspectives Part I*' (1st edn. DLA Piper 2018) 10
[197] CMS Legal Services, '*Liability of holding companies: A CMS Corporate/M&A Publication*' (1st edn. CMS Legal Services 2016) 11
[198] D.K. Millon, '*Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability*' [2007] 56 Emory Law Journal 5, 1309 1312
[199] Supra note 198 11

4.3 The United Kingdom

The United Kingdom, the representative of the common law countries in the comparative assessment of the doctrine of piercing the corporate veil may also be regarded as a cradle of such doctrine. Despite such label, the doctrine itself is rarely used by the courts of the United Kingdom.[200] This approach has its roots in the history of the development of the doctrine, which Cheng divides into three time periods.[201] The first one started in 1987 with the famous Salomon v Salomon[202] case up until the Second World War. This period is according to Chen represented by different attempts of the courts to approach the doctrine of piercing the corporate veil.[203] The second period lasted from the end of the Second World War until 1978, when the peak of the doctrine was reached due to rational and liberal judgment of Lord Denning.[204] The third and the last period commenced from 1978 onwards, when the decision in the case Woolfson v Strathclyde Regional Council[205] was issued. This decision marks a period which is represented by the decline of the utilization of the doctrine. This trend was further observed in the case of Adams v. Cape Industries'[206].

As the historical development of the doctrine of piercing the corporate veil depicts, the application of the doctrine by the English courts lacks systematic approach.[207] The courts could not develop any specific rules to support the application of the doctrine. The only development that may be observed is the categorization of the cases in which courts had used the doctrine to pierce the corporate veil.[208] Such categorization was based on rather vague criteria that court tend to rely upon when piercing the corporate veil. Some of the criteria include agency, trusts, fraud, enemy, group enterprises, taxation and breaches of provisions of Companies Act and/or other legislation.[209] We are of the view that the criteria

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[200] T.K. Cheng, '*Form and substance of the doctrine of piercing the corporate veil*' [2010] 80 Mississippi Law Journal 497, 528
[201] T.K. Cheng, '*The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines'* [2011] 34 Boston College International and Comparative Law Review 329, 334
[202] *Salomon v. A. Salomon & Co. Ltd.,*[1897] A.C. 22 (H.L.) 38
[203] Supra note 202 334
[204] S. Worthington, 'Sealy & Worthington's Text, Cases, and Materials in Company Law' (8th edn. OUP 2008) 53
[205] *Woolfson v. Strathclyde Regional Council,* [1978] UKHL 5 SLT 159, 38 P&CR 521
[206] M.T. Moore, '" *A Temple Built on Faulty Foundations": Piercing the Corporate Veil and the Legacy of Salomon v Salomon*' [2006] MAR Journal of Business Law 180, 181
[207] Supra note 202, 337
[208] A. Beck, '*The Two Sides of the Corporate Veil*' in J.H. Farrar (eds), *Contemporary Issues in Company Law* (1st edn. Commerce Clearing House 1987) 69, 71-73
[209] ibid.

itself create to certain extend a discrepancy in the application of the doctrine, for each of the criterion may encompass different reason for piercing the corporate veil, without creating complex, comprehensible and logical applicability structure.

For instance, taxation cases and cases concerning breaches of provisions of Companies Act operate only on the plane of the provisions that were breached.[210] The group enterprises cases concern only cases of holdings and that the mother company shall be liable for the debts of its daughter.[211] The enemy category is rather obsolete, as it was used only once in history – during the First World War the corporate veil of Daimler was pierced.[212]

One of the most frequently used criteria for applying the doctrine of piercing the corporate veil by the English Courts is the agency criterion. Shall the court find that the company is merely an agent for the shareholders, the court would pierce the corporate veil. This condition must always be satisfied, otherwise the court would not pierce the corporate veil. This was confirmed in case Adams v Cape Industries Plc. in which the court stated that it is not *"[...] open to this court to disregard principle of Salomon v A Salomon & Co Ltd merely because it considers it just to do so."*[213] The emphasis on the agency criterion sometimes leads into court to omit other categories upon which the court could pierce the corporate veil. This is supported by the decision in the case Commissioner of Inland Revenue v. Sansom[214], the case concerned defendant – Mr. Sansom who used his company only to prevent tax liabilities. The court however, decided the case in favour of Mr. Sansom without contemplating other categories of criteria for piercing the corporate veil such as taxation policies. As the court focused solely on the agency criterion it ruled in favour of Mr. Sansom stating, that had the court used the agency criterion and pierce the corporate personality, it would have meant that Mr. Sansom as a shareholder had made a loan to himself, which would be illogical.[215]

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[210] A. Beck, '*The Two Sides of the Corporate Veil*' in J.H. Farrar (eds), *Contemporary Issues in Company Law* (1st edn. Commerce Clearing House 1987) 69, 72
[211] J.H. Farrar, '*Company law*' (1st edn. London: Butterworths 1985) 77
[212] *Daimler Co Ltd v. Continental Tyre and Rubber Co (Great Britain) Ltd,* [1916] 2 AC 307
[213] *Adams v. Cape Industries plc* [1990] Ch 433
[214] *The Commissioners of Inland Revenue v. John Sansom* [1924] 8 TC 20
[215] ibid.

The common law frequently also uses the criterion of fraud. The English courts use fraud as one of the most predictive categories for piercing the corporate veil.[216] This fact, however, does not change the degree of reluctancy of English courts to pierce the corporate veil. One of the reasons is that fraud is, in comparison to misrepresentation, harder to prove.[217] Whereas the misrepresentation may be done intentionally or negligently, fraud must be intentional and have malicious intent.[218] In other words, all frauds are logically speaking misrepresentations, but not all misrepresentations are frauds. Stemming from that, the actual proving of the existence of fraud is one of the most challenging parts of lifting the corporate veil.[219] As Cathy S Krendl & James R Krendl state *"[...] fraud cases are difficult to prove, and the quantum of evidence available in most corporate veil cases is considerably smaller than would be required to carry the burden on a fraud claim."*[220]

On the other hand, the category of tort as a ground for piercing the corporate veil, is an example of a criterion that is rarely used for piercing the corporate veil. The exemplary case in this regard is the case Williams v Natural Life Health Food Ltd (NHLF)[221], in which the judiciary shown their position towards tort being used as a criterion for piercing the corporate veil: *"[...] in order to fix a director with personal liability, it must be shown that he assumed personal responsibility for the negligent misstatement made on behalf of the company [...] a company director is only to be held personally liable [...] if the plaintiffs can establish some special circumstances setting the case apart from the ordinary [...]."*[222]

The overall decline and the reluctancy of English judiciary to utilize the doctrine of piercing the corporate veil is best portrait by the decision in Adams v. Cape Industries' case in which the American parent company had closed its English subsidiary in order to avoid liabilities for intentionally locating asbestos operations in the underfunded subsidiary. In the presented case the court stated: *"[W]e do not accept as a matter of law that the court is entitled to life the corporate veil as against a defendant company which is the member of a*

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[216] T.K. Cheng, '*The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines'* [2011] 34 Boston College International and Comparative Law Review 329, 358
[217] *Re Darby, ex parte Brougham*, [1911] 1 KB 95
[218] F.J. Cavico, '*Fraudulent, Negligent, and Innocent Misrepresentation in the Employment Context: The Deceitful, Careless, and Thoughtless Employer*' [1997] 20 Campbell Law Review 2, 68
[219] T.K. Cheng, '*The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines'* [2011] 34 Boston College International and Comparative Law Review 329, 358
[220] *C.S. Krendl, J. R. Krendl, 'Piercing the Corporate Veil: Focusing the Inquiry'* [1978] 1 Denver Law Journal 55, 58
[221] *Williams v Natural Life Health Foods Ltd.,* [1998] UKHL 17
[222] *ibid.*

corporate group merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law."[223]

As it may be observed from the analysis of the English' judiciary approach towards the piercing the corporate veil, currently the judiciary are rather reluctant to utilize the doctrine of piercing the corporate veil. The historical development of the practical applicability of the doctrine has led into categorization of cases in which the doctrine of piercing the corporate veil may be used. However, as those cases often operate on separate planes, the complex system for assessment of the cases is yet to be developed. The conservative approach of English judiciary is rather pragmatic, as limited liability is a cornerstone of business entrepreneurship and the doctrine of piercing the corporate veil poses a direct threat to its basis.

4.4 Overview

The chapter analysed and compared the implementation of the doctrine of piercing the corporate veil in the selected jurisdictions.

The first jurisdiction analysed was the Czech Republic. The analysis of the legal framework and the jurisprudence of the Czech Republic has shown the usage of action that resembles the doctrine of piercing the corporate veil. This is realized via invalidation of agreement on transfer of shares which subsequently leads into restoration of the former partner of the company to his position and ultimately such partner is held liable for the debts of the unfairly liquidated company.

As second selected jurisdiction the thesis analysed the doctrine of piercing the corporate veil in the legal framework of the Republic of Austria. The doctrine of piercing the corporate veil (Durchgriffshaftung)[224] is widely recognized by the Austrian' judiciary, however, its application is restricted only to certain categories such as undercapitalisation of the company, abuse of the corporate structure and factual control over the company. Moreover,

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[223] *Adams v. Cape Industries plc* [1990] Ch 433
[224] OGH, 26 April 2006, Ref. no.: 7 Ob 236/05i

the actual application of the doctrine is rather limited due to its impact on the well-established principles of separate legal personality and limited liability of shareholders in the company. Nota bene, the application of the doctrine is further limited by the need of providing the proof that the activity of the shareholder/partner fulfilled the objective and subjective elements of the actions that could trigger the application of the said doctrine.

The third analyses focused on the doctrine of piercing the corporate veil in the English jurisdiction. The historical development of the doctrine led into creation of so-called categories of action that could trigger the application of the doctrine. Stemming from that, the English' judiciary tend to pierce the corporate veil provided that the partner used the company for fraudulent practices, circumventing tax obligations and using company as an agent of the shareholder/partner. However, it must be added, as the relevant jurisprudence has shown, the practical application of the doctrine is on the decline. The main reasons being the impact of the doctrine on basic principles of the commercial law and the difficulties in proving that the actions of the shareholder/partner amounted to the action that would trigger the application of the doctrine.

Based on the analyses of the three selected jurisdiction, one can observe comparable features of each jurisdiction's application of the doctrine.

The difference stems from the historical legal development of the countries. The Austrian' approach uses the doctrine of piercing the corporate veil that is statutory-based, whereas the English counterpart operates on the case-law developed doctrine of piercing the corporate veil – typical for common law countries. However, similarities may be observed as to application of the doctrine. Both jurisdictions – Austrian and British – apply the doctrine in specific cases that may be divided into specific categories whereas depending on the action of the shareholder (Austrian model) or on the consequences of the action (English model). The completely different application may be observed in the Czech Republic. The Czech' approach uses basic principles of commercial law such as loyalty principle based on which it derives the hybrid form of doctrine of piercing the corporate veil. The peculiarity of the said form of doctrine of piercing the corporate veil rests on the fact, that the doctrine is not explicitly used by the court, however, the actions taken by the court in application of the basic principles of commercial law have a result similar to that of the doctrine of piercing the corporate veil.

Upon examination of the practical application of the doctrine of piercing the corporate veil in the selected jurisdiction, we have derived to following observation. The approach of the Republic of Austria and the United Kingdom creates on one hand categories in which a partner/shareholder may be held liable for the debts of the company which leads into rigid application with increased legal certainty. However, on the other hand, this limits the potential of the doctrine of piercing the corporate veil which in connection with lack of evidence of proof creates applicability limitation of the doctrine. Stemming from that, the practical implementation of the doctrine has limited outreach. The different trend may be observed in the hybrid form of the doctrine as utilized in the Czech Republic. As the judiciaries in the Czech Republic do not operate with specific doctrine in order to hold the partner liable but are using the basic principles of commercial law instead, this allows them to engage in so-called "piercing" in vast array of cases, and thus are not limited to specific categories. On one hand, this enhances the applicability of the doctrine and may in certain cases lead into better protection of creditors. On the other hand, however, it must be noted that the results of application of the doctrine may vary as each and every case comprises of different subjective and objective elements that must be weighted out by the courts. This leads into decrease in legal certainty and may ultimately lead into decrease in protection of creditors.

As such, the conclusion may be drawn that whereas Austrian and English model offer rigid and rather precise rules on the application of the doctrine of piercing the corporate veil, the Czech' hybrid model is rather uncertain in its application. The question of which form of application of the doctrine provides better protection, however, remains to be open.

5 De lege ferenda and final remarks

5.1 De lege ferenda

As we have analysed the implementation of the doctrine of piercing the corporate veil in different jurisdictions, we can now asses the possibility of the application of the said doctrine in the conditions of the Slovak Republic. The criteria that are worth considering are as follows: The Slovak Republic is a civil law country with statutory provision being the fundamental source of law; the judicial system of the Slovak Republic is similar to that of the Czech Republic, based on the mutual historical developments; the Commercial Code and other statutory provision are identical in their principles and core provisions; henceforth the hybrid form of the doctrine of piercing the corporate veil as implemented in the Czech Republic could potentially lead into enhancement of the rights of the creditors in the event of unfair liquidation of the company. Another reason for preferring such approach is the fact, that such implementation may be used on wider scale, i.e. be applicable to variety of cases with different merits. The increased applicability in comparison to restrictive application of English and Austrian judiciary could not only impose repercussions on the perpetrators engaged in unfair liquidation but could also serve as a preventive and deterrent measure. Regardless of the chosen format of the doctrine of piercing the corporate veil, as the analysis of the possible applicability of the doctrine of piercing the corporate veil in the legal framework of the Slovak Republic has shown, we can assess that the implementation of the said doctrine would require much scrutiny in order to be fully compatible with the current legal framework. As such, we are also proposing less invasive measures that could enhance both *ex ante* and *ex post* protection of creditors in the event of an unfair liquidation of the company. In the process of devising the proposed solution we focused on the measure that are not formalistic or bureaucratic burden on the companies and yet increase the protection of the creditors.

At first, we propose the creation of the centralized registry of the business companies, in which one could verify the solvency of the prospective business partner. Nowadays there is an already existing privately owned database of the companies, which is accessible on the website www.finstat.sk. However, as the database in privately owned, its shortcoming is that it relies solely on the data that are publicly available, which are not necessarily up-to-date or precise. Building on that, we are of the view, that if the state created its own, publicly available database which would be interconnected with Financial administration authority of the Slovak Republic, this could lead into database that offers relevant information on every business entity in regard to its solvency and tax discipline.

At second, another measure that could increase the protection of creditors and estop the process of unfair liquidation is the enhancement of communication between the courts administering the business registry and the Financial administration authority of the Slovak Republic. In practice it would work as follows: whenever there would be an application for registering the transfer of shares of the company and/or change in statutory organ of the company in the business registry, the courts could analyse and asses the economic validity of the transaction as tax authority already exercise pursuant to Article 3 par. 6 Tax procedural code of the Slovak Republic.[225] Alternatively, the assessment could be done on the basis of index of tax reliability, which portraits the assessment of the tax subjects based on the fulfilment of their legal obligations towards Financial administration authority. The said assessment and control could lead into prevention of those transfer of shares that raise suspicion of being done with malicious intentions. The subjects of the transfer could liberate themselves from such suspicion by provision of documents and other means of evidence. The exchange of such information could be realized via the database shared between the courts administering business registry and the Financial administration authority of the Slovak Republic. Stemming from that, the security of the information (as some of them may fall within the tax secret) would be ensured and there would be minimal bureaucratic pressure on the companies.

However, it must be added that any measure that as a result limits the transferability of shares of the company represents a significant impact on ownership right, in particular, the right to dispose with one's shares. As such, each and every measure must take into account different aspects of its effect and legislators must carefully draft and balance the rights and obligations stemming from ownership of the shares, so as to provide the business environment that is safe and not overly bureaucratic.

[225] Act No. 563/2009 Coll. on administration of taxes (Tax procedural code) (Zákon o správe daní (daňový poriadok)) [2019] Slovak Republic Article 3(6)

5.2 Final remarks

The aim of the thesis was to analyse and assess whether the legal framework of the Slovak Republic offer sufficient protection of rights of the creditors of the company that has been unfairly liquidated. In particular the main research question rested on the following hypothesis: Does Slovak legal framework, in light with the amendment of the Commercial Code provides the creditors of the unfairly liquidated company any effective protective measures? The subsequent research sub-questions were therefore postulated as follows: Does the amendment of the Commercial Code fulfils its purpose to enhance the protection of creditors? Could the doctrine of piercing the corporate veil be implemented to the Slovak legal order so as to provide better protection of creditors in an event of an unfair liquidation of the company?

As for the main research question, the thorough analysis of the current legal framework could be synthetized into following observation:

The protection of the creditors and their respective claims in the event of an unfair liquidation operates on three different planes depending on the format of the actual unfair liquidation.

First of all, in an event of unfair liquidation via transfer of shares, the creditor is not informed about the upcoming transfer of shares and/or any change in the structure of the debtor/company, and as such, one can only claim his rights *ex post* via challenging the validity of the agreement on transfer of shares. However, even in this scenario there is a legal uncertainty so as to how court would interpret the imperative legal interest on the creditor on the invalidity of the agreement on transfer of shares, and/or how would courts assess the existence of subjective and objective elements for invalidating the agreement itself. Therefore, we are of the view that the legal framework of the Slovak Republic does not offer adequate protective measures for the creditors in respect to commercial aspects of the unfair liquidation realized via transfer of shares.

Second of all, the amendment of Commercial Code effective as of 01.01.2018 implemented measures that are tackling unfair liquidations realized via merger/acquisition.[226] As mentioned in Chapter 3.2 letter c) of the presented thesis, the amendment introduced requirements that the companies must fulfil prior to merger/acquisition. The result of such measures is effectively estoppel to all unfair liquidation realized via merger/acquisition. Therefore, we asses this step of the legislators as the step enhancing the protection of creditors. However, the question must be asked so as to proportionality of the measure as its portraits another bureaucratic burden on all of the companies, even one's engaged in genuine merger/acquisition.

Third of all, the amendment of the Commercial Code introduces the notion of criminal liability for engaging in the unfair liquidation of the company, it does so by creation of new criminal offence of unfair liquidation.[227] However, we are of the view, that the newly introduced criminal offence is redundant and unnecessary, for the following reasons: Firstly, the notion only criminalizes unfair liquidation via transfer of shares and not the unfair liquidation via merger/acquisition. Secondly, the criminal offence only tackles natural person whilst most of the transfer of shares are facilitated by legal persons specialised in commercial law.[228] Thiy, the actual criminal offence serves only as a preventive measure rather than measure protecting the creditors that are affected by the unfair liquidation. As the main commercial aspect of the unfair liquidation is the non-recoverability of the claims of the creditors, we are of the view that the introduced criminal offence does not fulfil any significant protective measure. Furthermore, the redundancy of the criminal offence is supported by the fact, that the actions that lead and portrait unfair liquidation may have criminal repercussion in form of other, already existing criminal offences.

The first research sub-question tackles the effectiveness of the amendment of the Commercial Code in protection of creditors in the event of unfair liquidation. Based on the analysis stipulated in the previous paragraph we can deduce that the amendment of the Commercial code introduces measures that *prima facie* enhance the protection of creditors

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[226] Act No. 87/2015 Coll. amending and extending Act No. 513/1991 Coll. Commercial Code as amended and amending and extending other statutes (Zákon č. 87/2015 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2015] Slovak Republic

[227] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251

[228] P. Šamko, '*The proposal for the introduction of the new criminal offence of unfair liquidation and amendments to the obstructing of insolvency proceedings*' (Návrh na zavedenie nového trestného činu nekalej likvidácia a zmeny v marení konkurzného konania) [2017] 04 Legal letter (Právne listy), 10, 12

as they tackle the abuse of straw-man for the purposes of unfair liquidation. The effectiveness of such measures shall, however, be closely watched as their practical implication, i.e. providing sufficient evidence and proving *actus reus* and *mens rea* in criminal offence of unfair liquidation may render some of the measures ineffective.

The second research sub-question contemplates the applicability of the doctrine of piercing the corporate veil as the effective instrument in enhancement of the rights of the creditors in the event of unfair liquidation. The doctrine in itself offers effective protection of creditors as it makes the shareholder/partner in the company directly liable for the damages/debt to the creditors of the company.

In the assessment of the applicability of the doctrine we focused on the current legal framework of the Slovak Republic, the existing forms of protection of creditors in the event of unfair liquidation and the relevant jurisprudence of the Slovak courts. Upon such examination we have compared the implementation and practical application of the doctrine in selected jurisdictions – the Czech Republic, the Republic of Austria and the United Kingdom. Each of the jurisdiction compared uses different form of the doctrine with differences being either in its legal basis, or to the conditions of its application. The comparative analysis of the selected jurisdiction along with above-mentioned assessment criteria in the Slovak legal order we have derived to the conclusion that the Slovak Republic could potentially introduce the hybrid model of the doctrine of piercing the corporate veil as observed in the Czech Republic. The so-called hybrid model of the doctrine does not operate on its explicit enshrined in the statutory provision or the case law, instead it uses the basic principles of the commercial law which are enshrined in the Commercial law itself and as such, may be used for variety of different cases with different *modus operandi*. The shortcoming of such form however, may be the legal uncertainty and length of the proceedings which would eventually lead into liability of former/current partners in the company. Therefore, we are of the view that the possible application of the doctrine within the legal order of the Slovak Republic shall be subject to much scrutiny and may require substantial legislative changes which are however dependent upon the political will of the national parliament.

6 Conclusion

Even though the unfair liquidation is the term explicitly stated in criminal law, i.e. the term used only in the reference to Penal Code[229], its negative aspects shall not be restricted only to Criminal law itself. On the contrary, the unfair liquidation mainly encompasses negative aspects related to the commercial law. The creditors of the company are the most vulnerable and the most harmed entities in the process of unfair liquidation of the company.

Therefore, the presented master thesis aimed, via the comparative analysis, to asses whether the legal order of the Slovak Republic, and particularly the amendment no. 264/2017 Coll. which amends and updates the Act no. 513/1991 Coll. Commercial Code as amended[230], offers sufficient amount of protection for the creditors of unfairly liquidated company. The thesis has to a certain extend interdisciplinary character as the analysis also assess institutes of the criminal law, namely – newly promulgated criminal offence of unfair liquidation.[231]

The subsequent aim of the thesis was to assess via the process of comparative analysis of different jurisdictions, the possibility of application of the doctrine of piercing the corporate veil as the measure enhancing the protection of creditors of the unfairly liquidated company.

For the purposes of defining the obligations that are circumvented by the unfair liquidation, the first chapter briefly depicted the process of legally approved forms of winding-up and subsequent dissolution of the company in form of liquidation, insolvency or winding-up of the company by legal successor – without liquidation.

The second chapter was dedicated to the actual notion of unfair liquidation in which we derived the notion from its legal definition of the criminal offence of unfair liquidation as enshrined in Article 251b Penal Code.[232] The writing of this chapter has shown however, that from the commercial law perspective, the notion of unfair liquidation cannot be limited

[229] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic
[230] Act No. 87/2015 Coll. amending and extending Act No. 513/1991 Coll. Commercial Code as amended and amending and extending other statutes (Zákon č. 87/2015 Z.z., ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony) [2015] Slovak Republic
[231] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251
[232] Act No. 300/2005 Penal Code (Trestný zákon) [2019] Slovak Republic Article 251b

only to the action as stipulated in the objective and subjective parts of the criminal offence, i.e. only unfair liquidation via transfer of shares. Therefore, for the purposes of the presented thesis the term unfair liquidation shall represent both unfair liquidation via transfer of shares and also unfair liquidation via merger/acquisition. This argument is further supported by the fact that one comes across both forms of circumvention of legally approved forms of winding-up of a company.

The third chapter focused on the instruments that are available to the creditors of the unfairly liquidated company within the context of the legal order of the Slovak Republic. As such we have analysed the possibility of contesting the validity of the agreement on transfer of shares in the relevant jurisprudence of the Slovak judiciary. Furthermore, we have analysed the amendment of the Commercial Code and discussed the possible increase in the protection of creditors via newly introduced innovatory notions and instruments. The two planes of unfair liquidation – via transfer of shares and via merger/acquisition were tackled differently by the legislation. Whilst the transfer of shares is tackled by criminalizing the behavior, the merger/acquisition are rendered impossible by introduction of rigid requirements that must be fulfilled prior to merger/acquisition. This has a result of minimizing the total number of merger/acquisitions and it poses another burden even on genuine business enterprises.

The chapter also contemplates and discusses the possibility of introduction the doctrine of piercing the corporate veil to legal framework of the Slovak Republic.

The fourth chapter forms a main analytical part of the presented thesis as it offers a comparative analysis of the implementation of the doctrine of piercing the corporate veil in three different jurisdictions. As the analysis shown, each country has a different approach to the implementation of the said doctrine which takes into account different legal, social and historical development of the countries compared. The analysed doctrines may be differentiated in three respective forms. The Czech' version of the doctrine resembles a hybrid which is not explicitly enshrined nor in the statutory provisions nor in the jurisprudence but operates on the basic principles of commercial law. The Austrian' form of the doctrine is explicitly enshrined in the statutory provision, but its application is limited to specific cases. The United Kingdom's mutation of the doctrine represents a doctrine that is case-law based, but it is also limited to specific categories of cases.

Building on the findings of chapter four, the fifth chapter offers possible form of the doctrine that could be implemented in the legal order of the Slovak Republic, whilst respecting legal, economic and social tradition of the country – the mutation of the Czech' hybrid doctrine of piercing the corporate veil. Furthermore, the chapter offers alternative measures that could be implemented in order to tackle or to prevent the unfair liquidation and which would subsequently lead into increased protection of creditors such as exchange of information between courts administering business registry and Financial administration authority of the Slovak Republic.

Lastly, the presented thesis is concluded with the final remarks which recapitulate the findings of each chapter with the emphasis placed on the answers to the main research question along with sub-questions.

As it may be observed from the analysis done in the presented thesis, the issue of unfair liquidation and the harm done to the creditors is a delicate issue to solve. On one hand there is a need for administration-free business environment that would benefit the society at-large, on the other hand there is a possibility of abuse of flexible rules. As such, the Damocles sword or ever-lasting conundrum is – to find balance between protecting the creditors of the company, but not limiting the owners of the company, at least not those who pursuit their business activity genuinely.

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