/ Slovakia: Insolvency law (Covid-19)

selected issues

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Restrukturierung & Insolvenz | Bratislava

As many companies now close their premises – either voluntarily such as is the case of some production plants in order to protect their employees (all four largest automotive plants in Slovakia are currently closed) or under an official measure issued by the Chief Health Officer of the Slovak Republic (from 16 March 2020, almost all retail outlets, save for e.g. food retailers and pharmacies, are closed in Slo-vakia) – and thus experience revenue shortfalls, a situation may occur when they will not have sufficient financial reserves to cover short-term closure of business.

Pursuant to the Slovak Commercial Code, a company is in crisis if it is bankrupt or bankruptcy is imminent (i.e. the ratio of its own assets to its liabilities is less than 8 to 100). As soon as managing director finds out that the company is in crisis, he or she is obliged to take all necessary measures in accordance with the re-quirements of professional and due care (Section 67b Commercial Code). This means that the managing director is obliged to summon the supreme body of the company, draw up a proposal of appropriate measures, and to submit such proposal to the body for discussion.

A company in crisis is prohibited to return payments substituting own means (e.g. credit from shareholder) as well as any pertinent accessories (default interest) and contractual penalty. If the company infringes this prohibition and returns the payments to the respective creditors, such payment must be re-paid to the company.

The payment of a share of the profits to the shareholders of a limited liability company is also subject to legal rules. Shareholders can only redeem it or re-allocate other own resources if it does not lead to company's crisis.

Managing directors should therefore monitor the company's current and future financial status, its assets and obligations for them to be able to take timely measures to avert a threat of bankruptcy.

However, where a company is already in crisis, it is necessary to implement measures aimed at either recovery of the business under a restructuring plan (restructuring) or at liquidation of the debtor's assets to satisfy its creditors via insolvency proceedings.

In order for the managing directors to find out whether the debtor is bankrupt, a cash flow test shall be carried out. **A debtor is bankrupt** (Section 3 of Insolvency Act) **when it is insolvent**, i.e. not able to meet at least two payment obligations towards more than one creditor 30 days after respective maturity dates. Following the so called balance sheet test, it might be established that the company **is over-indebted**, i.e. it has more than one creditor and the amount of obligations exceeds the amount of assets (negative equity).

RESPONSIBILITY OF MANAGING DIRECTOR (AND OTHER SUBJECTS) FOR TIMELY INSOLVENCY FILING

When, upon the above tests, the managing director finds out that the company is indeed over-indebted, he or she is obliged to file an **application for insolvency proceedings** within 30 days after he or she has become aware with professional care of the exceeding debt (Section 11 (2) Insolvency Act). The Insolvency Act assumes that a debtor has the best and up-to-date information about its financial standing. If the application is not filed by the debtor, it can be done also by the creditor.

Legal update: Under the adopted law on certain emergency measures in connection with the spread of dangerous contagious human disease COVID-19 dated 25 March 2020, the deadline for filing application for initiation of insolvency proceedings by the debtor is being extended from 30 to 60 days, where the debtor becomes insolvent in the period from 12 March 2020 to 30 April 2020.

WHAT NOW? ALERT FOR MANAGING DIRECTORS

After becoming aware of the company being over-indebted, the company itself – or particularly its managing directors – must take imminent measures. The Insolvency Act provides for a rebuttable presumption of the damages suffered by the creditors in

case the application for initiation of insolvency proceedings is not filed in a timely manner. An untimely filing includes also cases where the insolvency proceeding is not initiated due to lack of debtor's assets or where the proceedings is dismissed due to debtor's insolvency. Enforcement proceedings dismissed due to debtor's insolvency should also be borne in mind as, also in these, persons obliged to file the respective application are held responsible for such non-filing.

The managing director is not held liable in the following cases:

- if he or she has acted with professional care, mainly if he or she could not have met the respective obligation due to other parties' failure to cooperate, whereby he or she has stored a notification in the collection of deeds, immediately after becoming aware of being over-indebted, evidencing the company's over-debt; or
- he or she was appointed as a member of the statutory body during insolvency with the aim to handle the situation, and he or she filed the application for initiation of insolvency proceedings without undue delay after having found out, and while proceeding with professional care, that the adopted measures would not lead to company's recovery; or
- he or she has authorised a trustee within 30 days to execute a restructuring report and to file an application on the basis of which the court approves restructuring measures (note: such authorisation does not relieve the debtor from its obligation to file an application for initiation of insolvency proceedings).

Final court's decision imposing the obligation for a statutory body or other obliged person to compensate damage incurred due to breaching their obligation to file the respective application is also a **decision on expulsion of the managing director** from the company; the expulsion is effective on the date of the effectiveness of the decision. Furthermore, such managing director shall not act as a member of the statutory body or supervisory body in any other company (this shall also apply to acting as the head of a branch of an enterprise, head of a branch of a foreign person's enterprise, proxy holder, and member of supervisory body). If the expulsed managing director does not notify the affected parties about such expulsion and continues in carrying out his or her office, he or she shall be obliged to satisfy its creditors, provided these have not been satisfied by the respective company yet.

Where the application has not been filed timely, internal damage can be caused too (i.e. damage towards the company). For such cases, a contractual penalty is stipulated under the Insolvency Act in an amount corresponding to the amount of one half of the lowest stock capital value in case of a joint stock company. An agreement between a company and obliged person, e.g. managing director, excluding or limiting the entitlement to a contractual penalty is prohibited and cannot be excluded or restricted by Articles of Association either.

The company can neither waive its right to a contractual penalty, nor settle such penalty with the obliged party in any other way (e.g. by means of a settlement agreement). Where the actual damage is higher than the statutory contractual penalty, the creditors are entitled to claim the actual damage exceeding the contractual penalty.

CORONAVIRUS AS STARTING LINE FOR COMPETITIVE RACE?

Creditors are entitled to file for bankruptcy if they can reasonably presume the debtor's insolvency. If the debtor is in delay with paying at least two obligations towards at least two creditors for more than 30 days, and either of the creditors demands for payment in writing, the creditor is entitled to file subsequently the respective application. However, such filing is not an instrument for a competitive race, as the creditor can be held liable for a damage if it becomes apparent that the debtor has not been insolvent and the insolvency proceeding is dismissed due to debtor's solvency.

LIABILITY OF MANAGING DIRECTORS UNDER CRIMINAL LAW

The managing director's liability is covered also in terms of criminal law. By its actions described above (or the non-performance of such actions), the managing director can commit several crimes, even though the criminal-law classification of such actions with a private-law basis should be considered as ultima ratio means having primarily societal significance, i.e. protection of core social values.

The most common offenses committed by managing directors include e.g. violation of obligations in the administration of foreign assets, non-payment of wages and severance pays to employees, various forms of fraud, or creditor detriment. The

2017 amendment of Slovak Criminal Code introduced a new form of criminal offence in this regard, i.e. non-filing of application for initiation of insolvency proceeding by a statutory body and thereby obstructing bankruptcy, settlement proceedings, proceedings on restructuring or proceedings on debt relief (Section 242 Criminal Code).

RECOMMENDATIONS

In the current situation, all companies are urged to monitor closely their liquidity and financial obligations so that they can take early measures if there is threat of bankruptcy. Cessation of business activities and winding-up of company should always be the last resort of how to solve financial issues.

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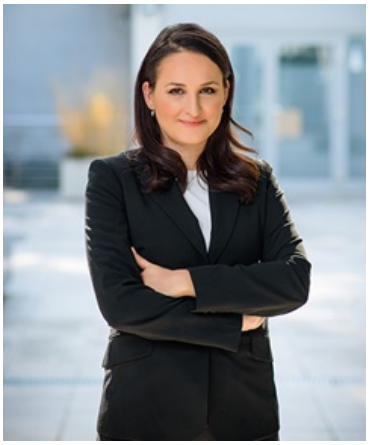

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