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Directors' Duties – Slovakia

Considerations for Directors When a Company Is in Financial Difficulty

This quick guide summarises the duties that directors of companies incorporated in Slovakia are subject to, and how those duties change when the company is insolvent or at risk of being insolvent.

It also gives an overview of the personal risk to directors when the company is in financial difficulty.

This note is intended as an overview and should not be relied on as legal advice. Should you require legal advice in relation to your specific circumstances, please contact the Restructuring & Insolvency team member whose contact details are at the end of this note.

Directors' Duties When Solvent

- Each director has a fiduciary duty to act with the diligence of a prudent businessperson.
- Directors must exercise their duties in compliance with applicable laws, the company's articles of association and bylaws, any instructions issued at shareholder meetings, and the obligations under their agreement.

Financial Distress

Directors' Duties When Insolvent, or at Risk of Being Insolvent

- A company will be bankrupt if it is (a) insolvent, or (b) over-indebted under a "balance sheet test", where it has at least one creditor and the company's liabilities (actual, contingent and prospective) exceed its assets.
- If a company is bankrupt, directors are ordinarily obliged to file for the company's bankruptcy within 30 days of the date the directors knew of the company's over-indebtedness, or when they ought to have known about it, if they were exercising professional care.
- Apart from the above, the company may also find itself within "crisis". The company is in crisis when it is either bankrupt or the company is in danger of going bankrupt, i.e. when the ratio of company's equity to company's liabilities is less than 8 to 100. In such case, the directors are obliged to act with due diligence and do everything to overcome the crisis. The company in crisis has various statutory obligations, including an obligation not to enter into any transaction where the company would provide disproportionate consideration to the company's shareholder.

It is important for directors to understand their directors' duties, as well as how their actions and the decisions the board makes when the company is in financial distress, could expose them to personal liability, criminal sanction and risk.

Below is an overview of the potential claims and potential exposure for directors if the company is insolvent or at risk of insolvency.

Liability to Creditors

If a director fails to file a petition on time, they may be obliged to compensate creditors for the damage suffered by creditors in relation to the creditors' receivables deficit due to insufficient assets at the end of the bankruptcy process, or for a different amount of proved damage.

Obligation to Pay Contractual Penalties

If the petition is not filed on time, the directors will be obliged to pay a contractual penalty of €12,500 into the bankruptcy estate.

Fines

A director must cooperate and assist a bankruptcy trustee. Failure to do so renders a director liable to a fine of up to €165,000.

Disqualification

If a court decides that a director breached the obligation to file for bankruptcy and is, thus, liable for damages, the relevant director will be disqualified from being a member of the statutory body or supervisory body, the head of a branch or a procurist (disqualified representative) for a period of three years from the effective date of the decision.

Criminal Liability

Failure to submit a petition for bankruptcy proceedings in a timely manner may constitute a criminal offence.

Directors may be criminally liable if they do not fulfil their statutory duties. This may result in a prison sentence and/or other punishments available under the Criminal Code.

Preference

If a company is in financial difficulties, directors may be committing a crime if they make preferential payments to creditors.

Practical Tips to Mitigate Liability

- Maintain good lines of communication on a regular basis with suppliers, logistics providers and end customers as to what they are doing and the steps they are taking to mitigate the impact of the virus on the business.
- Agreeing extended payment terms could be considered as a legitimate tool for maintaining the business and avoiding illiquidity of the company. The Slovak Commercial Code allows parties to agree payment terms longer than 60 days only if it is expressly agreed and such payment terms are not grossly unfair to the creditor. Public sector entities can only extend for a maximum of 60 days.
- Consider if the company can pay in instalments.
- Prepare and review short-term and mid-term liquidity forecasts to assess whether the company is illiquid and, therefore, obliged to file for insolvency, and to help determine whether the company can survive the crisis.
- Seek professional advice, if cash flow issues cannot be managed.
- Keep records of key decisions. This will help the directors if the company does not survive and they later have to justify their decisions.
- Consider whether the company can make use of available government support, as not doing so may be considered a failure to act like a prudent businessperson and result in liability (see below for a link to the financial support measures available).
- Directors should consider convening the general meeting to consider appropriate measures to deal with current issues. However, currently, only public joint-stock companies are able to vote remotely and an amendment to the Commercial Code is, therefore, required.
- Directors should avoid preferential treatment of creditors.

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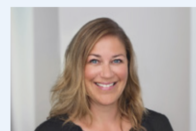

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