Company Law and Law on Cooperatives – General introduction to the topic and definition of basic terms

(Innovative university textbook regarding governing and control of atomistic and polycorporate structures)

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CONTENT

Introduction[1]

The regulation of general questions of companies, individual types of companies and cooperatives can be found in the legal regulations contained mainly in the second part of the Commercial Code. The instruments of incorporation of companies are *lex constractus sui generis* and "non-state normative acts", which are classified as important sources of autonomous law; therefore the question of the nature of the legislation in this section is particularly important. As the Commercial Code does not contain any special regulation, the provision of Section 2(3) of the Civil Code is applicable. The provisions of the second part are then largely imperative within the meaning of that rule with regard to their nature. Those that allow for a different regulation by the wording *"unless the articles of association specify otherwise",* etc. are undoubtedly default provisions. At the same time, the most problematic place for interpreting the nature of the legal regulation of companies and cooperatives will also arise as to the extent to which the coercive provisions of heterogeneous law affect the possibility of the creation of autonomous law by establishing a prohibition of such regulation. In the sphere of private law, it is also appropriate in this context to demand a prohibition and not to seek a permit for autonomous regulation, since in the absence of a prohibition the permit is implicitly given by law. The prohibition of a certain autonomous regulation may result from all "sources" of the legal regulation of relations which are the subject of the Commercial Code, not least from the principles on which the Commercial Code is based.

The principles on which the Commercial Code is based are listed as last in the order of sources of commercial law. Nevertheless, in our opinion, their real significance lies in influencing the interpretation of heterogeneous law and the creation of rules within the framework of autonomous law. These principles should affect the interpretation and application of the law, especially in the case of a loopholes that need to be filled in (completing the law) by analogy, by a logical interpretation (*argument a fortiori*, argument by nature, *argument a contrario*, etc.), through the principle of proportionality, or *largo sensu* (where a legal obligation or authorization is implicitly derived from a legal standard), or in the sense of the constitutional interpretation of simple law, they should also find application within the explicitly expressed norm, e.g., in moderating the interpretation of *senso strictu*, if the grammatical interpretation is in clear contradiction with the fundamental principles of justice. In this way, these principles contribute to resolving the conflict of the incompleteness of the law and the principle of prohibiting *denegationis iustitiae* within the framework of a balanced solution to the legitimacy of judicial law-making, while respecting the limits of normative judiciary activity.

Good morals are a rule of conduct as a result of standards referring to them (i.e. they are not intended to perform the function of an interpretative means but the standard to be applied), but as to the position of interpretative means, these rules are pushed through the principles underpinning the Commercial Code. In this sense, this includes other general principles of private law, in particular, the equality of participants, autonomy of will, contractual freedom,

[1] Based on PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, 2016.

informal expression of will, prohibition of abuse of rights, *pacta sunt servanda* (contracts to be respected), *rebus sic stantibus*, *contra proferentnem*, *venire contra factum proprium* or more specific commercial principles such as fairness in business relationships, professionalism in proceedings, professional decision-making and acting. Company law accepts the principles of contract law, such as good faith, by respecting their contractual nature, and through the Principles of European Contract Law (Article I: 201: 1).

This textbook on company law and cooperative law will present material related to this issue in the context of the above-mentioned general principles as well as principles that can be used to adapt the interpretation of the standards to the current state of development of social relations, both national and European.

Part I. The right to conduct business, definition of the terms "conducting business" and "business owner"

Chapter 1.1 The right to conduct business

The conducting of *business activities* is subject to legislation governing several branches of law. The normative form of *business*, and especially its application level, largely reflects the maturity of any given society and its underlying values. A society whose main source of law states that its economy *"is based on the principles of a socially and environmentally-oriented market economy"* [Article 55(1) of Constitutional Act No. 460/1992 Coll., the Constitution of the Slovak Republic, hereinafter as "The Constitution"] must *"naturally take account of the fact that conducting business cannot be merely a discretion of the private nature of commercial-law regulation – in a democratic country it is a constitutional right to make one's living by freely entering a free market and, with intellectual skill, ensure one's financial well-being." Seen from this point of view, conducting business has become one of the vital priorities of entities with an appropriate level of decision-making power and courage to use what lawmakers have provided as a legislative service to the public. The right to conduct business was thus naturally included in the act of the highest legal authority, specifically in Article 35 as follows: "Everyone has the right to the free choice of profession and to obtain training for it, as well as the right to engage in a business or other gainful activity."*[2] In light of the above, it is crucial (not only for the sake of this publication and the careers of university students) to apply a sensitive approach to the interpretation of the *constitutional right to conduct business*. This means not only providing an interpretation of the actual wording (i.e. who is guaranteed this right and to what extent is it guaranteed), but also understanding its content, inter alia, in relation to the degree of assertiveness that business owners can apply in competition. This is not only due to the wording of the first sentence of Section 55(2) of the Constitution, under which "*the Slovak Republic protects and promotes competition*," but also due to the nature of this publication, which describes corporate law as one of the essential pillars of the business environment. Considering the conciseness of the Constitution (and rightly so), the most authentic sources for interpreting individual articles are the legal opinions contained in the decisions of the Constitutional Court of the Slovak Republic, the Supreme Court of the Slovak Republic, and applicable legal doctrine. As a result, we will now draw attention to the most important legal opinions of this kind, while obviously bearing in mind the scope of this publication.

One of the legal opinions that defines the scope of application of Section 35 of the Constitution and which is often rightfully cited in specialized literature is the ruling of the Constitutional Court of the Slovak Republic dated 27 February 1997, according to which "*the right to conduct business is a constitutional guarantee of the freedom to pursue an economic activity at one's discretion. This right is granted to each person. Through the right to conduct business, the*

[2] MAMOJKA Jr., M. *The Equivalence of the Rights and Obligations of a Member of a Limited Liability Company*, p. 26.

possibility to carry out an economic activity shall be guaranteed wherever competition is present as well as wherever competition is absent. This guarantee does not include the protection of a business owner from the entry of a competitor into the selected economic sphere."[3] The above was specified by the Constitutional Court in further proceedings as follows: *"This guarantee does not include the protection of a business owner from the entry of a competitor into a selected economic activity, nor a guarantee that the business owner will succeed in their activity. In the private interest, the right to conduct business is safeguarded as a means for an individual to make a living. At the same time, this right safeguards the public interest in the development of business as an important element of the market economy*."[4] The concepts, *business owner* and *conduct of business, can therefore be regarded as synonymous with natural individual efforts to assert one's interests vis-a-vis competitors but with an uncertain outcome. By its very nature, the outcome cannot be guaranteed by the state or business owners themselves. The natural selection of "weaker" entities benefits consumers as well as the final contractors. By representing the desire to advance and improve the quality of goods and services with the aim of reaching customers and maximizing profits, it provides a favourable incentive to every business owner. This is embodied in the existential concerns of business owners that stem from fears of personal failure and from the potential failure to deal with business risks, which is even more important considering the place of finances in the present-day world. The reasonable stringency of the Commercial Code (Act No. 513/1991 Coll., the Commercial Code, hereinafter referred to as the "Commercial Code") as the primary representative of commercial regulation is not an uncalled-for fact, but a logical "spokesman" for the natural laws of competition. The Constitution itself recognizes just as clearly the requirements for the formation of competition and the subsequent successful operations of business entities, with the Constitutional Court*[5] *stating that "the basis of a market economy and competition lies in the freedom to enter the market and in equality vis-a-vis the rules governing the behaviour of all competitors on the market. Market entry is part of a Constitution-guaranteed right to conduct business and carry out another gainful activity, as in a market-driven economy it is essential that the right under Article 35(1) be enforced on the market. Market entry is legally ensured via administrative proceedings based on the principle of registration or permission. The principle of registration enables free entry on the market, while the principle of permission has a restrictive nature". As a result, in the initial stage of the creation of one's business plan, the right to conduct business can be linked to making use of the free entry on the market that requires the fulfilment of registration requirements."*[6] Drgonec is of a similar opinion, as he states that *"the purpose of the right to conduct business is not to give such guarantees to all those who want to conduct business. The purpose of the*

[3] Decision of the Constitutional Court of the Slovak Republic, case PL 7/96.
[4] Decision of the Constitutional Court of the Slovak Republic, case I 70/97.
[5] Decision of the Constitutional Court of the Slovak Republic, case I 70/97.
[6] The relatively extensive quotes are due to the previous publications of the author of this chapter, who discussed the definition of the *constitutional right to conduct business* in several of his earlier works. And although long-term scholarly work draws from (among other things) the fact that some views are later revised by their authors, as far as the interpretation of Section 35 of the Constitution is concerned, the author of this chapter maintains the same views concerning interpretation as formulated in his first monograph and believes that the interpretation above has not only retained its relevance, but will also apply *pro futuro* (MAMOJKA Jr., M. *The Equivalence of the Rights and Obligations of a Member of a Limited Liability Company*, p. 26-28).

right to conduct business is to give each person with such right the appropriate opportunity to attempt to conduct business."[7]

Section 35(1) and Section 55(2) of the Constitution together with the case law of the Supreme Court of the Slovak Republic formulate the standard of conduct of business owners in that, drawing on the words of Petr Hajn, the Czech doyen of competition law, in business (especially as regards the right to protection against unfair competition), *"it is not possible to demand a particular grandness of manners. On the contrary, disproportionately stringent requirements for the conduct of competitors would distort competition, as, under Section 41 of the Commercial Code, every business owner has the right to freely pursue their activity in order to achieve financial profit.*"[8] As a result, business owners not only *may* but, considering the financial and legal mechanisms of competition, *must* act with a reasonable degree of assertiveness (not only) when entering into contracts. The exercise of their rights is primarily limited by the so-called *principle of fair business conduct* (Commercial Code Section 265) as a criterion naturally taking into account the nature of the business strategy (i.e. in particular to maximize profits and minimize costs).[9]

Although the aim of this publication is to examine Slovak legislation, let's recall that the constitutional framework of the *right to conduct business* is neither formulated nor interpreted through the autonomous prism of national legislation but, like other fundamental rights, it is part of transnational law-making. In the context of the Treaty on the Functioning of the European Union, *"the right to conduct business (subsumed under the free movement of persons) is also guaranteed by Community-level law, in particular, Article 49 of the Treaty, under which restrictions on the freedom of establishment of nationals of one Member State in the territory of the other Member State are prohibited.*"[10]

Chapter 1.2 Definition of the term 'conducting business'

According to Section 2(1) of the Commercial Code, the term 'conducting business' is defined as: *"a continuous activity that is conducted autonomously by a business owner in his own name and at his own responsibility for the purposes of making a profit or reaching a quantifiable*

[7] DRGONEC, J. *The Constitution of the Slovak Republic. Theory and Application*, p. 770.
[8] Ruling of the Supreme Court of the Slovak Republic, case 3 Obo 141/2007. For an interpretation of relations between *business owners* and *consumers* (not only in the constitutional interpretative framework), see, for example: PETREK, F., KATKOVČIN, M. *The rule of a business owner's judgement in Slovak legal contexts*, p. 224-237; PETREK, F. *On the limitation period in consumer contracts against the backdrop of a derogation ruling of the Constitutional Court of the Slovak Republic*, p. 182-187; JABLONKA, B. *Consumer trades – the fifth type of commercial relationship of obligation as consumer protection in commercial-law relationships*, p. 440-446; SMALIK, M. *The doctrine of the rule of a business owner's judgement in theory and application*, p. 385-392.
[9] For more about refinement of the transparency of activities of businesses in entering into contracts with state authorities, please see, for example, LUKÁČKA, P., PETREK, F. *The register of the public sector's partners and the related obligations of tender bidders*, p. 50-66; MIHÁLIK, S., VINCENT, F., ZIGO, D. *Corruption from the viewpoint of criminal law and criminology and with a focus on public procurement in the Slovak Republic*, p. 106-122; DURAČINSKÁ, J. *The effect of the public procurement process on contracts signed on the basis of the process*, p. 5-22; LACKO, P. *To what extent are entries in the public sector's partner register aligned with reality?*, p. 157-161.
[10] PATAKYOVÁ, M. et al. *Commercial Code. A Commentary*. 5th edition, p. 10.

positive social effect if it concerns an economic activity pursued by a registered social business under a special regulation." For the sake of an interpretation of 'conducting business', let's highlight three core aspects that will be further explained through the prism of legal doctrine and application:

1. The aforementioned provision defines *conducting business* as the *activity of a business owner* that is:
    - *continuous*,
    - conducted *autonomously*,
    - conducted *in one's own name*,
    - conducted *at one's responsibility*, and
    - conducted with the *aim of achieving a profit*.
2. *All* five attributes must be met. Even if only one is not met, the activity cannot be viewed as *conducting business*.
3. This wording is not only contained in the Commercial Code. Almost the same wording has been incorporated into Section 2 of the Trade Licensing Act. This law, however, does not deal with the term *conducting business*, but defines *sole trade* instead – the difference between the two terms will be covered later in this publication or, for wider context, readers may want to refer to the current results of our scholarly work[11].

Ad 1.) The nature of this publication does not allow us to describe all of the implications surrounding the interpretation of *conducting business* available in specialized literature. As a result, we will limit ourselves to a brief examination of the current state of knowledge and compare it with the current application. At this stage, it is also worth pointing out that the order in which the individual characteristics of *conducting business* as an activity of a business owner are listed in Section 2(1) of the Commercial Code does not determine their individual importance (i.e. the term *conducting business* would have the same legal content even if the wording began with the "aim of *achieving a profit*"). Against this backdrop, we do not aim to change the legal state of affairs. In other words, we follow the order in which the characteristics are listed in Section 2(1) of the Commercial Code.

First, to describe an activity as *conducting business*, it must be *continuous*. In the linguistic implication (not only) of this aspect, we stress that it is necessary to interpret its *legal meaning*, as this meaning may not always be consistent with the description provided by the dictionary of Slovak language. In the case of continuity, it means the following: while the literal meaning would imply a *continuous*, i.e. *uninterrupted*, activity, the doctrine is right in noting that continuity "*may not be interpreted restrictively in that it should be an uninterrupted business activity*", because this criterion is also "*met by a seasonal activity or an activity that is conducted for a certain period of time, before being interrupted and resumed again*". *The important fact is that the business owner aims to carry out this activity repeatedly*, which excludes "*an activity that is carried out incidentally, exceptionally or occasionally"*[12].

[11] PATAKYOVÁ, M., MAMOJKA Jr., M., DURAČINSKÁ, J. et al. *Economic Law*, p. 351.
[12] OVEČKOVÁ, O. et al. *Commercial Code. An Extensive Commentary*, p. 55. A similar argument has also been laid out, for example, by a team of authors led by doc. Štenglová, who, in one of their older commentaries to the Commercial Code, stated "*continuity is not equivalent with constancy and persistence. In this respect, the business*

Patakyová rightly notes that "*continuity stems from the business owner's rational expectations of the repetition of this activity, even though they may not carry out the activity with the same intensity at all times.*"[13]

The requirement for continuity is likely to become clearer when we think of examples of activities where it would be objectively impossible (or significantly more difficult) to meet the literal requirements of the law. This includes the operation of an outdoor swimming pool, a ski lift on a natural body of water, an ice skating rink, or the sale of vegetables and fruits grown in Slovakia. The theory isn't isolated in this, because similar interpretations have been adopted by decisions of Slovak and Czech courts – see, for example, the ruling of the Supreme Court of the Czech Republic, file reference, 22 Cdo 679/2007, which cites the theoretical-legal definition of continuity from the commentary on the Commercial Code by Štenglová, Plíva, Toms et al. (the relevant parts in question were quoted below).

Against this backdrop, we will formulate the following definition of continuity as the first criterion[14] of a *business activity* conducted by a business owner: *continuity* is the reasonable expectation of the recurrence of an activity, considering that the frequency of recurrence in each individual case is subject to objective factors, in particular (but not exclusively), to the seasonal character of the activity.

The second feature of a *business activity* is *autonomy*. As in the previous case, it is not appropriate to interpret *autonomy* literally, as this could lead to the conduct of business being seen as completely autonomous and free from the effects of external forces. However, the prisms of theory and case law are different – an activity is conducted autonomously by a person who decides based on their free will (i.e. *individual will* in the case of sole traders, self-employed lawyers, tax advisers, etc.) or their *collective will* (for example, in the case of the adoption of a resolution by the general meeting of a limited liability company of its managing director), provided its will is not subject to instructions from another entity (i.e. another natural or legal person). We realize that the previous sentences use a formal language, much like the case of the explanation of *continuity*; let's also provide the practical aspect: A person conducts business *independently* if they *"decide, within the scope of the law, what products to produce, services to provide, at what price, and so on. The person also decides whether they will carry out this gainful activity by themselves or whether they will employ workers and organize their work."*[15] Specialized Slovak literature[16] defines *autonomy* in a similar way, but we must also

will therefore be operated seasonally or at certain, even if irregular, intervals. However, it cannot be an activity that is carried out incidentally, exceptionally or occasionally. Continuity is to be assessed for each particular case, taking into account the nature of the activity" (ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *The Commercial Code. A Commentary*. 10th substantially expanded edition, p. 6).

13 PATAKYOVÁ, M. et al. *Commercial Code. A Commentary*. 5th edition, p. 11.

14 To reiterate, the order in which the conceptual features of *business* as an *activity* conducted by a business owner are listed is not decisive for the term as such. However, for the sake of interpretation of the individual normative and doctrinal aspects of *conducting business*, we will follow the order in which they appear in the Commercial Code.

15 LAVICKÝ, P. et al. *The Civil Code. I. The General Part (Sections 1-654). A Commentary*. 1st edition, p. 1607.

16 cf., for example, Ovečková's comment that *"autonomy in the conduct of business must be viewed in the sense that the business owner decides on the ways and forms of their business activities and, therefore, is not subordinate*

apply these statements to take into account the 'contractual reality in commercial law' – intact *autonomy* occurs only up to the point when a business owner faces various types of obligations (e.g. obligations arising from a contract, tax obligations and obligations connected to the Trade Licensing Office, the Social Insurance Agency, etc.), which ultimately influence its *decisions.* In other words, a business owner decides on the services that they will provide and the prices for such services, but (e.g.) once a contract is signed, they are bound by obligations that they took on themselves at their own discretion. As a result, once a contract becomes effective, the business owner's freedom to act is limited. A similar effect in business practice is exercised by negotiations with a potential contractual partner (in the pre-contractual stage) who is well-established in the relevant business segment, which results in higher "bargaining power." The natural consequence of such contracting is that the *freedom to decide on the goods, services and prices* of the "weaker negotiator" is reduced because these aspects are usually determined by the "stronger entity."

In order to take the above into account, we will (as in the case of the interpretation of *continuity*) aim at our own definition of *autonomy*, which seeks to combine the core elements of theory while reflecting the basic mechanisms of actual application. The autonomous character of an activity conducted by a business owner represents their free will in the way this activity is conducted, i.e. especially the choice of goods and services to be offered, the prices at which they will be offered, and the contractual partners to be sought out. In doing so, the business owner is not subject to the orders of other natural or legal persons. The scope of the business owner's free decision-making is limited, inter alia, by the obligations to which they are bound on the basis of contractual relationships they have voluntarily entered into, as well as by their obligations *ex lege* (e.g. towards the tax office, the Social Insurance Agency, etc.)

The third feature associated with the *conduct of business activity* is the realization of this activity *in one's own name*. Unlike the previous two requirements, this requirement is clear when it comes to interpretation. Among other things, this is because the Commercial Code contains a relatively complex regulation of the *business name* (i.e. the concept corresponding to the business owner's *own name*). Since, including for the above reason, the business name is extensively interpreted in commentaries, for the purposes of this publication let's focus on the key points: The "business name" is covered by Sections 8 to 12 of the Commercial Code. Under Section 8, *"the business name shall mean the name under which the business owner carries out legal acts while conducting business."* According to the later sections, the formulation of the name of the entrepreneur is simple – the business name of a *natural person* is their *name* and *surname*. The business name thus created may include an addition to the name

to another entity whose orders they have to fulfil (e.g. in an employment contract). The negation of autonomy is not the fulfilment of assumed obligations, or the binding character of clients' orders, etc." (OVEČKOVÁ, O. et al. *Commercial Code. An Extensive Commentary*, p. 55). Suchoža also offers a relatively comprehensive definition of *autonomy* – "*autonomy must be understood both in economic (commercial) and legal terms. The legal aspect consists in the fact that the business owner who conducts a business activity is doing so for someone (or is handing over its results) on a commercial (mainly commercial-contractual) basis and not as part of an employment relationship. The person who carries out such an activity also has their own financial and organizational (e.g. operational) facilities and decides on the concept and further development of the company (business)"* (SUCHOŽA, J. et al. *The Commercial Code and Related Regulations. A Commentary*, p. 52).

and surname that distinguishes the business owner or their form of business[17] (see the first and second sentences of Section 9(1) of the Commercial Code[18]). Therefore, a part of a natural person's business name is predetermined; some creativity only applies to the amendment.[19] By contrast, companies and cooperatives have broader possibilities when it comes to creating their business name, not only as a necessary identifier, but also as part of their set of marketing instruments.[20] This is because the core part of the business name (the so-called *corpus firmae*) of a company or cooperative is subject to only two requirements, which will be explained in the next two paragraphs.

The first requirement involves ensuring that the proposed *core part* of the business name is not *identical* to the business name of a business owner who is already registered in the Commercial Register (the verification of this fact is called the *consultation* of the business name in the electronic version of the Business Register[21]). Thus, if the applicant applies for the registration of an already registered business name, the court maintaining the Register will refuse to make the entry, because, pursuant to Section 7(12), the court verifies whether a proposed name is *identical* to the name of a previously registered business owner. It should be added that the *legal form* of the business is not a distinguishing criterion in this assessment. As a result, if a motion to register the business name "ABC, s.r.o." is filed, the court will refuse the registration even if a company with the business name "ABC, a.s." is already registered in the Commercial Register. We noted earlier that the legal form of business is an obligatory part of the business name of companies and cooperatives and the actual text of the legal form is explicitly limited[22] (e.g. within the meaning of Section 107 of the Commercial Code, the designation of the legal form of a business in the business name of a limited liability company has only three legal alternatives – the full phrasing "limited liability company (s.r.o.)", while the second and third are abbreviations of the same ("spol. s r. o." or "s. r. o.").

[17] e.g. Ján Novák – car mechanic.

[18] Commercial Code Section 8 Subsection 1 reads as follows: *"The business name of an individual shall be the person's name and surname. The business name of an individual may include an addition in order to distinguish the business owner or the type of his or her business.* For more on the issues of legal protection of a business name, see, for example, BARKOCI, S. *Instruments to protect the business name*, p. 71-77.

[19] As mentioned above, we do not intend to complement the available commentaries, so we will only mention that the *addition* to the name and surname of the natural person may be *factual* (e.g. Ján Novák – construction work), *personal* (e.g. John Doe and son), *fancy* (e.g. John Doe – color master) or *mixed* (e.g. John Doe and son – color masters). For greater context, please refer to one of the available commentaries to the Commercial Code [e.g. BOHRNOVÁ, M. *Commentary on Sections 8-12 of the Commercial Code (Business Name)*, p. 13-20; or MAMOJKA Jr., M. *Commentary on Section 107 of the Commercial Code (Business Name of the Limited Liability Company)*, p. 432-435 - both are part of the following publication: MAMOJKA M. et al. *Commercial Code. The Extensive Commentary*.

[20] Section 9 Subsection 2 first and second sentences of the Commercial Code reads as follows: *"The business name of a partnership, company and cooperative shall be the name under which it has been entered in the Commercial Register. The provision above shall also apply to legal entities that are entered in the Commercial Register pursuant to a special act."*

[21] www.orsr.sk

[22] See the third sentence of Section 9 Subsection 2 of the Commercial Code which reads as follows: *"The business name of a legal entity shall also include an addition designating their legal form of business.* In this context, see, for example, the ruling of the Supreme Court of the Slovak Republic, case 5 Obdo 8/1997: *"If the plaintiff is a company or cooperative, the form of business shall be part of the business name [Commercial Code Section 9(2)]. If it is missing from the designation, it must be added. The error shall not be deemed to be an insurmountable obstacle for the proceedings, but as incomplete information that the court can complement (Civil Procedure Code Section 43)."*

The second requirement has to do with the fact that the core part of the business name must be *unique*. However, the potential *confusion* of the name of a company (or cooperative) that is to be entered into the Commercial Register with an already-registered entity *does not* prevent the entry from being made. This has to do with the fact that, as noted earlier, the relevant court only verifies whether the *core part* of the business name is *identical* (i.e. "ABC") with an already registered entity. However, if an already-registered business owner (e.g. "ABC-1, s.r.o.") were to *"justifiably feel (i.e. supported by a justified legal opinion) that the business name of a business owner that was registered later (e.g. "ABC, s.r.o.") can be confused with their own business name, they could – citing the distinctiveness principle – request that the court order the subsequently registered business owner to change their business name so that it can no longer be confused with the business name of the previously registered entity."*[23]

While interpreting the previous characteristics of a business activity (i.e. continuity and autonomy) we have formulated our own definition of the aspects under review. In this case, we will only quote Ovečková: *"A business owner conducts business in their own name as long as they do not act on behalf of someone else. It is not necessary to conduct business in person, but the person acting on their behalf (deputy) must act in the name of the business owner. A business owner conducts business in their own name when they conduct business under the business name within the meaning of Section 8 of the Commercial Code . ... An activity carried out on their own behalf, thus a business activity, is also deemed to be an activity under a contract of mandate or agency contract."*[24] It should only be added that other types of contracts (innominate contracts) in which the element of *direct representation* is included also allow for acting on behalf of a business owner (i.e. it is not necessarily only a mandate contract or an agency contract).

The fourth characteristic of a *business activity* involves *under one's own responsibility*. The following brief description may somewhat disrupt the usual order of a legal interpretation (i.e. starting from legal theory to practical elements), but in conducting business under one's own responsibility we consider it to be appropriate, because the aspect of legal responsibility is one of the decisive criteria in the mindset of each person's choice of a form through which they will participate in competition[25]. In other words, there is a fundamental difference between whether a person joins a public company as a partner and is liable for the company's liabilities with all of their personal assets or whether the person becomes part of a limited liability company in which they are only liable for the company's obligations up to their unpaid contribution (to the company's registered capital) as recorded in the Commercial Register (i.e. once the capital is

[23] MAMOJKA Jr., M. In: PATAKYOVÁ, M., MAMOJKA Jr., M., DURAČINSKÁ, J. et al. *Economic Law*, p. 50.
[24] OVEČOVÁ, O. et al. *Commercial Code. An Extensive Commentary*, p. 55.
[25] For an interpretation of competition law and its overlap in interpretation in criminal law, see, for example, the publications of Jana Strémy [STRÉMY, J . *Private-law means of consumer protection against unfair competition*, p. 217-238; STRÉMY, J. In: PATAKYOVÁ, M., MAMOJKA Jr., M., DURAČINSKÁ, J. et al. *Economic Law*, p. 243-351; STRÉMY, J., TURAY, L. *Selected aspects of liability in corporate environments in the context of commercial and criminal law*, p. 52-74].

paid up in full, the person is no longer liable for the company's obligations[26]). As a result of these natural considerations vis-a-vis the calculation of *risks to one's personal assets*[27] before conducting business, a limited liability company is by far the most widely used (in almost 97% of cases[28]) form of business (not only) in the Slovak Republic. This is not to say that various companies and cooperatives hold *differing* degrees of *legal liability*. On the contrary – each company and cooperative is responsible for its liabilities with *all of its assets*, but the scope of liability of company members (or shareholders) for the company's obligations is different. This is a crucial factor in the choice of the form of business in which the company member (or shareholder) will participate by exercising their rights (i.e. the right to information, the right to participate in profits, the right to participate in decision-making on the company's affairs[29]).

As indicated, the previous paragraph, it is a deliberate 'bridge' to legal doctrine – e.g. according to Ovečková, *"a business activity is carried out by a business owner under their own responsibility when no one else is responsible for their conduct of business. ...* This means that *a business owner's conduct is binding on that business owner themselves*, while *"their own responsibility involves a business risk"*[30]. According to Lasák, however, the conventional theoretical view *"does not rule out the possibility that the business activity is based on acting on behalf of someone else (e.g. a commission agent[31]). In that case, the commission agent acts on behalf of the principal but fulfils the conditions of a business activity (profits are usually a commission or fee for storing items in an operating facility and the like)*.[32]*"*

The last feature of an *activity* which, together with all of the above elements, complements the legal definition of *conduct of business* is the pursuit of that activity *with the aim of achieving a profit*. This criterion is based on a natural psychological and legal presumption, because, unlike the previous characteristics that constitute the *conduct of business*, this *aim* cannot be

[26] The explanation of liability mechanisms is formulated in other parts of this publication, so we will not discuss this in more detail in this chapter. Still, it is worth noting that *"legislation distinguishes between legal relationships involving primary liability (which result in the primary and unlimited liability of a company) versus the so-called liability of legal relationships that result in the secondary and limited legal liability of the partners for a company's obligations",* MAMOJKA Jr., M. In: MAMOJKA, M. et al. *Commercial Code. The Extensive Commentary*, p. 425-432.

[27] Above, we use the phrasing *risks to assets* rather than *business risk*, because, for example, under one ruling of the Supreme Court of the Slovak Republic, case 5 Cdo 109/03, participation itself in the membership/shareholder structure of a company *is not* an activity constituting the *conduct of business* but merely an arrangement with its own assets. Readers should be aware of the broader perception of *risks to assets*, i.e. not only as a risk that arises from a full-fledged *business* activity, but also as a risk arising from a *non-business* liability relationship (i.e. the liability for the obligations of a company in which a natural or legal person has the status of member or shareholder).

[28] based on data from the Statistical Office of the Slovak Republic as of the end of 2018 that summed up all four legal forms of companies (i.e. excluding the private limited company).

[29] An interpretation of the rights and obligations of members (or shareholders) of companies is outlined in other chapters of this publication.

[30] OVEČKOVÁ, O. et al. *Commercial Code. An Extensive Commentary*, p. 56.

[31] Lasák uses an example of a commission agent operating a second-hand shop, but for the purpose of this publication we will use examples that are more tangible and closer to actual application – e.g. an auction company acting as a commission agent in the sale of a work of art, or a bookstore acting as a commission agent in the sale of books.

[32] LASÁK, J. In: LAVICKÝ, P. et al. *The Civil Code. I. The General Part (Sections 1-654). A Commentary*. 1st edition, p. 1607.

demonstrated on the day on which the *activity* is commenced. This is mainly because the *pursuit of profit* – even if it is based on actual business efforts, a thought-out business strategy etc. – may not necessarily lead to favourable financial results. From the legislative point of view, the key is the *intent* to make a profit and not to *actually achieve it*. This is also why we believe that although this feature may be meaningful for the definition of conducting business from the viewpoint of legal theory, its actual application may be different.

Ad 2.) In the previous text, we emphasized that for a particular activity to be considered a *business activity* under Section 2(1) of the Commercial Code, all five requirements must be fulfilled. This requirement has applied both in legislative and interpretative contexts; in other words, the provision has not changed since the Commercial Code was adopted on 5 November, 1991. Although the aim of this publication is not to provide broad-ranging comparative legal research, we include two footnotes that reference provisions *indirectly*[33] regulating the conceptual characteristics of the *conduct of business* in the Czech Civil Code (Act No. 89/2012 Coll., the Civil Code),[34] and we will leave it to each reader to assess which wording is more suitable – that of the Federal Czechoslovak Commercial Code (i.e. the Code that remains in force in the Slovak Republic) or that of the new Czech Civil Code, or that there is no significant normative or interpretative difference between them.

Ad 3.) The wording of Section 2(1) of the Commercial Code appears, almost verbatim, in Section 2 of the Trade Licensing Act, except, as we have already stressed, the Commercial Code does not define a *business activity* but a *trade*. Against this backdrop, we do not aim to repeat the same points from our previous publications that dealt with legal issues, including the issue of trade licensing,[35] so we will only explain the fundamental differences between the aforementioned provisions. Essentially, the difference is that the Trade Licensing Act regulates a narrower scope of business activities than the Commercial Code. The theorem holds that all *sole trades* are *business activities*, but not all *business activities* are *sole trades*. This is partly because in addition to the so-called *positive definition of sole trade* (contained in Section 2 of the Trade Licensing Act), the same body of law also includes the so-called *negative definition* (Section 3 of the Trade Licensing Act). In other words, the Act defines activities for which obtaining a trade license is impossible (e.g. *liberal professions* such as lawyer, distraint officer or auditor; as well as other activities, including alternative medicine, sporting activities subject to a special regulation and others).

[33] The provision of the Czech Civil Code describes *conduct of business* only indirectly, as it does not define the business but its entrepreneur through its traditional legislative features (see the following footnote).
[34] Section 420, Subsection 1, the Czech Commercial Code reads: as follows: *"Whoever carries out a gainful activity independently and on their own account and responsibility as a sole trader or in similar capacity, and aims to do so continually for the purpose of making a profit, is, with respect to this activity, considered to be a business owner."*
[35] LUKÁČKA, P. In: PATAKYOVÁ, M., MAMOJKA Jr., M., DURAČINSKÁ, J. et al. *Economic Law*, p. 351.

Chapter 1.3 Definition of the term 'business owner'

While the definition of *conducting business* relies on the fulfilment of five attributes, i.e. it is a set of actions (*continuity* and *independence*), formal legal requirements (acting in *one's own name* and *under one's own responsibility*) and the psychological-legal mindset of the business owner (acting with *the aim of achieving profits*), the definition of business owner is created on a more austere normative and interpretative basis. According to the wording of the Commercial Code, a *business owner* must carry out one of the four alternative registration procedures, the result of which is considered in Section 2(2)of the Commercial Code . This is in part why legal doctrine designates all forms of business that can be included in the aforementioned provisions as *formal business owners*.[36] The *status of business owner* always applies to a "*person registered in the Commercial Register*,"[37] the Trade Register or another list or register (i.e. particularly in the list of a professional chamber that associates a liberal profession or in the lists of municipal offices in the case of people operating a business in agriculture). Since the entry in a register or list is only a *formal procedure*, it is immaterial (this time only paraphrasing Lasák) whether the person actually conducting the business and their registration is voluntary or mandatory. This involves a rebuttable presumption that these persons are *business owners*,[38] i.e. it is irrelevant whether they actively pursue an *activity* that meets the conceptual characteristics of the *conduct of business*.

Section 2(2) of the Commercial Code foreshadows the following concise interpretation, i.e. under the relevant provisions of the Commercial Code a *business owner* is:

1. *a person listed in the Commercial Register* [Section 2(2)(a) of the Commercial Code]: the provision in question may only be interpreted in conjunction with Sections 27(2)(a), (b) and (c) of the Commercial Code that define persons to be entered in the Commercial Register. Given that this is a comprehensible definition, let's only quote the wording in the footnote.[39] Readers will obtain a more accurate picture by dint of a few practical examples: letter (a) of the provision under examination covers all five legal forms of companies (i.e. general partnership, limited partnership, limited liability company, joint

[36] For more on the phrase 'formal business owners', see, for example, PATAKYOVÁ, M. et al. *The Commercial Code. A Commentary*. 5th edition, p. 12, also LASÁK, J. In: LAVICKÝ, P. et al. *The Civil Code. I. The General Part (Sections 1-654). A Commentary*. 1st edition, p. 1610-1611.

[37] The opinion quoted above relates to the interpretation of Section 421 of the Czech Civil Code, and therefore Lasák interprets *formal business owners* only in relation to entities registered in the Commercial Register. In the text above, however, in line with the current wording of the Section 2 Subsection 2 of the Commercial Code, we extend this interpretation to other registers, lists and records (i.e. particularly the Trade Register, lists of professional chambers that bring together liberal professions or the lists of municipal offices in the case of people operating a business in agriculture). – see LASÁK, J. In: LAVICKÝ, P. et al. *The Civil Code. I. The General Part (Sections 1-654). A Commentary*. 1st edition, p. 1610-1611.

[38] LASÁK, J. In: LAVICKÝ, P. et al. *The Civil Code. I. The General Part (Sections 1-654). A Commentary*. 1st edition, p. 1610-1612

[39] Section 27 Subsection 2 of the Commercial Code reads as follows: *"The following entities shall be entered in the Commercial Register: (a) companies, cooperatives and other legal persons stipulated by a separate law, legal persons established under European Union law, businesses and organizational units of businesses owned by foreign nationals, (b) branches and other organizational units of businesses, if so stipulated by a separate law, (c) natural persons who have a permanent residence in the Slovak Republic and act in the capacity of business owners are entered into the Commercial Register only at their own request or if so stipulated by a special law (hereinafter as "listed person")."*

stock company and private limited company[40]) and a cooperative, a European company[41] (i.e. a person incorporated under European Union law), and also includes legal entities stipulated by a special law (e.g. Radio and Television of Slovakia[42]). Much like Ovečková, we note the paradox of the compulsory registration of companies and organizational units of foreign companies [Section 27(2)(a) of the Commercial Code], and branches and other organizational units of businesses, if so provided by a separate law [Section 27(2)(b) of the Commercial Code]. However, these entities do not have a legal personality, i.e. *"they are not subjects of the law and therefore they are not business owners within the meaning of Section 27(2)(a) of the Commercial Code ."*[43]

2. *a person conducting business on the basis of a trade license* [Section 2(2)(b) of the Commercial Code], as noted earlier when defining the *conduct of business*, sole traders operating their *trade* under Section 2 of the Trade Licencing Act , and the exercise of the *trade* is always viewed as the exercise of an *activity* that represents a *business activity* under Section 2(1) of the Commercial Code, i.e. the Commercial Code considers each *sole trader* to be a *business owner*. In this context, it should be noted that sole traders represent the largest group of business owners in the Slovak Republic. At the end of 2018, more than 300,000 were registered (see the table of the Statistical Office of the Slovak Republic at the end of this subchapter). Among other reasons, this is due to the fact that obtaining a sole trader's licence is less time-consuming as well as cheaper than the formation and incorporation of a company.[44] However, it is worth highlighting a substantial drawback of the legal standing of any sole trader – the liability for their obligations to the full extent of their personal assets). In other words, sole traders run a higher risk to their *business* and *personal assets*[45] than they would if they were members

[40] For selected issues in the application and interpretation of the joint-stock company and for relationships in the interpretation of this form of business and a private limited company, see publications of Angelika Mašurová, e.g. MAŠUROVÁ, A. *The liability of members of statutory bodies, de facto members of statutory bodies and shadow members of statutory bodies towards creditors under new regulations in the Commercial Code and the Act on Bankruptcy and Restructuring,* p. 169-181; MAŠUROVÁ, A. *The locus standi of a shareholder in the filing of a motion to invalidate a decision of the general meeting in light of current case law of the Constitutional Court of the Slovak Republic and the Supreme Court of the Slovak Republic*, p. 139-147; MAŠUROVÁ, A. *Separate arrangements to the shareholder's agreement in a private limited company*, p. 62-93.

[41] For selected issues concerning the establishment of a European company (Societas Europea), see, for example, HAJNIŠOVÁ, E., FULLOVÁ, M. *The formation and incorporation of a European company*, p. 200-204.

[42] Previously, the National Property Fund of the Slovak Republic was frequently used as an example of a legal entity registered in the Commercial Register pursuant to the provisions of a special law, but this authority was voluntarily removed as of 21 January 2016.

[43] OVEČKOVÁ, O. et al. *Commercial Code. An Extensive Commentary*, p. 57 and 58.

[44] For some aspects of the overlap of corporate law into financial and legal contexts, please refer to GRAMBLIČKOVÁ, B. *A company in a crisis – the impact on the distribution of profits or its own resources*, p. 253-260; GRAMBLIČKOVÁ, B. *Regulations governing the funding of capital-based companies through capital funds following the amendment to the Commercial Code No. 264/2017 Coll*., p. 150-156; GRAMBLIČKOVÁ, B., KAČALJAK, M. *The tightening of rules protecting creditors of Slovak companies against the backdrop of the EU's fundamental freedoms,* p. 1593-1607; PATAKYOVÁ, M., GRAMBLIČKOVÁ, B., MAZÚR, J., DUTKOVÁ, P. *Specificities of corporate governance and the financial regulation of companies under the challenges of sustainability*, 89 p. Available online at: (https://www.flaw.uniba.sk/fileadmin/praf/Pracoviska/Katedry/KOPHP/rozne/Specificities_of_Corporate_Governance_and_Financial_Regulation_of_Companies_under_the_Challenges_of_Sustainability.pdf)

[45] Here, too, it should be noted that we need to distinguish between *business* risks and risks to one's *assets*, as the involvement itself in a membership or shareholding structure does not constitute the conduct of business, but

of a limited liability company. For a more detailed interpretation of the legal standing of sole traders, readers may want to refer to our earlier publications that examined the Trade Licensing Act against the backdrop of regulations that fall within *economic law*.[46]

3. *a person conducting business pursuant to a licence other than a trade license in line with special regulations* [Section 2(2)(c) of the Commercial Code]: earlier, we touched on so-called *liberal professions*. The conduct of a liberal profession constitutes the conduct of business, and the licence to carry out business activities is normally obtained by being included in the relevant register (e.g. a lawyer is listed in the register of the Slovak Bar Association, a distraint officer is listed in the register of the Slovak Chamber of Distraint Officers, an auditor is listed in the register of the Slovak Auditors Chamber). In these cases, too, the above holds true; as soon as the person concerned is entered in the register of the pertinent professional association, they become business owners under Section 2(2) of the Commercial Code .

4. a person who is engaged in agricultural production and registered under a special regulation [Section 2(2)(d) of the Commercial Code]: these cases involve the smallest amount of paperwork, where, as opposed to previous cases, their licence to carry out a business is conditional on being included in a particular register of a municipal office under Act No. 105/1990 Coll. on operating a private business by citizens. In other words, they do not have to comply with criteria set by the Commercial Code, the Trade Licensing Act or the rules of professional associations. Patakyová rightly draws attention to a particular group of people who are subject to a different legal arrangement[47] but may be included here by mistake. In other words, they are not business owners under Section 2(2) of the Commercial Code .

merely an arrangement involving one's assets (see, for example, decision of the Supreme Court of the Slovak Republic, case 5 Cdo 109/03).

[46] LUKÁČKA P. In: PATAKYOVÁ, M., MAMOJKA Jr., M., DURAČINSKÁ, J. et al. *Economic Law*, 351 p.

[47] Natural persons who sell unprocessed or processed products from the soil and stock farming from their own agricultural or farming activities, as well as the sale of forest fruits, are not subject to the registration requirement under Act No. 105/1990 Coll. on operating a private business by citizens, and this activity is not a sole trade under the Trade Licensing Act or the Commercial Code. PATAKYOVÁ, M. et al. *Commercial Code. A Commentary*. 5th edition, p. 12).

Legal entities in the Slovak Republic between 2015-2018:

Legal form	2015	2016	2017	2018
Total	546,122	575,102	597,272	596,213
Legal persons	207,655	228,110	248,945	265,835
Companies	183,531	200,104	207,486	217,107
Joint stock companies	5,340	5,516	5,387	5,311
Limited liability companies	176,956	193,300	200,782	210,490
Cooperatives	1,323	1,353	1,367	1,396
Foreign entities	2,670	3,549	4,541	5,875
Non-profit institutions	14,393	17,344	29,479	35,692
Organizations fully funded from the public purse	6,395	6,372	6,366	6,353
Organizations partly funded from the public purse	638	641	663	663
Other non-profit institutions	7,360	10,331	22,450	28,676
Natural persons – business owners (in total)	338,467	346,992	348,327	330,378
Sole traders	316,460	322,968	323,948	303,961

Source: The Statistical Office of the Slovak Republic, DATAcube database.[48]

Revision questions:

1. *Provide an interpretation of the right to conduct business within the context of Section 35 of the Constitution and legal opinions in decisions of the Constitutional Court of the Slovak Republic.*
2. *Provide an interpretation of the normative, case-law and doctrinal characteristics of an activity that constitutes the conduct of business.*
3. *Explain the differences in wording and interpretation between the definition of the conduct of business under Section 2(1)of the Commercial Code and that of a sole trade under Section 2 of the Trade Licensing Act.*
4. *Compare the definition of the conduct of business under Section 2(1) of the Commercial Code and that of a business owner under Section 420(1) of the Czech Civil Code.*
5. *Explain the meaning of the phrase formal business owners.*

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[48] The availability of pertinent statistics is one of the advantages of today's scholarly work. Readers may want to refer to the publications of Martin Hamráček, who has examined the relationship between the theory and actual application of conducting a business under a sole trader's licence. Selected statistics were one of the core arguments for the inefficiency of supervisory mechanisms, among others (for example, HAMRÁČEK, M. *Conducting unauthorized business*, p. 91-99).

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Part II. The right to associate as one of the elements of companies and cooperatives

Chapter 2.1 The term associating

The right of free association and assembly is undoubtedly one of the fundamental pillars of any democratic society and a manifestation of a civil society. Civic activities play an irreplaceable role in any democratic society. The year 1989 was an important milestone. It brought about fundamental changes in the emergence of competing political parties (a pluralistic system) and various civil society institutions. Within the framework of civil society building, the so-called third sector[49] was established, which has become a significant spiritual, political and economic force. The constitutional guarantee to form associations covers both formalized associations - legal entities with their own legal personality, as well as informal associations not regulated by the rule of positive law.[50] The right of association is a fundamental right for corporations operating on a personal basis. The democratic establishment and the market economy presume the existence of various societies, associations, unions and companies that are not subject to the state. In addition to legal entities - organizations of persons in our legal environment, we also recognize legal entities - organizations of property, such as foundations, non-investment funds, non-profit organizations, etc. Only by means of a positive law does the state set the basic rules concerning their establishment, creation, organizational structure, governance, cancellation, extinction, etc. According to Prusák, civil society should have autonomy under democratic conditions and be separated from the state, as civic associations are an organic element of a democratic society.[51] According to Černý, the essence of democracy is its ability to solve problems through open discussion.[52]

The right of free association through the feature of organization enables isolated, powerless individuals to change the social reality and influence the exercise of public authority.[53] Unlike other fundamental rights enshrined in the European Convention for the Protection of Human Rights and Fundamental Freedoms, they are subject to the limitations of Art. 10 and 11 of the Convention, which are provided for by law and are necessary in a democratic society for the sake of national security, public security, the prevention of riots or crime, the protection of health or morality or the rights and freedoms of others. This Article shall not preclude the imposition of legal restrictions on the exercise of these rights by members of the armed forces, the police and civil servants. *In genere*, the right to associate freely has its limits set directly in Art. 29 (3) of the Constitution if it is necessary in a democratic society for the security of the

[49] „*On one hand, the state with its state ("governmental") institutions and on the other hand, civil society and its non-state ("non-governmental") institutions. ... Non-state (non-governmental) non-profit institutions represent the so-called third sector. The first sector is reserved for the economy (economy). The second sector represents state power. In the third sector, non-state (non-governmental) non-profit organizations focus mainly on humanitarian and charitable activities, the environment, education and youth, culture and human rights, the development of free and independent media and so on.*" See: PRUSÁK, J. *Teória práva*, p. 173 *et seq*.
[50] PATAKYOVÁ, M. In: PATAKYOVÁ M., MAMOJKA M. DURAČINSKÁ J. *Hospodárske právo*, p. 25
[51] PRUSÁK, J. *Teória práva*, p. 50.
[52] ČERNÝ, P. LEHKÁ, M. *Zákon o právu shromažďovacím . Komentář*. 1st edition, p. 14.
[53] STEIN, E. *Staatsrecht. 13. neubearbeitete Auflage*, p. 126.

state, for the protection of public order, for the prevention of crime or for the protection of the rights and freedoms of others.

In one of its findings, the Constitutional Court of the Slovak Republic defined the characteristic features of the constitutionally guaranteed fundamental right of association as follows: "*The constitutional concept of an association or association is an autonomous concept, which corresponds to the concept of the European Court of Human Rights in relation to Art. 11 (1) of the Convention for the Protection of Human Rights and Fundamental Freedoms, which guarantees everyone the right to freedom of association with others (judgment of 29 April 1999 in Chassagnou and Others c. France). The legislature cannot be granted the right to exclude the scope of Art. 29 of the Constitution to entities reviving the protection of the right of association only through the formal legal-type designation of a legal entity."*[54] The Constitutional Court of the Slovak Republic further negatively defined the scope of jurisdiction following Art. 29 of the Constitution in such a way that the formation of companies cannot be considered as an exercise of the "political" right of association within the meaning of Art. 29 (1) of the Constitution, but as an exercise of the basic "economic" right to conduct business and conduct business under Art. 35 (1) of the Constitution.[55] In this context, it is important to clarify the focus of the regulation of business activity, which can be understood in the constitutional framework as the manner and extent (scope) of the regulation (limitation) of the constitutional right to freedom to pursue business and to pursue other gainful activities. In this sense, it is necessary to differentiate and deal with the conflict of public interests between the purpose of regulating a business, which is to limit the eligibility (riskiness) of a particular business, to jeopardize the protected interest and between the purpose of public law, which in this context is an interest in encouraging the emergence of new non-profit associations and the further development of existing non-profit associations.

The political nature of the right of association implies the ambition to participate in the political system. In this sense, the right of association constitutes an important level of the process by which an individual coming from an atomized mass of individual legal entities is integrated into society for the purpose of promoting and transforming one's own will and individual interests to the level of society-wide interests. This process is constitutionally determined in the first instance by freedom of expression (Articles 26 (1) and (2) of the Constitution), by the right of peaceful assembly at the second stage (Article 28 of the Constitution), by the right to associate freely at the third stage (Article 29 (1) of the Constitution) and culminates in the exercise of the right of association in political parties and movements (Article 29 (2) of the Constitution). Freedom of association plays a key role in the outlined process. In the modern

[54] Decision of the Constitutional Court of the Slovak Republic, case PL. ÚS 11/2010-42.
[55] Decision of the Constitutional Court of the Slovak Republic, case PL. ÚS 8/96. Further, in decision of the Constitutional Court of the Slovak Republic, case PL. ÚS 10/08, the court stated that the right to freedom of association does not apply to the establishment of public institutions and associations, such as public law corporations. This is also reflected in the view expressed in case III. ÚS 205/07, according to which Art. 29 Par. 1 of the Constitution prohibits the state, or a public authority from interfering with the freedom of association which belongs to private individuals. In another judgment, case PL. ÚS 10/08, the Constitutional Court stated that the association of churches and religious societies is not a form of exercising the fundamental right to freely associate under Art. 29 of the Constitution, but is subject to Art. 24 Par. 2 of the Constitution.

rule of law, democracy is crucially dependent on it, since it ensures the bridging of the imaginary gap between the state and the individual.

In the historical context, the exercise of the right to associate freely is based on a number of essential features that stabilized in the mid-19th century. It expresses the possibility of natural and legal persons, on the basis of a private initiative, to establish associations, in which they freely associate and by means of which they fulfil their stated objectives. Prusák states that civil society is organized according to interests, and that the organizational units of civil society are institutions (organizations, civic associations) that are created and operate on the basis of the interests of individuals associated with their common interest. The primary purpose of the right of free association is to enable the association of persons and to protect it from undue State interference. The legal order of the Slovak Republic operates with the term association to designate a wide range of entities. The concept of *association* subsumes a number of meanings which must be taken into account when establishing different types of associations, as well as in the exercise and control of their activities. Despite the existing regulation of their legal status, the manner and purpose of their establishment, the conditions of business and many other attributes of their activities, the legislation can still be described as relatively vague. Gajdošová defines associations as private entities with an independent legal personality on a membership basis. The basic determinants include their self-governing character and separation from the state; they are not entrusted with the exercise of public authority and do not have public finances. The members of an association are not responsible for its obligations.[56]

Pursuant to Art. 29 (1) of the Constitution, "*The right of association is guaranteed. Everyone has the right to associate with others in associations, societies or other associations.*"

The right to free association has its own legal regulation in our conditions. The internal division of the right to associate freely as a political right has two bases:

- Section 4 par. 1 of Act No. 85/2005 Coll. on political parties and political movements regulates the rights of citizens to form a party and associate in it and in free competition of political forces to seek the favour of citizens and voters.

- Section 2 of Act No. 83/1990 Coll. on the Association of Citizens as amended (hereinafter referred to as the "Association of Citizens Act") stipulates that citizens may establish associations, companies, unions, movements, clubs and other civic associations as well as trade unions and associations in them. The Act also uses the legislative abbreviation "association".

The sources of the right to associate freely also include the general provisions of Act No. 40/1964 Coll., Civil Code, as amended (hereinafter referred to as the "Civil Code"), which *expressis verbis* regulate two types of associations:

[56]GAJDOŠOVÁ, M. *Združenia a právo slobodne sa združovať*, p.VI (Foreword).

- interest associations of legal persons according to Section 20f et seq. of the Civil Code; and
- de facto associations under an association agreement according to Section 829 et seq. of the Civil Code.

Pursuant to Section 11 let. b) of Act No. 575/2001 Coll. on the organization of government activities and the organization of central state administration, the Ministry of the Interior of the Slovak Republic is the central institution of the state administration for the assembly, association and registration of certain legal entities, and such registers are a practical consequence of its activities.

Individuals has diverse interests (economic, political, cultural, charitable). Organizations of economic interests (based on personnel principle) include private companies and business associations, political parties and civic associations in the field of arts and culture.[57] From a European perspective, the unification of law on the European platform cannot be expected in the near future, because in this area the national approach to the concept of individual forms of legal persons remains. The European Convention for the Protection of Human Rights and Fundamental Freedoms, as well as the case law of the European Court of Human Rights are also unifying.[58]

Chapter 2.2 Subjects of the right to associate freely

It is appropriate to ask whether the right to associate freely belongs only to natural persons or also to legal persons. The doctrinal consensus on the essence of the right to associate freely concludes that it is expedient to also guarantee it to legal persons. The beneficiary of the general right of association is everyone, i.e. both natural and legal persons, irrespective of the citizenship or registered office of the legal person.[59] According to Orosz, the term legal person means a fictitious person, an individual subject of law, which is an organization of persons or property[60] created for a specific purpose. Prusák considers the internal organization, features and purpose to be the basic elements of a legal entity.[61] Legal entities that are subject to registration are established on the date of entry into force of their registration. A typical element of an association is cooperation between natural and legal persons, or personal or economic obligations. Luby *in abstracto* divides legal entities into associations of persons (companies), special-purpose associations of assets (foundations) and special legal entities.[62] It can thus be stated that legal entities are, in particular, associations of persons, special-purpose associations

[57] PRUSÁK, J. *Teória práva*, p. 50.
[58] The final judgment of a decision of the European Court of Human Rights is binding on the state and the state is obliged to enforce it, including the adoption of general and specific measures to prevent similar violations of the Convention by the Slovak Republic. The execution of the judgment also involves the payment of just satisfaction to the complainant. General measures include the publication of a judgment in legal journals or a change in legislation. An example of a specific measure is an order to reopen a case.
[59] PATAKYOVÁ, M. In: PATAKYOVÁ M., MAMOJKA M. DURAČINSKÁ J. *Hospodárske právo.* p. 26
[60] OROSZ, L. *Právnické osoby ako subjekty základných práv a slobôd*, p. 416 – 436.
[61] PRUSÁK, J. *Teória práva*, p. 282.
[62] LUBY, Š. *Základy všeobecného súkromného práva*. 3th edition (reprint), p. 55 *et seq*.

of property, and other persons as required by law. The legislative definition can be found in Section 18 of the Civil Code.

The term society (societas) is discussed in reference to the right to associate freely and we use this terminology mainly with reference to company law. Companies and associations are characterized by a personal feature. It should be noted that companies cannot carry out their business without capitalization; and in order to make a profit they engage in entrepreneurial activity not only because of the personnel feature, but also because of the registered capital, which, pursuant to the provisions of Section 58 of the Commercial Code, is the expression of the sum of monetary and non-monetary contributions of all of the partners in the company. Capital companies create capital *ex lege*. Pursuant to Section 62 para. 1 of the Commercial Code, companies are formed on the date of their registration in the Commercial Register. The data to be registered in the Commercial Register are specified in Section 2 of the Commercial Register Act. Natural and legal persons may establish foundations, non-investment funds and non-profit organizations. Foundations and funds are characterized by a property feature that is dedicated to generally beneficial goals, especially the development of spiritual values, the protection of human rights or other humanitarian goals, the protection and creation of the environment, the preservation of natural values, the protection of cultural monuments, etc. A foundation requires a property feature, which is either movable or immovable property, its internal organization and the purpose for which it was established. The notion of non-profit organizations subsumes organizations of persons; i.e. member organizations with a legal personality, as well as property organizations pursuing a publicly beneficial purpose. The sources of non-profit organizations and various associations are mainly membership fees, donations, revenues from public collections, profits from business activities, revenues from securities etc.

Based on the above explanation, we recognize corporate legal entities (associations under the Act on the Association of Citizens, companies) characterized by a personal element, which, according to the other described conditions, may be subject to protection under Art. 29 of the Constitution and funds (foundations, funds) based on the property feature, which naturally do not enjoy the freedom of association under Art. 29 of the Constitution. The purpose of a foundation is determined by a third party (the founder). This distinguishes it from a corporation whose purpose is determined from within the corporation itself by the common will of the persons in the associated corporation.[63] Non-profit organizations in the Slovak legal environment are located at the interface between corporate and fundamental types of legal entities.

Moreover, the right of association relates not only to natural persons but also to legal persons who may also be members of associations. While the European Convention for the Protection of Human Rights and Fundamental Freedoms does not explicitly confer specific rights and freedoms to legal persons, the provisions of certain articles are in fact applicable to them. Thus, to a certain extent, legal persons may also exercise the right of association. (although they

[63] HERMANN-OTAVSKÝ, E. In: HÁCHA, E. et al. *Slovník veřejného práva československého*, p. 711 – 712.

cannot submit a registration themselves). As previously mentioned, the Act on the Association of Citizens applies to private-law corporations established for purposes other than business purposes, which are separately regulated in the Commercial Code. On the other hand, it cannot be ruled out that companies and cooperatives are private law corporations only established for another purpose. The result of the registration is an individual administrative act, which is not in the form of an administrative decision but a factual registration. The registration of an association is not a license (concession), but only an order of action which examines whether the conditions for the formation of the association have been met.[64]

Chapter 2.3 Framework typology of associations

2.3.1 Association of persons vs. association of property

A starting point regarding associations, which has particular significance in legal practice (especially when establishing an association) and causes considerable problems is the differentiation between an association of persons and an association of property. The essence of an association of "personal corporations" is based on the membership principle, unlike a corporation based on the territorial principle (state, municipality, higher territorial unit), but mainly unlike an association of property, which expresses that the purpose of the association is not to associate persons for a specific purpose but to associate assets (foundations and funds) in the form of the monetary or non-monetary contributions of its founders. Distinguishing associations on a personal and property basis is not the only key feature of associations; more details are provided below.

2.3.2 Association with legal personality and association without legal personality

Legal personality is the ability granted by law to be a holder of rights and legal obligations and to be a subject of legal relations. Our legal order grants legal personality to natural and legal persons under Section 18 of the Civil Code. The legal personality of legal persons must be viewed comprehensively as the capacity to have rights and obligations inherent in the capacity to perform legal acts, which begins with their formation and ends with their termination and is defined depending on the purpose for which the legal person was established. Legal acts on behalf of a legal person are performed by its individual bodies. We distinguish between its passive and active sides. In our conditions, it is necessary to determine whether it is an association of persons with legal personality (an association with legal personality that has the status of a legal person with the capacity to acquire rights and obligations, to act independently and to act outside and bear responsibility for it), or is it an association without this ability, i.e. without legal personality. Associations without legal personality are also referred to as free associations or special-purpose associations of persons (usually pursuing a specific economic

[64] JEMELKA, L., BREŇ, J. *Zákon o sdružování občanů, zákon o právu shromažďovacím, zákon o právu petičním s komentářem*, p. 14 *et seq.*

purpose) established under an association agreement pursuant to the provisions of Sections 829 to 841 of the Civil Code. From the point of view of legal personality, it is irrelevant whether the founders of such an association act under a common designation (Section 10 (4) of the Commercial Code).[65] The Civil Code only generally regulates association agreements.

2.3.3 Private and public associations

We divide associations according to typology on the basis of their origin. Private associations are established on the basis of a unilateral or multilateral act (*ex contractu*). Public-law associations are established on the basis of a generally binding legal regulation (*ex lege*), which also defines other details, such as the name, registered office, bodies, method of their creation (creation), etc. In this context, we consider it important to note that the private status of associations is not affected by the public nature of the activity (purpose) that they fulfil.[66] On the other hand, it is necessary to determine the private-law nature of the foundation by the public-law method of its establishment, i.e. by the registration of the association by the competent authority; for example, the Ministry of Interior of the Slovak Republic is the competent authority for the registration of civic associations and foundations, while the department of general internal administration of the district office in the seat of each region is the competent authority for the registration of interest associations of legal entities or non-profit organizations providing charitable services.[67]

The legal theory of the formation of legal entities, including associations of persons, and the principles of evidence (liberal) and **concession** (permitting).

- the principle of evidence means that the establishment of a legal entity does not require the participation of public authorities, or the official approval or verification of its statutes. The establishment of a trade union organization currently corresponds to the principle of evidence in the Slovak Republic, and shall become a legal entity on the day following the date of receipt of a proposal for its evidence by the Ministry of the Interior.
- concession (permitting) principle - single-phase act. It means that a legal entity (association) will be established only on the basis of an individual administrative act by the competent

[65] Its character is mainly that of a *consortia* which was introduced into the Slovak legal order between 1990 and 1991 by an amendment to Act No. 103/1990 Coll., the Economic Code, as an association of persons for carrying out one or more business cases under an association agreement pursuant to Section 360a of the Economic Code. The current legal order of the Slovak Republic does not regulate a consortium as a special organizational and legal form.

[66] E.g. on the basis of authorization by another law, unless such associations also have (coercive) power.

[67] In this sense, we can also talk about *private association regulation*, which is primarily represented by the Civil Code and *public association regulation*, which is represented by special generally binding regulations regulating the conditions of the establishment, functioning and termination of individual types of special associations, eg. Act No. 83/1990 Coll. on the Association of Citizens, as amended, Act No. 34/2002 Coll. on Foundations and on Amendments to the Civil Code, as amended, Act No. 213/1997 Coll. on Non-Profit Organizations Providing Public Benefit Services, Act No. 147/1997 Coll. on non-investment funds and the amendment to Act No. 207/1996 Coll., of the National Council of the Slovak Republic and so on.

public authority, which, upon request, decides to authorize the establishment and activity of the entity. It is typical for authoritarian regimes.

- registration principle – a two-phase act. Registration is subject to an administrative fee. It is primarily a multilateral private act and subsequently an individual administrative act of a public nature. The Association itself is established by its registration by the Ministry of the Interior on the basis of an application for registration. The registration principle is now also applied in our country.

Given that, according to Černý, the legal regulation of the establishment and operation of basic trade union organizations as legal entities with a justified legal personality contained in the Czech Act on Association of Citizens is "*relatively loose, the statutes must include a provision on how organizational units are created, how its existence is proved and who is the person authorized to act on behalf of the organizational unit (statutory body*".[68]

2.3.4 Business Purpose Associations and Other Purpose Associations

In the case of associations that have a legal personality, we distinguish between associations according to the purpose for which they were founded. The first group includes associations established for the purpose of doing business (e.g. companies) or for another purpose (e.g. satisfying members of the association, public benefit). It should be noted that associations established for purposes other than business may, under certain conditions, engage in business and acquire entrepreneurial status within those intentions; for example, interest associations of legal entities are not business entities, but they may also conduct business as an ancillary activity from which the net profits will be used in full to develop the principal purpose for which the association was founded. Further, under the Foundation Act, a foundation may not conduct business except for leasing real estate and organizing cultural, educational, social or sporting events if it uses its assets more effectively and is in accordance with the public benefit purpose of the Foundation. Even if an association established for a purpose other than doing business carries out an activity that meets the characteristics of a business, it is subject to the conditions and obligations that apply to entities based on such business purpose. Therefore, it is important to understand the terms business and entrepreneur. Some authors point out that it is necessary to differentiate between what can be understood as doing business in a legal sense and an activity which, under the conditions of non-profit associations, is capable of bringing the necessary financial resources for its further development. It is also important to clarify the concept of entrepreneur, especially in terms of assessing the relationship between the regulation of the status of (legal) persons established for the purpose of doing business and for a purpose other than the purpose of doing business, and hence from the point of view of assessing the merits of possible differentiated regulation (effects) that may arise from that different position.

68 ČERNÝ P. *Zákon o sdružovaní občanů – Komentář*, p. 86 *et seq*.

Chapter 2.4 Forms of association

2.4.1 Association without legal personality under an association agreement

According to the Civil Code, several persons may associate to work together to achieve an agreed purpose. However, these associations do not have any rights and obligations unless they are registered in the Commercial Register or in another statutory register. An Association Agreement is governed by the provisions of Sections 829 - 841 of the Civil Code. Pursuant to Section 829 of the Civil Code, two or more natural or legal persons may associate for the purpose of achieving a stated objective, but such an association of persons does not have its own legal personality. In other words, an association agreement under Section 829 of the Civil Code constitutes the legal basis for the formation of an association of persons, but one which does not create a new independent legal entity with its own legal personality. In this way, two or more natural or legal persons may associate.[69]

For the purpose of the effective cooperation of participants in an association we consider it important to stipulate the following elements of an Association Agreement:

- the name of the association;
- a declaration that the participants are legal entities and the agreement does not establish any new legal entity;
- the distribution of income and expenditures in connection with joint business activities;
- the assets provided for the joint business;
- the authorization of the person in charge of accounting for the association;
- the determination of the shares of assets acquired in the joint business; and
- the procedures for making decisions on assets acquired in the joint business.

Based on the essence of the association agreement, it is clear that the legislation does not impose any obligation on the formation of certain bodies of the association. On the other hand, the provisions of Section 830 of the Civil Code impose an obligation on all members of the association to actively participate in the achievement of the established goal, while at the same time authorizing all participants to participate in the decision-making on all issues related to the association. This right to participate in the decision-making on the affairs of the Association is strictly reserved to all participants and the relevant legislation shall be applicable to the Parties; the participants in the association may not agree otherwise and exclude any participant from the decision-making process.[70] In addition, the legal regulation of an association agreement, which differs from the legal regulation of an interest group of legal persons, deals in detail with the issue of equity, namely the regulation of property and its settlement. The relevant provisions of the relevant legislation provide answers to the questions of the state of ownership of the assets provided by the participants of the association for the purpose of achieving the stated objective and to the questions of the ownership of the assets acquired by the joint activity of all

69 Section 829, the Civil Code.
70 Section 836, the Civil Code.

of the participants.[71] The law of the association agreement also lays down rules for the withdrawal and exclusion of a participant from the association, including the issue of property settlement between the participants and the association, even if the participant's participation in the association ends on the basis of an agreement on their withdrawal from the association. Thus, the legislation on association agreements is considerably more specific, detailed and comprehensive compared to the legislation on interest-based associations of legal persons, notwithstanding the comparison with possible legal forms of consortia whose existence is regulated by the Commercial Code. Pursuant to Section 20f of the Civil Code, an association may conduct business (even though it is not a business entity) if it is an interest association of legal persons and if, according to its articles of association, it also conducts business as an ancillary activity (profits to be used in full to develop the main purpose for which the association was founded).

2.4.2 Interest association of legal persons

The provisions of Section 20f - 20j of the Civil Code regulate interest associations of legal persons. Pursuant to the provisions of Section 20f of the Civil Code, an interest group is a special type of legal entity that can be created solely by legal entities to protect their interests or for other purposes. An interest association of legal persons must be established by at least two legal entities, irrespective of their nature, however, natural persons may not be founders, even if they are natural persons as business entities. Legal entities are entities defined in the provisions of Section 18(2) of the Civil Code. We classify them as legal entities of private law and associations of persons, i.e. corporations based on the personal principle. As stated by Gajdošová, from the systematic point of view of its regulation contained in the Civil Code, it is not a business entity, although its economic activity cannot be excluded. It may engage in a variety of activities, including business and gainful activities. However, the legally unspecified purpose of an interest association of legal persons must be in accordance with generally binding legal regulations and may not be contrary to good morals. The activities of such an association may include the satisfaction of the legitimate interests and needs of its founders, and later members, e.g. the coordination of joint activities, professional services, humanitarian objectives, development programs, or the representation of members before state, social and other bodies and institutions. An interest association is based on the membership principle, and its founders or members may be legal entities, including non-entrepreneurs.[72] The provisions regulating an interest association of legal persons cover and set the minimum legal basis for its establishment and functioning, and stipulates only the minimum requirements for the establishment and termination of the interest group, the requirements of its statutes and the question of its responsibilities.[73]

[71] Sections 834 and 835, the Civil Code.
[72] GAJDOŠOVÁ, M. *Združenia a právo slobodne sa združovať*, p.129.
[73] Sections 20f – 20j, Civil Code.

Establishment and formation of an association

The formation of the association has two phases. The first phase is the manifestation of the will of the founders expressed in their efforts to establish an association. The second phase consists of the expression of the will of the state authority (district office in the seat of the region), which grants the established association its legal personality.

There are two ways to set up an association:

- by a foundation agreement concluded by the founders in accordance with the provisions of Section 20g of the Civil Code which must include the statutes approved by the founders, and the designation of the persons authorized to act on behalf of the association (statutory bodies); and
- on the basis of a resolution of the constitutive members' meeting, whose minutes indicate that the association was established, i.e. that the legal persons agreed with the association, the purpose to be achieved by such association, the list of names of the founding members, the registered offices and signatures of the members, and the designation of the persons authorized to act on behalf of the association (statutory bodies) approved by the constitutive meeting,

In addition to the foundation agreement or the minutes of the constitutive members' meeting drawn up in accordance with the provisions of Section 20g of the Civil Code, the following must be submitted in order to register an interest association of legal persons in the register:

- a written application submitted by the person designated by the founders;
- articles of association drawn up in accordance with the provisions of Sections 20h par. 1 and 2 of the Civil Code;
- the identification of the persons authorized to act on behalf of the association - statutory bodies (the identification of persons authorized to act on behalf of the association may also be listed in the memorandum of association or the minutes of the constituent meeting);
- an extract from the business register of founders, the register of non-investment funds, etc.; and
- the application fee.

The statutes must include the name of the association, the registered office, the subject of its activity, the adjustment of property relations, the establishment and termination of membership, the rights and obligations of the members, the organs of the association and their scope, the manner of dissolution of the Association and the disposal of its liquidation balance. The statutes may also contain other facts; for example, membership in an association may be linked to a specific membership fee. The statutes, which must also stipulate their form of amendment, are approved by the founders or the constituent members' meeting. The choice of formation of the association (by contract, resolution establishing the members' meeting) depends on the number of legal persons establishing the association.

Registration is carried out by the departments of general internal administration at the district offices at the seat of the region.[74] The jurisdiction is determined by the registered office of the association. The procedure for the registration of the association commences upon the submission of a written application by the authorized person for this act by the founders or the constitutive members' meeting. An association is established (acquires legal capacity and becomes a legal entity) upon its entry in the Register of Associations.[75]

Due to the vague provisions of the Civil Code, the founders or the members of an interest association are free to set up the mechanism of the association's operation, namely in relation to the issues of the formation of association bodies, their rights and obligations, the decision-making processes and procedures, the property settlement mechanism between the interest association and its members and thus to choose the specific character of the interest association. Taking into account all the above information, the legal regulation of an interest association of legal persons only provides the basic legal framework of the association. The actual nature of the association will depend on the will of its founders or members and, in fact, it may acquire the characteristics of a cooperative or the legal form of a company, such as a limited liability company or a public limited company.

Any change or removal of recorded facts (change of registered office, statutory bodies, etc.) is also recorded in the Association Register. The interest association is obliged to report any changes to the data registered in the register without undue delay to the registry office. This procedure must also be maintained in the event of a change in the data in the articles of association which are not entered in the register. In the event of changes in data in the register, or in the articles of association, the interest association must submit the amendment to the articles of association, or the new wording of the statutes to the registration office.

If all of the capital of an interest association has not passed to the legal successor (as in the case of the merger of the association with another association or the merger of an interest association of legal entities with another interest association of legal entities), liquidation shall be carried out in accordance with the relevant provisions of the Commercial Code. If the association's assets are not transferred to the legal successor, liquidation is required before it is dissolved. The provisions of the Commercial Code on the winding-up of companies (Sections 70 to 75) shall apply accordingly. Pursuant to the provisions of Section 20a (2) of the the Civil Code the association ceases to exist upon its deletion from the register. The manner of dissolution of an association and the disposal of its liquidation balance are determined by its articles of association. According to Section 20h (1) of the Civil Code, the articles of association of the

[74] The Register of Interest Associations of Legal Entities is published on the website of the Public Administration Section of the Ministry of the Interior of the Slovak Republic and on the websites of the relevant authorities.
[75] Association by registration. The decision on registration should take the form of a decision in administrative proceedings. For this reason, it must contain all of the particulars specified in Section 47 of the Act No. 71/1967 Coll. on Administrative Proceedings. The Ministry of the Interior decides on appeals against decisions of the Registry Office. The Registry Office shall announce the formation of the association, its name and registered office to the Regional Administration of the Statistical Office of the Slovak Republic within 10 days from the date of registration.

association must specify its name, registered office and subject of activities, adjustment of property relations, establishment and termination of membership, rights and obligations of members, statutory bodies and their competences, method of dissolution and disposal. Membership in an association may be linked to a specific membership fee. The Civil Code does not specify the issue of the compensatory share of an association member upon the termination of its membership, nor does it refer to other legal regulations in this respect; it only stipulates that the adjustment of property relations, the establishment and termination of membership, and the rights and obligations of the members are contained in the articles of association. On the basis of the above, we believe that the content of the articles of association are decisive in terms of the entitlement of an association member to a compensation share. Based on the fact that an association of legal persons is established for the protection of the interests of its members and the majority of the income is generated by its main tax-free activity, it can be assumed that it is a balanced share of the assets acquired as part of the principal non-taxable activity of the interest association of legal persons and therefore this compensatory interest should be taxable income for a member of that association. The withdrawing member may, in respect of tax expenses, claim an embedded membership contribution to its tax expenditures.

Legal entities that are organizations of persons include associations, companies, unions, movements, clubs and other civic associations, as well as trade unions and employers' organizations.

2.4.3 Non-governmental non-profit organizations

• civic associations, trade unions and employers' organizations (according to the Act on Association of Citizens)
• foundations (according to the Act on Foundations)
• non-investment funds (according to the Act on Non-Investment Funds)
• non-profit organizations providing services of general interest (according to the Act on Non-Profit Organizations Providing Services of General Interest)
• organizations with an international element

In addition to legal entities that are organizations of persons, there are also legal entities that are organizations of property. Typical for this type of association is the property (material) element of its foundations and funds. A non-profit organization is a kind of sui generis entity, an association of persons and property. It contains personnel and property features and may only be based on a publicly or socially beneficial purpose. Even in this form of legal entity, the property feature is relatively strong, but the person of the founder, who has influence over the existence and operation of the non-profit organization, remains. However, the business activities of a civic association should be of a supportive nature for the development of the primary purpose on which it was founded. In order to generate its own resources, a civic association may engage in a secondary activity in relation to the field of achieving its objectives and mission and in accordance with generally binding regulations and statutes. This is *expressis verbis* the secondary character of the business of a civic association in support of its main purpose for which it was originally established. The main task of foundations is to collect

property and redistribute it for public benefit purposes. A foundation may also perform other activities in accordance with its public benefit purposes and the implementation of endowment activities, unless otherwise provided by law. A foundation may not engage in business activities other than operating a charity lottery, leasing property, organizing cultural, educational, social or sporting events if it uses its assets more effectively and is in accordance with its publicly beneficial purpose. A foundation may not conclude a silent partnership agreement, and its assets may not be used to finance the activities of political parties or political movements or for the benefit of a candidate for an elected office. However, it may own shares of a company (similar to a civic association), but it may not use capital for this purpose. The right of a foreign foundation to operate in the territory of the Slovak Republic through an organizational unit, which must be a legal entity with its registered office in the territory of the Slovak Republic, arises as of the date of registration of the organizational unit in the Register. Non-profit organizations operate on the principle of non-profit. The expression of this principle in the definition is particularly important because it distinguishes a non-profit-making organization from business entities that can also provide similar services. The essence of this principle is that a non-profit organization may, in addition to providing services of general interest, carry out, on its own behalf and under its own responsibility, other profit-making activities. Its activity may not directly or indirectly result in material benefits for its founders or employees. A non-profit organization must provide the services of general interest for which it was established.

Effective from 1 January 2019, the Act on the Register of Non-Governmental Non-Profit Organizations introduced a new, unified register of non-governmental non-profit organizations, replacing the existing partial registers and records (foundations, non-investment funds), and no later than 31 December 2020, a new, unified and common register of those legal forms, called the Register of Non-Governmental Non-Profit Organizations, shall be established.

Until the establishment of the Register of Non-Governmental Non-Profit Organizations, data on non-governmental non-profit organizations shall kept in the existing registers, records and lists. The original registers, registers and lists shall be abolished by 31 December 2020 and the data entered therein shall be automatically transferred to the Register of Non-Governmental Non-Profit Organizations without the requirement for their re-registration.

The enrolled entities have the possibility to indicate in the Register of Non-Governmental Non-Profit Organizations the purpose or purposes of the activities to which they are dedicated. The "daughter" units of civic associations with legal personality, so-called "subsidiary" units of civic associations, will also have to be registered in the Register of Non-Governmental Non-Profit Organizations. These subsidiaries have not yet had a register and the new register of NGOs will make their existence more transparent in relation to their parent (founding) organizations.

2.4.4 Legal entities that are registered in the Commercial Register

According to the provisions of Section 27(2) of the Commercial Code the following entities are registered in the Commercial Register:

- companies, cooperatives, other legal entities provided for by a special law, legal entities established under European Union law, enterprises and branches of foreign companies;
- branches and other organizational units of enterprises, if so stipulated by a special law; and
- natural persons with permanent residence in the territory of the Slovak Republic who are entrepreneurs pursuant to this Act and who are registered in the Commercial Register at their own request or if so stipulated by a special law.

In general, it is important for businesses to maintain an environment of healthy competition. It is a place for the establishment and development of commercial relations and forms the basis of the legal and economic environment for the competitiveness of the business environment. Pursuant to Section 41 et seq. of the Commercial Code, natural and legal persons participating in competition, even if they are not entrepreneurs, have the right to freely develop their competitive activity in order to achieve economic benefits and to associate for the performance of this activity; binding competition rules and may not abuse participation in such competition.

2.4.4.1 Commercial companies and cooperatives in the context of the right of association

Although the case law of the Constitutional Court clearly emphasizes the "political"[76] nature of the fundamental right guaranteed by Art. 29 of the Constitution, and thus it does not affect the forms of association which are intrinsically linked to the realization of fundamental rights and freedoms protected by other constitutional articles [freedom of religion and belief (Art. 24 (2) of the Constitution), the fundamental right of establishment (Art. 35 (1) of the Constitution), the right of association to protect its economic and social interests (Art. 37 of the Constitution)], Patakyová emphasizes that, although there is still no consensus on doctrinal or case-law levels on whether the right of association may result in an association in the form of a company or cooperative within the meaning of the Commercial Code, based on the constitutional guarantee of the right of association, it includes the existence of private companies under the law of association.[77] Based on the above, we believe that this extensive conceptual definition of the right to associate under the Constitution also applies to private corporations, such as companies.

[76] *As far as the political nature of the right of association is concerned, it implies the ambition to participate in shaping the political system. In this sense, the right of association constitutes an important level of the process by which an individual from an atomized mass of individual legal entities is integrated into society for the purpose of promoting and transforming one's own will and individual interests to the level of society-wide interests. This process is constitutionally determined in the first instance by freedom of expression (Art. 26 Par. 1 and 2 of the Constitution), by the right of peaceful assembly at the second stage (Art. 28 of the Constitution), by the right to associate freely at the third stage (Art. 29 Par. 1 of the Constitution) and culminates in the exercise of the right of association in political parties and movements (Art. 29 Par. 2 of the Constitution). Freedom of association plays a key role in the outlined process. Democracy is crucially dependent on it in the modern rule of law, as it bridges the imaginary gap between the state and the individual.* See decision of the Constitutional Court of the Slovak Republic, case PL. ÚS 11/2010.

[77] PATAKYOVÁ, M. In: PATAKYOVÁ, M., MAMOJKA, M. DURAČINSKÁ, J. *Hospodárske právo*, p. 26

As previously mentioned, companies with a personal element cannot operate without financial resources and capital. Therefore, they develop their business activities not only thanks to the personal element, but also thanks to their registered capital, which is the sum of monetary and non-monetary contributions of all of its partners. The term society can also be found in the definition of the Latin term *societas*.[78] Knapp is inclined to use the term *societas iuris civilis* for associations created to bring people together for a specific purpose.[79] Havel argues that the foundation of a commercial society can be found in the Roman *societas iuris civilis* as well as in the heritage society (*consortium*).[80] Roman doctrine classifies *societas* among the forms of association and, under Roman law, it had the following features: (i) the contributions of the shareholders, (ii) the specification of the purpose of the formation and (iii) the consent of the partners to its formation.[81] The subject of the contribution in *societas* could be property in the widest possible sense, claims, but also manual work or intellectual activity.[82,83] In the case of *societas*, the contribution became co-owned by all of the partners.[84,85] *Societas* was based on a contractual principle and did not have the form of a separate legal entity.[86] The Roman example of *societas* was also applied to the formation of companies and guilds.[87] In the case of Slovak law, *societas* in the Roman form is mainly mirrored in associations established under Section 829 *et seq.* of the Civil Code, in the case of which no independent legal entity is created,[88] the property brought into the association is co-owned by the members of the association[89] and the contribution may be both intellectual and manual work.[90] Pursuant to Section 221 of the Commercial Code, a cooperative is defined as a community of an unspecified number of persons established for the purpose of doing business or providing for the economic, social or other needs of its members. The establishment and termination of membership of a natural or legal person in a cooperative is regulated by the Commercial Code, while a more detailed

78 GAJDOŠOVÁ, M. *Združenie a právo slobodne sa združovať*, p. 8.
79 KNAPP, V. *O právnických osobách*, p. *980* – 1001.
80 HAVEL, B. *Obchodní korporace ve světle proměn: variace na neuzavřené téma správy obchodních korporací*, p. 44.
81 BARTOŠEK, M. *Encyklopedie římského práva*, p. 297; DOBROVIČ, Ľ. In: ŠULEKOVÁ, Ž., ČOLLÁK, J., ROSTÁŠ, D. (eds.). *Inštitúty práva obchodných spoločností (Verejnoprávne a súkromnoprávne aspekty)*, p. 6.
82 Pursuant to the provisions of Section 59 Subsection 2 of the Commercial Code, work, whether manual or intellectual, or the provision of services as the subject of a non-monetary contribution is excluded as such in the case of a shareholder in a company. However, such a contribution is not excluded for an association formed on the basis of Sections 829 *et seq.* Civil Code (Association Agreement). For questions related to contributions and their limits See: PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. *Capital doctrine in the European Union – a lesson to learn from Finland?;* PATAKYOVÁ, M., GRAMBLIČKOVÁ, B., KISELY, I. *Current changes in the capital doctrine report from the Slovak Republic*.
83 BARTOŠEK, M. *Encyklopedie římského práva*, p. 297; DOBROVIČ, Ľ. In: ŠULEKOVÁ, Ž., ČOLLÁK, J., ROSTÁŠ, D. (eds.). *Inštitúty práva obchodných spoločností (Verejnoprávne a súkromnoprávne aspekty)*, p. 6.
84 An association established on the basis of Sections 829 *et seq.* of the Civil Code (Association Agreement) in the provision of Section 833 of the Civil Code is also covered by this regime.
85 DOBROVIČ, Ľ. In: ŠULEKOVÁ, Ž., ČOLLÁK, J., ROSTÁŠ, D. (eds.). *Inštitúty práva obchodných spoločností (Verejnoprávne a súkromnoprávne aspekty)*, p. 7.
86 DOBROVIČ, Ľ. In: ŠULEKOVÁ, Ž., ČOLLÁK, J., ROSTÁŠ, D. (eds.). *Inštitúty práva obchodných spoločností (Verejnoprávne a súkromnoprávne aspekty)*, p. 7. and HAVEL, B. *Obchodní korporace ve světle proměn: variace na neuzavřené téma správy obchodních korporací*, p. 44.
87 HAVEL, B. *Obchodní korporace ve světle proměn: variace na neuzavřené téma správy obchodních korporací*, p. 45.
88 Section 829 Subsections 2, the Civil Code.
89 Section 833, the Civil Code.
90 Section 831, the Civil Code.

regulation of its membership, establishment and termination is also provided in its articles of association. The statutory methods of termination of membership may not be extended by other reasons in the articles. The status and legal conditions of a state-owned enterprise are regulated by Act No. 111/1990 Coll. on state-owned enterprises as amended (hereinafter referred to as the "State-enterprise Act") and the status and legal conditions of contributory organizations are regulated in Act No. 523/2004 Coll. on budgetary rules of public administration and on amendments to certain acts, as amended. The issue of state-owned enterprises is dealt with by prof. Mamojka, Jr., who positively defines it as a legal entity established under Section 13 of the State Enterprise Act, created under Section 12 of the State Enterprise Act and continues to operate in the legal status of a state enterprise. It is a producer of goods and/or a provider of services under Section 2(2)(a) of the Commercial Code. In the context of the general definition of legal entities in the Civil Code, a state enterprise is a *another entity* provided for by law.[91]

The Commercial Code does not allow for the possibility of changing the legal form of a company to a legal entity other than a company or cooperative; in other words, a company may not change its legal form to that of an interest association of legal entities according to the provisions of Section 20f *et seq.* of the Civil Code or an association according to the Act on the Association of Citizens, which are also legal entities and may have a similar activity (e.g. as in the case of capital companies that do not have to be established solely for business purposes). Such a change may only be achieved if the legal personality of the original legal person, i.e. the person establishing one of the above legal forms and cancelling or terminating the other is not preserved. On the other hand, a number of specific rules, in particular in the field of social security law, allow and even in some cases, under the threat of termination, order the transformation of some specific legal entities, such as supplementary pension insurance companies and state organizations established to provide health care under the Commercial Code.

Revision questions:

1. *Explain the concept of association in a constitutional context.*
2. *Why do civic activities play an irreplaceable role in any democratic society?*
3. *Name the subjects of the right to associate freely.*
4. *What kinds of corporations do we recognize in terms of their elements?*
5. *What types of associations do we recognize in terms of their legal personality?*
6. *Do the organizational units of a civic association have a separate legal personality? Are they subject to registration?*
7. *Explain the difference between the principle of recordkeeping, concession and registration?*
8. *Can a civic association and a foundation carry out business activities? Give specific examples.*

[91] MAMOJKA Jr., M. In: PATAKYOVÁ, M., MAMOJKA, M. DURAČINSKÁ, J. *Hospodárske právo*, p. 41 *et seq.*

9. *Does the law of the Slovak Republic govern the existence and activities of a foreign foundation?*
10. *Can the right of association result in an association in the form of a company and a cooperative within the meaning of the Commercial Code?*

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Part III. Mandatory and default provisions regulating not only business companies[92]

Chapter 3.1 Mandatory and default provisions

The difference between mandatory[93] and default provision lies in the fact that in case of the mandatory provision, the legal entity shall not derogate from such provision, while in case of the default provision, the derogation is allowed.[94] The wording of the provision, Section 263(1) of the Commercial Code, stipulating that: "*Parties may derogate from provisions of this Part of the Act or exclude its individual provisions with the exception of the provisions…*" may be considered as imprecise. The above-cited rule provides for a possibility of the "exclusion" of the individual provisions. It is the used terminology "to exclude" which appears inappropriate or even confusing. This is also confirmed by Knapp. In case of a default provision, there does not have to be the exclusion of such provision, but the parties may also agree on the derogation from the provision as a consequence of which the application of the default provision is excluded. Meaning, the explicit exclusion of the default provision is not a must, but the parties' agreement on the derogation is sufficient.[95]

Default as well as mandatory provisions represent applicable legal provisions of the legislative system. According to Knapp, the mandatory provision binds its addressee to something, while the default provision does not bind anybody to anything.[96] In relation to freedom, particularly the freedom of contract, the mandatory provision limits the freedom of contract and the default provision limits the freedom of contract only hypothetically, whereby they regulate rights and obligations between the parties only in addition or alternatively.[97] A default provision represents a provision of legal act which enables participants of legal relationships to derogate from its regulation based on affirmative expression of their will.[98] The mandatory provision disrespects the human will and does not allow for derogation from this provision with regard to the freedom of contract. On the contrary, the default provision not only respects the human will, but even prefers it, meaning, gives priority to the freedom of contract.[99] Default provisions may

92 Written according to Section 3.2 in PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. *Posudzovanie dohôd medzi zakladateľmi obchodnej spoločnosti v kontexte výkonu súdnej moci.*
93 As *Csach* asserts, it is essential to eliminate the confusion of the concept of a section and a provision which often occurs, whereas a section is only a bearer / medium of the provision and not the provision itself. CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem) (in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 104.
94 KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 4.
95 KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 4.
96 KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 8.
97 FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok,* p. 57 a KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 8.
98 FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 57.
99 FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok,* p. 58.

be regarded as interpretation rules of rights and obligations of participants of legal relationships.[100]

The principle of default provision is, based on Section 2(3) of the Civil Code, one of the fundaments of civil law relationships, whereas the participants of these relationships may regulate, based on the agreement, their mutual rights and obligations differently from the law if the law does not explicitly prohibits the derogation and from the character of act's provision it does not arise that the derogation from the provision is not allowed. This provision, Section 2(3) of the Civil Code, is reflected in the above-mentioned freedom of contract which assumes that the contracting parties will regulate their mutual rights and obligations according to their preferences. This provision of the Civil Code is the core of perceiving the private law as a cluster of default provisions.[101]

The specific provision may be recognized as a default provision with respect to the wording of the provision in most of the cases. The most frequently used phrases defining default provisions are, for instance "*if it was not agreed otherwise*", "*unless from the content of the legal action it does not result otherwise*", "*may derogate from the act*", "*unless it is agreed otherwise*".[102] Default provisions fulfil the following functions: (i) the corrective function, whereby in case that the contracting parties did not regulate a certain question in the agreement differently from the legal regulation, the default regulation will apply; (ii) the interpretative function, whereby default provisions help to interpret the content of the contract if the wording of the contractual provision is unclear or uncertain, the default provision is used as a lead for the interpretation of such contractual provisions; (iii) the preventive function, whereby the default provision determine boundaries of the freedom of contract since as Fekete asserts: "*if the contractual provision evidently or unusually derogates from the default provision to the disadvantage of one of the contracting party, it may be the case of abuse of the individual right or execution of the right which is contrary to good manners under Section 3(1) of the Civil Code*".[103] Interpretative function of default provisions declared by *Knapp*[104] is described in details by *Csach* who reasons that the purpose of default provisions regarding their interpretative function is the following: (i) default provisions help to interpret unclear contractual provision; (ii) at the same time these provisions interpret the content of the contract if the contract is quiet about the specific question, in such case, it is essential to confront the omitted question with default provisions; (iii) the application of default provisions is the most problematic if the contracting parties did not regulate the specific question, however, in such case the application of default provisions may be justified by the argument that if contracting parties had interest on a

[100] FEKETE, I. *Občiansky zákonník, Veľký komentár. I. zväzok,* p. 57.
[101] CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem) (in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 105
[102] CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem)(in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 105 and FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 57.
[103] FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 58.
[104] KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 8.

regulation differing from the default provisions, they would explicitly state so in the contract; and (iv) a specific situation arises in the case when the omitted question is neither regulated by contractual provisions nor by default provisions; in such case analogy may apply.[105]

On the other hand, the mandatory provisions also apply in civil (and therefore private) law with the objective to ensure in specific required cases "*respect for objectively justified interests of third parties or public interests*".[106] The mandatory provisions represent such regulation in case of existence of which it is not possible to apply the freedom of contract, meaning, the contracting parties are not allowed to derogate from its content.[107]

In case that a legal act does not contain the enumeration of mandatory provisions, it is necessary to assess the mandatory or default character of the provision in regard to the context, purpose and meaning of the legal regulation as well as other provisions of the legal act.[108] In case of mandatory provisions we often rely on specific wording of the provision which stipulates clear restriction or order.[109] If it is not possible to unambiguously determine whether the provision is mandatory or default, it is essential to apply the *favor contractus* principle – therefore, to prefer the conclusion that the provision has a default character.[110]

Chapter 3.2 Default and mandatory provisions in the context of commercial law with the focus on company law

In the context of the commercial law, it is necessary to separately address the question of mandatory and default legal provisions.[111] The Commercial Code does not address this question and also does not set any general rule in this context. However, Section 263 of the Commercial Code puts forward that it is possible to derogate from or exclude the application of all provisions of the third part of the Commercial Code, except for those specified here.[112] Patakyová at the same time claims that the enumeration of these mandatory provisions by Section 263 of the

[105] CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (II. časť – rozbor dispozitívnych noriem a vybraných problémov (nielen) Obchodného zákonníka) (in English: Place of default and mandatory provisions (not only) in the company law (Part II – Analysis of default provisions and specific problems (not only) of the Commercial Code)*, p. 248-249.
[106] FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 59.
[107] FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 59.
[108] ŠTEVČEK, M. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 17.
[109] ŠTEVČEK, M. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 17.
[110] FEKETE, I. *Občiansky zákonník: Veľký komentár. I. zväzok*, p. 59.
[111] To see the question about default provisions in the company law in details look at: CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (II. časť – rozbor dispozitívnych noriem a vybraných problémov (nielen) Obchodného zákonníka) (in English: Place of default and mandatory provisions (not only) in the company law (Part II – Analysis of default provisions and specific problems (not only) of the Commercial Code)*.
[112] As it was already stated, according to *Knapp*, the wording "to exclude" used only in Section 263 of the Commercial Code is inappropriate and confusing. Provisions, from which legal entities may deviate or which they may exclude, are default provisions which do not have to be explicitly excluded, whereas legal entities may just deviate from them. KNAPP, V. *O právu kogentním a dispozitivním (a také o právu heterogenním a autonómním) (in English: About mandatory and default law (and also about heterogenous and autonomous law))*, p. 4.

Commercial Code is not definite. According to Patakyová, it is essential to asses other non-enumerated provisions of the third part of the Commercial Code based on the grammatical and systematic interpretation, while at the same time it is necessary to respect unity of the legal order and the separation of power.[113]

From the assessment of the mandatory or default character of legal provisions, the second part of the Commercial Code (regulating general questions of business companies and the cooperative) is more complicated. Corporate documents of business companies and the cooperative represent contracts *sui generis*,[114] and therefore, the core issue is to deal with the question of mandatory or default character of the provisions contained in the second part of the Commercial Code with respect to the identification of limits of the freedom of contract. The corporate documents cause effect not only between the parties to this contract, but they also affect the business company and third parties (bodies of the company) which willingly or unwillingly enter into legal relationships with this company.[115] Due to the fact that the Commercial Code, in contrast with the third part of this act,[116] misses the rule determining mandatory or default character of provisions contained in this second part, Section 2(3) of the Civil Code which sets the general principle of primarily default character of the legal provisions of the private law, shall apply. In case of the Commercial Code and the Czech Commercial Code[117] applicable until the end of 2013, legal provisions of the company law are/were considered primarily as mandatory.[118] Patakyová (partially) agrees with this above-mentioned conclusion, while in this context declares that provisions included in the second part of the Commercial Code are under the rule set by Section 2(3) of the Civil Code considered as imperative, and therefore mandatory, considering the character of these provisions containing individual rules.[119] As a result of this, Patakyová partially corrects the above-mentioned approach and asserts that "*in sphere of the private law it is also adequate in this context to require a restriction, and not to search for permission for autonomous regulation, whereby in case of an absence of restriction, the permission is implicitly given by law and participants of legal relationships may express relevant will praeter legem. I consider it necessary to highlight that the prohibition of certain autonomous regulation may arise from all 'sources' of the legal regulations of relationships which are subject to the Commercial Code and also from principles which the Commercial Code lies on*."[120] Based on this, the question how the provisions of the company law are (or should be) seen should be addressed. Provisions of the company law are (or should be) seen and interpreted from the view of their mandatory or default character. Havel

113 PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 4-5.
114 The character of the articles of association as a contract *sui generis* was also confirmed by Court of Justice of the European Union in case C-214/89 *Powell Duffryn plc v Wolfgang Petereit* from 1992.
115 ŠULEKOVÁ, Ž. *Zmluvná sloboda v korporátnom práve – kde nachádzať jej limity? (in English: Contractual freedom in the corporate law – where to find its limits?)*, p. 274.
116 Section 263, the Commercial Code.
117 Act no. 513/1991 Coll. Commercial Code (the "Czech Commercial Code").
118 ROVONSKÁ, K., HAVEL, B. *Kogentnost úpravy právnických osob a její omezení autonómií vůle, nebo vice versa?(in English: The mandatory character of legal persons regulation and its limitations of autonomous will or vice versa)*, p. 33 and PLÍVA, S. In ŠTENGLOVÁ, I. - PLÍVA, S. – TOMSA, M. et al. *Obchodní zákonník. Komentář. 13th edition*, p. 3.
119 PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 4-5.
120 PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 4-5.

and Ronovská also agree with such approach and declare that to consider provisions of the company law included in the second part of the Czech Commercial Code as mandatory provisions is incorrect and that these provisions should be primarily perceived as default provisions.[121]

Taking into consideration a need to stabilize the mandatory and default character of legal provisions, it is essential to point out the derogation and legal consequences of the derogation from mandatory provisions. As Csach states, it is necessary to differentiate (i) mandatory legal provisions whose infringement causes the invalidity of legal action based on Section 39 of the Civil Code;[122] and (ii) mandatory legal provisions whose infringement does not cause the invalidity of legal action, but it results in the modification of the content of the legal action for the benefit of the mandatory legal provision.[123] It means, in the second case, the mandatory provision will apply instead of the agreed autonomous regulation contrary to the mandatory provision and the implication of the mandatory provision's infringement is not invalidity of the legal action but its modification.[124]

Revision questions:

1. *Define a default provision and determine its functions.*
2. *Define a mandatory provision and determine its functions.*
3. *Characterize how to distinguish the mandatory and default provisions in the first and second parts of the Commercial Code (Sections 1 - 260 of the Commercial Code). When answering, refer to the specific provisions of the Commercial Code and the Civil Code.*
4. *Characterize how to distinguish mandatory and default provisions in the third and fourth parts of the Commercial Code (Sections 261-775 of the Commercial Code). When answering, refer to the specific provisions of the Commercial Code.*

[121] ROVONSKÁ, K., HAVEL, B. *Kogentnost úpravy právnických osob a její omezení autonómií vůle, nebo vice versa? (in English: The mandatory character of legal persons regulation and its limitations of autonomous will or vice versa)*, p. 33.
[122] Also a partial invalidity may occur. CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem) (in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 107.
[123] CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem) (in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 107.
[124] CSACH, K. *Miesto dispozitívnych a kogentných právnych noriem (nielen) v obchodnom práve (I. časť – Všeobecné otázky a rozbor kogentných noriem) (in English: Place of default and mandatory provisions (not only) in the company law (Part I – General questions and mandatory provisions analysis))*, p. 107.

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PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. *Posudzovanie dohôd medzi zakladateľmi obchodnej spoločnosti v kontexte výkonu súdnej moci*, In: Bratislavské právnické fórum 2019, Bratislava: Univerzita Komenského v Bratislave, Právnická fakulta, 2019 (in print).

RONOVSKÁ, K., HAVEL, B. Kogentnost úpravy právnických osob a její omezení autonomií vůle, nebo vice versa? In: *Obchodněprávní revue*, 2016.

Decision of the European Court of Justice, case C-214/89 *Powell Duffryn plc v Wolfgang Petereit*.

ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, Bratislava: C.H. Beck, 2015.

ŠULEKOVÁ, Ž. Zmluvná sloboda v korporátnom práve - kde nachádzať jej limity? In: *Acta Facultatis Iuridicae Universitatis Comenianae*, 2013.

Part IV. Legal personality of companies

Chapter 4.1 Legal personality of a business company

The character of the business company depends on its legal personality which represents one of its basic characteristic features. The legal personality of the business company is separated from its founders and shareholders. According to Kraakman et al., a property autonomy, which ensures the protection of (assets) corporation against claims of company creditors (*entity shielding*), represents the core feature of the legal personality. In other words, the core function of this separate patrimony involves shielding the assets of the entity – corporation – from the creditors or the entity's owners.[125]

The legal personality of the company provides mainly for the following: (i) to enter into relationships of obligations in its own name; (ii) to be an owner of moveable and immovable assets; (iii) to sue and be sued in its own name; (iv) to empower other persons to act in its name.[126] The above-mentioned substantive characteristics of the concept of the legal personality are provided only illustratively and the real character of the legal personality relies on the national legislation of the specific state regulating the company.

Not only legal scholars, but also sociologists, political scientists, and economists analyse the origin of the concept of the legal personality and its basic characteristics.[127] The most significant theories dealing with the essence of the character of the corporation and its legal personality are: *(i) theory of fiction, (ii) theory of contract, and (iii) theory of reality*. Any of these theories gives the answer to all questions about the character of the company, and therefore, the discussion among legal scholars on this issue is still ongoing.[128]

4.1.1 Business company as a fiction (theory of fiction)

The theory of fiction is the oldest one among the existing theories and characterizes the corporation as *persona ficta*. The foundations of this theory are linked with a German theorist of law – Friedrich Carl von Savigny who claimed that legal persons may have only those rights and obligations which are given to them by state. Later on, his assertions largely influenced

[125] The protection of (the property) of the company (*entity shielding*) consists of (i) the right of priority of company creditors if they claim their entitlements against the property of the company, and (ii) the protection against liquidation which constitutes the absence of the possibility that the partner may require the return of his contribution and causes the liquidation of the company. KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 6 and HANSMANN, H – KRAAKMAN, R. *Organizational Law as Asset Partitioning*, p. 390.

[126] KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 8 and SCHANE, S. A. *The Corporation is a Person: The Language of a Legal Fiction*, p. 563 and RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 5.

[127] IWAI, K. *Persons, Things and Corporations: The Corporate Personality Controversy and Comparative Corporate Governance*, p. 583.

[128] For the full analysis see: PATAKYOVÁ, M., CZÓKOLYOVÁ, B. *Teória spoločnosti v triáde rozhodnutí Daily Mail, Cartesio a VALE - spoločnosť ako fikcia, nexus kontraktov alebo reálna osoba? (in English: The theory of the company within the context of Daily Mail, Cartesio, and Vale – the company as a fiction, a nexus of contract, and a real person?).*

legal scholars of the common law legal system.[129] Pursuant to this theory, the corporation is a creation of the legislative, whereby it is the legislative which gives legal personality to the corporation. The fact that the corporation is a fiction, whose existence is created and maintained only due to intervention from the side of the state, is a key characteristic of this theory.[130] Pursuant to this theory, the company is considered as an entity without "*soul and body*"[131] to which the state breathes "*life*" through its legal norms. John Marshall as Chief Justice of the United States in case of *Trustees of Dartmouth College v. Woodward* came up with one of the fundamental definitions of the corporation as *persona ficta*: "*The corporation is an artificial person who is invisible and intangible and exist only through the intervention of the law. Due to the fact that the society is a creation of the law, it has only those attributes which the specific legislative attributes to it.*"[132] According to what was stated above, it may be concluded that the legal personality of the company is limited. The limitation of the legal personality is reflected mainly in the subject of the company's business activity and the related conduct of the company.[133] If the company acts through its statutory body and exceeds the scope of the subject of its business activity, such conduct, pursuant to this theory, would be considered as conduct *ultra vires,*[134] meaning that such conduct would be invalid.[135]

The theory of fiction is supported by the fact that at the beginning of the companies' incorporation, the companies were being incorporated as entities with specific purpose which was usually strictly regulated by the state.[136] As the time passed, the companies stopped being incorporated as privileged entities with specific purpose and its incorporation has become a right. These changes lead to the limitation of the intervention from the state regarding the companies' incorporation as well as the strengthening position of shareholders.[137] Shareholders started to be perceived as the main part of the company forming its fundamental essence. This change of perception of the character of the company resulted in the creation of new theory – the theory of contract.

[129] PETRIN, M. *Reconceptualising the Theory of the Firm – from Nature to Function*, p. 4.
[130] Chapter 1 – What Are Corporation? Available online at: https://www.malcolm.id.au/honours/chap1.html.
[131] SCHANE, S. A. *The Corporation is a Person: The Language of a Legal Fiction*, p. 565.
[132] SCHANE, S. A. *The Corporation is a Person: The Language of a Legal Fiction*, p. 565 and RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 6.
[133] FERRAN, E. *Company Law and Corporate Finance*, p. 9.
[134] Doctrine *ultra vires* declares that the company may act only within the subject of its entrepreneurial activity, because otherwise it is invalid. CSACH, K. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 109.
[135] SCHANE, S. A. *The Corporation is a Person: The Language of a Legal Fiction*, p. 566.
[136] KITCH, E. W. *The Simplification of the Criteria for Good Corporate Law of Why Corporate Law Is Not as Important Anymore*, p. 1.
[137] KITCH, E. W. *The Simplification of the Criteria for Good Corporate Law of Why Corporate Law Is Not as Important Anymore*, s. 1, METZGER, M. B., DALTON, D. R. *Seeing the Elephant: an Organizational Perspective on Corporate Moral Agency*, p. 3 and RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 6.

4.1.2 Business company as a nexus of contracts (theory of contract)

The theory of contract considers the company as a nexus of contracts which are concluded between various entities within the company.[138] The basis of this nexus of contractual relationships is a contract between the company's founders who decided to establish the company.[139] Subsequently, secondary contracts, which includes contracts concluded between: (i) managers and the company to ensure functioning of the company; (ii) employees and the company to ensure workforce for the company; (iii) creditors and the company to ensure external financing of the company; and others, are linked to this contractual relationship of founders of the company. The theory of contract fails to justify the essence of the legal personality's creation which would be differentiated from company's shareholders and ensured the limitation of their liability (the concept of shareholders' limited liability). If we perceive the company as a nexus of contracts, we would not be able to theoretically justify the limited liability of shareholders (the concept of shareholders' liability for obligations of the company).[140] From Ferran's point of view, the benefit of the theory of contract lies in the limitation of state legislature's interference to the law of business companies, whereas the legal regulation of companies is justified only if is inevitable and effective.[141]

4.1.3 Company as a real "being" (theory of reality)

Another theory of company is the theory of reality seeing the company as an entity which is more than a contractual relationship between its shareholders (*nexus of contracts*) and a fiction existing thanks to interference from the state (*persona ficta*).[142] The beginnings of the theory of reality may be dated back to the 19th century, when German historian and academic Otto von Gierke gave his opinion that the company should not be perceived as an artificial but a real person.[143] This theory has become significant with the incorporation of large corporations when the ownership of the company was separated from its management (separation of ownership and control).[144] The separation of ownership and control were conducted by the fact that the partner (shareholder) owns only a small fraction of the company (business share, share) which does not entitle him to effectively govern and control the company, which makes the partner (shareholder) rather a passive investor.[145] The theory of reality undermines the theory of

[138] IWAI, K. *Persons, Things and Corporations: The Corporate Personality Controversy and Comparative Corporate Governance*, p. 585.
[139] RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 6.
[140] PADFIELD, S. J. *Rehabilitating Concession Theory*, p. 5 and FERRAN, E. *Company Law and Corporate Finance*, p. 11.
[141] FERRAN, E. *Company Law and Corporate Finance*, p. 11 and KITCH, E. W. *The Simplification of the Criteria for Good Corporate Law of Why Corporate Law Is Not as Important Anymore.*
[142] Chapter 1 – What Are Corporation? Available online at: https://www.malcolm.id.au/honours/chap1.html and METZGER, M. B., DALTON, D. R. *Seeing the Elephant: an Organizational Perspective on Corporate Moral Agency*, p. 3.
[143] PETRIN, M. *Reconceptualising the Theory of the Firm – from Nature to Function*, p. 4.
[144] For the separation of ownership and control in details see: FAMA, E. F., JENSEN, M. J. *Separation of Ownership and Control.*
[145] RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 7.

contract. The incorporation of companies governed by managers caused the disappearance of the essential link between the company and its partners (shareholders) representing the core of the theory of contract which lead to the emergence of the first delineations that the company is an autonomous person.[146] On the other hand, the theory of reality challenges the theory of fiction by the fact that the state is perceived as an entity which declares the existence of the company, however, it does not actively participate in its incorporation.[147]

The problem of this theory built on the hypothesis that the company is a real person was the demonstration of the company's ability to act individually. This stumbling block was overcome with the argument that the bodies of the company reflect its mind and activity and thus are considered as its "*hands and mouth*".[148] Partners (shareholders) of the company are, according to this theory, perceived more like investors and residual owners of the company than persons who would oversee day-to-day running of the company.[149] The declaration of the existence of the company as a "living" person moves the perception of the company as an entity oriented only on partners (shareholder) to the entity oriented also on other stakeholders of the company – employees, creditors and others.[150] The above stated arguments justify the conclusion that statutory bodies of companies have to conduct their activities with professional care not only towards companies' partners (shareholders), but also towards other entities linked with the company, and therefore, this theory also attributes a moral responsibility to the company.[151]

Challenges of the company law lying in questions of the social responsibility and the sustainable development plead in favour of the theory of reality, whereas, from the point of view of these concepts, the company is seen as an entity targeted to and liable not only towards its partners (shareholders) as residual owners, but also towards a wider circle of entities existing within or out of the society.

Traces of the inclination to the theory of reality in regard to the character of the companies may be also found in the decision of the Court of European Union in case C-378/10 *VALE Építségi Kft.*, (2012).[152]

146 METZGER, M. B., DALTON, D. R. *Seeing the Elephant: an Organizational Perspective on Corporate Moral Agency*, p. 3.
147 RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 7-8.
148 FERRAN, E. *Company Law and Corporate Finance*, p. 11 and PETRIN, M. *Reconceptualising the Theory of the Firm – from Nature to Function*, p. 4.
149 Chapter 1 – What Are Corporation? Available online at: https://www.malcolm.id.au/honours/chap1.html.
150 FERRAN, E. *Company Law and Corporate Finance*, p. 11.
151 RIPKEN, S. K. *Corporations are People Too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 8.
152 With respect to this conclusion, see: PATAKYOVÁ, M., CZÓKOLYOVÁ, B. *Teória spoločnosti v triáde rozhodnutí Daily Mail, Cartesio a VALE – spoločnosť ako fikcia, nexus kontraktov alebo reálna osoba? (in English: The theory of the company within the context of Daily Mail, Cartesio, and Vale – the company as a fiction, a nexus of contract, and a real person?).*

Chapter 4.2 Legal personality and theories of the legal personality of business companies in the context of Slovak law

Within the Slovak legal theory, mainly Patakyová and Csach deal with the issue of the character of companies. Patakyová (in the Commentary on the Commercial Code, particularly in the interpretation of Section 13 of the Commercial Code)[153] deviated from the theory of contract and favoured the theory of reality of companies as legal persons, whose legal personality is regulated by the Commercial Code. Under Section 18(1) and 19a(1) of the Civil Code, legal persons have the competence to have rights and obligations (the legal personality) as well as the competence to acquire rights and obligations (the legal capacity to act), while this competence to acquire rights and obligations by own actions may be limited only by legal acts.[154] The doctrine of *ultra vires* characteristic connected with the theory of fiction has not been applied in the Slovak company law since the Economic Code has been repealed. According to Patakyová, the non-application of the *ultra vires* doctrine and the possibility to limit the legal personality only by legal acts represent the inclination to the theory of reality.[155]

Csach comments the theory of company through the character of the legal person in the commented provision, Section 18 of the Civil Code. However, due to the application of general provisions on legal persons contained in Civil Code on business companies, it is essential to depict his conclusion at this place.[156] Csach declares that in the Slovak legislative, the theory of legal persons is built on both theories (the theory of reality and the theory of fiction) and at the same time on neither of them.[157] In detail, Csach states as follows: "*The legal personality is attributed to a certain organized unit only by the legal act, not by social reality, and it also applies in relation to foreign entities. At the same time, it is assumed that the legal person may act by itself through its bodies (rather the theory of reality), however, depending on a position of the individual bodies, the principles of representation, therefore mental distinction of existing entity and other entity acting in the name of the legal persons, apply (rather the theory of fiction). Potential inclination toward the theory of reality is relative, whereas the legal act avoids the terminological conclusion that legal persons have the competence to legal or illegal actions."*[158]

At this place, Havel's opinions covering the question of theories of companies cannot be omitted. He declared that for the purposes of his work (*Business companies in the light of changes: Alternatives on open issues of corporate governance*, in Czech language: *Obchodní korporace ve světle proměn: Variace na neuzavřené téma správy obchodních korporací*), from

[153] PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 54 and PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 4th edition*, p. 50.
[154] PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 54 and PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 4th edition*, p. 50.
[155] PATAKYOVÁ, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th editon*, p. 54.
[156] CSACH, K. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 100-101.
[157] CSACH, K. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 100-101.
[158] CSACH, K. In: ŠTEVČEK, M., DULAK, A., BAJÁNKOVÁ, J., FEČÍK, M., SEDLAČKO, F., TOMAŠOVIČ, M. et al. *Občiansky zákonník, § 1-450*, p. 100-101.

his point of view, the discussion between the theory of fiction and the theory of reality is not relevant.[159] Havel focuses on the fact that the legal person exists in reality only after its "justification" provided by a human being, meaning that it is essential to concentrate on the purpose of the company which is the projection of its interests.[160] According to Havel, the legal person is a result of the negotiable and non-negotiable construct whose purpose is to minimize risks and expenses, and this entity should bring an optimal solution to questions on which founders as contracting parties would agree, and therefore, it is possible to perceive the company as the solution.[161]

The individual legal personality as a general characteristic feature of the company is also highlighted by Hanes who states that: "*The legislative creates the individual legal personality of the business company as societas of partners (shareholders) not from needs given by law, but from needs of economic life which requires from these entrepreneurial legal entities as entities of market relationships to act as individual owners and holders of property or other rights and obligations separated from partners (shareholders)*."[162] It may be concluded that Hanes, similarly as Havel, inclines to perceiving the company as an individual legal personality.

Chapter 4.3 Legal personality of a corporation in the context of a poly-corporate approach in corporate law (group of companies)

4.3.1 Moving from individual view to a "group view" of corporations

Almost all national legal orders (not only in Europe but worldwide) regard corporations as special legal entities having their own economic interest.[163]

Despite the fact that corporations can operate independently, in many cases their assets and organizational and decision-making structure are interconnected and corporations create so-called groups. The term group of companies is not generally defined. Different legal systems and within them different areas of law differentiate situations when a corporation is viewed as a separate legal entity and when the fact that several corporations are connected in a specific way is taken into account. In this chapter, the concept of a group of companies will be used in a way that emphasizes the didactic aspect of the term, not the strictly normative aspect. A group of companies is understood to mean a number of corporations that are economically or organizationally linked to the extent that, although they are separate legal entities, they externally (especially in economic terms) act as a unified entity.

159 HAVEL, B. *Obchodní korporace ve světle proměn: Variace na neuzavřené téma správy obchodních korporací, (in English: The corporation in the lights of changes: Alternative regarding the unclosed topics of corporate governance)*, p. 42-43.
160 HAVEL, B. *Obchodní korporace ve světle proměn: Variace na neuzavřené téma správy obchodních korporací (in English: The corporation in the lights of changes: Alternative regarding the unclosed topics of corporate governance)*, p. 42-43.
161 HAVEL, B. *Obchodní korporace ve světle proměn: Variace na neuzavřené téma správy obchodních korporací, (in English: The corporation in the lights of changes: Alternative regarding the unclosed topics of corporate governance)*, p. 43.
162 HANES, D. Spoločnosť s ručením obmedzeným (in English: *The Limited Liability Company)*, p. 20.
163 DORRESTEIJN, A.: *European Corporate Law*, p. 281.

Company law creates a fundamental regulatory mechanism for the distribution of risk and costs related to the operation of corporations, on the one hand with respect to external entities (creditors) and, on the other hand, with regard to internal subjects (shareholders and directors).

For centuries, corporations have not been granted specific legal personality and it were the owners (shareholders) who have provided a guarantee for the corporation's debts.

At the end of the nineteenth century, on the basis of a long development, legal entities were gradually granted legal personality. At the same time, new rules have been developed on the basis of which the liability of shareholders for the corporation's debts has been redefined. These rules were created for "one-tier" corporations whose shareholders were natural persons.[164]

However, during the twentieth century, corporations started to form which had other corporations as their shareholders - groups of companies began to emerge. Existing legislation failed to properly address the emerging corporate relations and the issue of distribution of liability has been particularly problematic.

Based on this, a gradual regulation of groups of companies originated.[165] By granting legal personality to a limited liability company and by allowing legal entities to become shareholders, the conditions have been established to ensure that liability within groups of companies is regulated in a specific way.[166]

Groups of companies are created for various reasons. The basic reason is the division of the risk when new corporations (within the group) are established in order to isolate the bankruptcy of this corporation only to the corporation itself. Riskier business activities within a group can be realized through a corporation that has a smaller amount of assets, while other corporations within the group can be used as a "repository" of assets.[167]

Other reasons for creating groups can be tax reasons, the possibility of easier management and segmentation by business type and geographical distribution of business activities.[168]

The ways in which groups of companies are structured are different. Most often, there is one major parent (controlling) company that creates subsidiaries (controlled companies) which are further structured. Also, "horizontal" groups of companies may be created that have more than

164 ANTUNES, J. E. *Liability of Corporate Groups. Autonomy and Control in Parent-Subsidiary Relationships in US, German and EU Law. An International and Comparative Perspective*, p. 2.; EMMERICH, V., HABERSACK, B. *Konzernrecht*, p. 10.
165 ANTUNES, J. E. *Liability of Corporate Groups. Autonomy and Control in Parent-Subsidiary Relationships in US, German and EU Law. An International and Comparative Perspective*, p. 1-3.
166 MÜHLENS, J. *Der sogenannte Haftungsdurchgriff im deutschen und englichen Recht. Unterkapitalisierung und Vermögensentzug*, p. 56.
167 DORRESTEIJN, A. *European Corporate Law*, p. 281.
168 MONKS, R. A. G. *Modern Company Law for a Competitive Economy: the strategic framework*, p. 177.

one parent company.[169] The degree to which subsidiaries and subsidiaries of subsidiaries are controlled by the parent are also different. The parent company, through its management powers, can directly control the subsidiaries, or leave these corporations a relative discretion in their management. In relation to the "lower" levels of controlled companies (subsidiaries of subsidiaries, etc.), the parent company exercises indirect control which may also have different degrees. The parent company may interfere with the management of these corporations fairly intensively, leaving management to its subsidiaries or allowing these corporations relative freedom of management.

4.3.2 The need to regulate groups of companies

"Holdings, groups owned or managed by affiliated companies are an inherent backbone of the world economy." [170]

The concept of groups of companies, on the one hand, and the separate legal personality of corporations, on the other hand, can create tensions between the interests of individuals involved in legal relationships with corporations that are members of a group of companies. In particular, the interests of the minority shareholders in the controlled companies and the interests of the creditors of those companies may be contrary to the interests of the controlling companies. Tensions can also arise between the statutory obligations of the directors of the controlled companies (which, when deciding, should take into account the interests of the corporations for which they are acting) and compliance with the instructions of the controlling companies.

In this context, conflicts of interest may arise in the management of a group of companies. In a corporation that is not part of any group, all parties involved in the legal relationship with that corporation are interested in its continuous operation and existence. The shareholders (both majority and minority) are motivated to maintain such a corporation through their share on profit, directors are motivated by the remuneration for the performance of their function and creditors are motivated with respect to the payment of their claim.

On the other hand, in the case of a corporation that is part of a group, such a unified intention may not be obvious. In the case of a group of companies, there is rather a motivation for the preservation of the group as such, the interest in the functioning and maintenance of its individual components (corporations that are part of a group of companies) may not exist in a particular case. If a company that is part of a group is in a situation where it would be necessary to invest capital on the part of the controlling entity for its continued operation, or if it is evident that such a corporation will not be able to continue to operate with the current economic development, the controlling entity may decide that the controlled entity will no longer be financed and will go bankrupt. Although this scenario does not need to pose a serious problem from the point of view of conflict of interest (a bankruptcy of a corporation may occur

[169] McCOURT, A. *A Comparative Study of the Doctrine of Corporate Groups with special Empasis on Insolvency*, p. 2.
[170] CSACH, K. *Subjektivizácia koncernových a suborganizačných štruktúr*, p. 8.

regardless of whether it is part of the group). However, a conflict of interest may arise, in particular, where the bankruptcy has been caused by the controlling entity's decisions affecting the management of the controlled entity.

4.3.3 Regulation of the group of companies on the international level

It is precisely because of the emergence of potential conflicts of interest that a new regulation dealing with the issue of groups of companies has emerged,[171] which perceives the overall economic substance and does not give absolute preference to the principle of separate legal personality of corporations. At the same time, this regulation began to be adopted not only in the national context but also at the international level. Examples are the OECD Guidelines for Multinational Enterprises. These are *"recommendations addressed by governments to multinational enterprises operating in or from adhering countries. They provide non-binding principles and standards for responsible business conduct in a global context consistent with applicable laws and internationally recognised standards"*[172] Their aim is to support the adoption of national legislation, whereby multinational corporations are committed to respecting certain fundamental principles and rules in different areas of law (e.g. environmental law, consumer protection, labor law, human rights and tax law) and did not misuse corporate structures to circumvent the set minimum standards for example in the event of a violation benefiting the entire multinational group, whereby the corporation operating at the national level will bear all the adverse consequences and its creditors (injured parties) will not be fully compensated for any damage. It should be noted that the OECD Guidelines contain only general rules that must be specified in national implementing legislation. However, it is clear from their acceptance that the world community of economically advanced countries perceives the issues related to the existence of groups of companies.

The issue of regulating groups of companies has also been analyzed for a long time at European Union level. Already in 1998, a group of law professors under the name *Forum Europaeum Konzernrecht* prepared a draft directive on European corporate group law. A substantial part of this proposal was based on the so-called *Rozenblum* doctrine.[173] According to the doctrine in question, a group of companies may pursue a common, clearly defined interest that is not consistent with the interests of individual members of that group, as long as the group is rationally structured and if the directors of a particular corporation that is a member of such a group can assume that the possible harm will be remedied in due time.[174] This concept was created by the French courts in order to prevent abuse of the group management in a way that damages individual members of the group and their creditors.

171 CSACH, K. *Subjektivizácia koncernových a suborganizačných štruktúr*, p. 8.
172 OECD Guidelines for Multinational Enterprises, p. 3.
173 MOHN, A. *Die Gesellschaftsgruppe im Italienischen Recht. Eine Untersuchung unter besonderer Berücksichtigung der Entwicklung im Europäischen Recht*, p. 248 et seq.
174 FUNATSU, K. *Trends in European Corporate Group Law Systems and the Future of Japan's Corporate Law System*, p. 477.

The work of *Forum Europaeum Konzernrecht* was developed by another commission dealing with the regulation of groups of companies at the European Union level, the High Level Group of commercial law experts created by the European Commission in 2001 to prepare a modern corporate law regulation. The group concluded that it does not recommend comprehensive regulation of groups of companies at the European level. Instead, it suggested that problems created by groups of companies be dealt with partially. Issues to be addressed in the new regulation should be the transparency of the structure and relationships within the groups, the conflicts of interest between the group and its individual members, and the specific problems related to the so-called pyramid structures. However, the conclusions of this commission were not generally accepted.

The issue of regulation of groups of companies was also addressed by the European Model Company Act (EMCA). This group has presented the European Model Company Act in 2017, which serves as a model for member states to inspire them to implement the regulation at a national level. Chapter 16 of this model act deals with groups of companies. At the same time, the EMCA expert group notes that there are no consistent legal rules for the groups of companies at the European Union level. Member states have different levels of regulation that can be classified into 4 categories: (i) comprehensive regulation (e.g. in Germany, Portugal, Hungary, Czech Republic and Slovenia); (ii) partial regulation (e.g. in Italy), (iii) recognition of the group's specific interest based on case law (e.g. in France) and (iv) absence of regulation (except as required by the EU directives mentioned below for specific areas, e.g. in the UK or Slovakia).[175]

So far, the preliminary conclusion is that achieving a unified regulation of all aspects of groups of companies under corporate law on the level of European Union is currently not realistic.[176] However, a number of rules have been adopted at the Union level to deal with the existence and functioning of groups of companies. We can mention e.g. the Transparency Directive[177] which introduced more detailed financial reports for issuers of shares admitted to trading on a regulated market which should increase transparency and allow investors to evaluate the issuer's situation on the basis of better information. It is also relevant to mention the Directive on Annual Financial Statements,[178] which also aims at protecting shareholders, members and third parties through the *coordination of national provisions concerning the presentation and content of annual financial statements and management reports, the measurement bases used therein and their publication in respect of certain types of undertakings*.[179]

175 European Model Company Act, Chapter 16 – Groups of Companies, p. 3-4.
176 DORRESTEIJN, A. *European Corporate Law*, p. 291-292.
177 Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.
178 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (hereinafter "Directive 2013/34/EÚ").
179 Preamble, Paragraph 3, the Directive 2013/34/EU.

European Union law therefore reflects the existence of groups of companies but has so far abandoned a complex regulation. It leaves this to the member states. For this reason, the scope of regulation of groups of companies at national level is very heterogeneous, and each member state determines to what extent it will regulate the issues related to groups.

4.3.4 The concept of controlling and controlled entity and the group of companies from the perspective of Slovak corporate law

Slovak corporate law is dominantly based on the concept of separate legal personality of corporations - each corporation is treated as a separate legal entity and only exceptionally it is considered that a corporation is part of a group of companies that are jointly managed and which, from an economic point of view, form a single entity.[180]

The aforementioned exception, when it is taken into account that a corporation may be part of a larger economic unit, is connected with the concepts of the controlling and controlled entities defined in Section 66a of the Commercial Code. Pursuant to Section 66a(1) of the Commercial Code a controlled entity is a corporation in which a person has a majority of the voting rights because it has a share in the company which is linked with a majority of the voting rights, or because it can exercise the majority of voting rights under an agreement with other authorized persons, irrespective of the validity or invalidity of such agreement. The voting rights are increased by the voting rights (i) associated with the shares of the controlled entity that are owned by other persons controlled directly or by the controlling entity, (ii) executed by other persons in its own name and on behalf of the controlling entity. The controlled entity is subsequently defined as a person which has the above-mentioned status in the controlling entity.

The mentioned concept is based on the following principles:

- Only the exercise of voting rights is taken into account. The decisive factor for assessing whether a company is a controlling entity is connected with the fact whether it has a majority of the voting rights. The exercise of voting rights may be *de iure* (on the basis of corporate documents that grant the controlling entity majority of voting rights) or *de facto* (by virtue of agreement with other persons the controlling entity factually exercises a majority of the voting rights).
- However, no consideration is given to the fact whether the controlling entity manages and influences the controlled entity in a manner other than the exercise of the majority of the voting rights (e.g. under a contract on the basis of which the controlling entity directs the controlled entity).
- The concept of controlling entity implements “direct” as well as “indirect” control of the controlled entity by a majority of voting rights.[181] Thus, the controlling person does not have to be a direct shareholder in the controlled entity but may also be at a “higher level” of corporate group structure.

[180] OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár*, p. 465.
[181] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 304-305.

- The definition of a controlling entity is not intended to find a the "beneficial owner" (i.e. a natural person who is the ultimate recipient of benefits from the corporation) or a "parent company of the holding" (i.e. a corporation that manages and controls the entire group of companies).

The concepts of controlled and controlling entity were rarely used in Slovak corporate law. Legal references can be found in Section 59a(3) , Section 66b, Section 120 (3) and Section 120 (4), Section 136, Section 161f (2-4), Section 180 (1) and Section 180 (4), Section 196, Section 196a and Section 208 (4) of the Commercial Code. In addition to this, by an amendment of the Commercial Code,[182] these concepts were introduced in a specific form of liability, namely the liability of the controlling entity for the bankruptcy of the controlled entity. The amendment, through the provision of Section 66aa of the Commercial Code, introduced a new legal principle, also referred to as piercing of corporate veil in Slovak law.[183] The basic conditions of this concept are defined in Section 66aa(1) of the Commercial Code as follows: *"The controlling entity is liable to the controlled entity's creditors for damage caused by the bankruptcy of the controlled entity if, by its conduct, it contributed substantially to the bankruptcy of the controlled entity. This liability does not arise if the controlling entity proves that it has acted based on relevant information and in good faith that it is acting for the benefit of the controlled entity."*

The explanatory memorandum to the amendment in question does not state what social circumstances led to the adoption of the amendment (e.g. whether the former liability towards the creditors was inadequate), why the chosen concept was partly inspired by German case-law and partly by Czech legislation or what result is expected from the upcoming regulation. Although the explanatory memorandum addresses the different conditions of liability and clarifies how it should work, there is no explanation why this form of liability has been chosen and what outcome can be expected from the new principle.

If we wanted to fill this gap, we would say that the aim was to strengthen the position of the creditors of the controlled entity and its better protection in the event of interference by the controlling entity with its management.

However, as discussed in more detail below, the effectiveness of the new regulation will largely depend on the approach of courts in specific cases. After a longer period of time, it will be possible, on the basis of an analysis of court decisions, to assess whether the courts have dealt with this issue in a way that really contributes to protecting the creditors of the controlled entities.

182 Act No. 264/2017 Coll., which changes and amneds the Act No. 513/1991 Coll. Commercial Code as amended and which changes and amends different statutes.

183 MAŠUROVÁ, A. *Zodpovednosť štatutárov, faktických štatutárov a tieňových štatutárov kapitálových spoločností voči veriteľom spoločností podľa novej úpravy obchodného zákonníka a zákona o konkurze a reštrukturalizácii*, p. 171.

The liability of the controlling entity for the bankruptcy of the controlled entity significantly disrupts the liability concept existing within the corporate law system. At the same time, it causes that the corporation is no longer viewed just as a separate legal entity but as part of a group of companies.

The purpose and objective of regulating the controlling entity's liability for the bankruptcy of the controlled entity was not declared by the legislator in the explanatory memorandum. However, it can be stated that it is an improvement in the position of creditors in the event of the debtor's bankruptcy, since creditors may also enforce their claim against the controlling entity under the conditions stipulated by law.

The controlling entity's liability for the bankruptcy of the controlled entity is very favorable for creditors. Although this was not stated in the explanatory memorandum, the newly adopted concept of the controlling entity's liability avoids the issues that exist with general liability for damage. First of all, the amount of the damage is presumed, which means that the amount of damage corresponds to the unenforced part of the creditor's claim and is the controlling entity who needs to prove a different amount of damage was sustained. Furthermore, there is a "mitigated" form of causality where it is sufficient if the creditor proves that the controlling entity has *contributed* to the bankruptcy. It is not required to prove a *100% causal link* and provide evidence that without the interference of the controlling person the bankruptcy of the controlled entity would not take place. Finally, contribution to bankruptcy may be caused due to any controlling entity's actions; liability is therefore not linked to specific (illegal) types of conduct.

It should be mentioned that with respect to the liability of the controlling entity for the bankruptcy of a controlled entity, it is possible to identify certain deficiencies that may cause complications in the exercise of creditors' claims:

- One of the decisive criteria for establishing liability is the fact that the controlling entity has at least indirectly a majority of the voting rights in the controlled entity. This does not take into account the fact that a shareholder with a much smaller number of votes may have an impact on the real functioning of the company.[184]
- The amount of damages that have been sustained will not be fixed until after the bankruptcy proceedings have been completed, i.e. only after several years. The creditors may not be motivated to use this concept in case of such a long "waiting period".
- In practice, it could be difficult to prove that the controlling entity has contributed substantially to the bankruptcy of the controlled entity. A number of factors (including market-related factors) affect the functioning of the corporation and it is expected that in the event of a dispute it will be difficult to establish which of the factors has contributed to the bankruptcy.

[184] MAŠUROVÁ, A. *Zodpovednosť štatutárov, faktických štatutárov a tieňových štatutárov kapitálových spoločností voči veriteľom spoločností podľa novej úpravy obchodného zákonníka a zákona o konkurze a reštrukturalizácii*, p. 171.

However, it should be noted that the appropriate approach of the courts in the application of the newly adopted provisions can eliminate the complications.

The functioning of corporations in the current business world is largely based on groups of companies. The law must respond to this, accept it and move forward so that the interests of the various stakeholders are balanced. In this case, it is necessary to ensure a better position of creditors.

Unless a comprehensive area of law regulating the functioning of holding companies is adopted in the Slovak Republic, it is appropriate to protect the interests of creditors at least in this manner, i.e. the liability of the controlling entity for the bankruptcy of the controlled entity.

Despite the fact that the limited liability of the shareholders is reduced, this does not imply a significant change in the position of shareholders in the event that they refrain from interfering with the operation of the controlled entity. If they remain only "passive investors" and leave the management of the corporation to its directors, they do not have to worry about creating direct liability towards creditors.

Revision questions:

1. *Describe the legal personality of the companies and their characteristics.*
2. *How does fiction theory explain the legal personality of a company, what is its historical background and what are its weaknesses?*
3. *How does the theory of reality explain the legal personality of a company, what is its historical background and what are its weaknesses?*
4. *Which company theory does Slovak law favour?*
5. *What was the historical evolution of groups of companies?*
6. *How are groups of companies regulated at the international level?*
7. *What is the approach of Slovak corporate law towards the regulation of groups of companies?*
8. *Which entity is considered to be the controlling entity and what is the controlled entity? Which factors are taken into account?*
9. *What are the conditions to establish liability of the controlling entity for the bankruptcy of the controlled entity?*
10. *Which aspects may be problematic in the practical application of the controlling entity's liability for the bankruptcy of the controlled entity?*

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Part V. The Purpose of Forming a Corporation and a Cooperative

Chapter 5.1 The Purpose of Forming a Corporation

The primary purpose of the formation of corporations,[185] rests in the effort to achieve economic power and a concentration of capital that is not accessible to an individual. Different countries were aware of the importance of such potential of capital concentration, as well as of the fact that such corporations could be beneficial to the public and the community. For example, early corporations in the US were formed to allow the use of private sources to perform tasks in the public interest (operating railroads, building roads and bridges).[186] The practical importance of corporations is attributed to such typical aspects as the limited liability of shareholders, the transferability of shares, legal personality/subjectivity and centralized management. These aspects fulfil the purposes of a business corporation in facilitating the accumulation of capital from different sources, as well as the operation of a business with many employees,[187] while, at the same time, the shareholders are not subject to unpredictable and unexpected risks.[188] Havel writes that a corporation is an instrument of organization and an ingenious establishment through which individual profit may be achieved without individual liability.[189]

According to Clark, the preconditions for the development of business activities in the form of a corporation included, among others, technological progress and the concentration of production requiring larger forms of organization and a diversity of sources not concentrated in the hands of a few individuals.[190] However, these positive functions brought the necessity to cope with newly related problems and conflicts (conflicts of interest of the shareholders, corporate boards, creditors, employees, customers). Corporate law, therefore, is designed to provide for the checks and balances to deal with conflict resolution, and to create and use instruments to mitigate some of the negatives (piercing the corporate veil, shadow or de facto directors, absolute priority rule, etc.). Considering the strength of corporations as the largest entities in the market allocating capital and providing goods, services and jobs,[191] they should not be solely oriented on profits, but on other objectives, such as the realization of public and community interests, improvement of the quality of life of their employees, protection of the environment and enhancement of the well-being of the society as a whole. A focus on ethical standards of social behaviour and its contribution to sustainable economic development included in the concept of corporate social responsibility (also "CSR") appeared in the theoretical literature in the fifties of the last century.[192] The questions concerning the objectives

185 We decided to use the term "corporation" in reference to American content and the term "business " in reference to Slovak content.
186 PINTO, A. R., BRNSON, D. M. *Understanding Corporate Law*. Durham, p. 7.
187 CLARK, R. C. *Firemní právo*, p. 34.
188 HAVEL, B. *Obchodní korporace ve světle proměn*, p. 47.
189 HAVEL, B. *Obchodní korporace ve světle proměn*, p. 44.
190 CLARK, R. C. *Firemní právo*, p. 36
191 PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. In: HUSÁR, J., CSACH, K. *Konflikty záujmov v práve obchodných spoločností*, p. 32.
192 PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. In: HUSÁR, J., CSACH, K. *Konflikty záujmov v práve obchodných spoločností*, p. 34.

or interests to be pursued by a corporation are closely related to the issues of the interest models in corporate governance (the shareholder model, the stakeholder model, and the enlightened shareholder model).

5.1.1 Shareholder Primacy - Shareholder Model of Corporate Governance

The crucial pillar of the shareholder model is the rule that shareholders are residual claimants, i.e. the holders of residual claims. This means that when a company is wound up with more property than is needed to meet the claims of other creditors, such surplus shall go to the shareholders. Under this rule, the surplus, or what has remained to the shareholders, will be determined only after all of the claims against the company have been discharged.[193] The concept of shareholder primacy, which is primarily found in the American legal environment,[194] means that the corporate directors are obligated to pursue the interests of shareholders, and based on their fiduciary duties of care and loyalty, they must run the company to maximize shareholder wealth.[195]

In relation to stakeholders (creditors, employees, customers), the first priority of shareholders in the American legal environment is based on the possibility to protect stakeholders through separate legal regulations concerning employees' rights, the protection of creditors or customers, environmental protection, as well as other regulations in areas related to stakeholders' rights, but not through corporate law.

However, shareholder primacy also has its critics who argue for the relevance of the interests of stakeholders (creditors, employees and customers/consumers). Corporations cannot solely concentrate on shareholders' interests and values, while ignoring other groups of stakeholders, and striving to reach short-term objectives, which, from the long-term perspective, may be harmful to a broader spectrum of interests. These views maintain that the pursuit of the interests of multiple stakeholders also takes into account the interests of the government as the authority enabling the legalization of corporations upon contractual freedom, and providing the legislative basis for the limited liability of shareholders.

Despite occasional academic arguments to the contrary, the shareholder wealth maximization norm expounded in judicial decisions is the law in the United States, and the courts remain committed to shareholder values. The essential judicial decision in support of the shareholder model was *Dodge v Ford Motor Co.* (Michigan Supreme Court) in 1919. In this case, the Court formulated the basis of the shareholder model, according to which, business corporations should be run to generate profits for the shareholders. The powers of corporate directors are to

193 DAVIES, P. *Introduction to Company Law*, p. 267

194 RHEE, R. J. *A Legal Theory of Shareholder Primacy*. Available online at: https://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1004&context=working

195 BAINBRIDGE, S. M. *Director Primacy: The Means and Ends of Corporate Governance*, p. 550. Available online at: HEINONLINE.

be employed for that end. A corporation is formed for a single purpose - to maximize the profits of its shareholders.[196]

5.1.2 Stakeholder Model

The stakeholder model was born out of the idea that if a corporation is legally recognized by the central government, it should also have social obligations. The main priority should not be shareholder profits, but also the interests of other groups with claims against the corporation, such as creditors, employees, customers. The primary task of corporate directors is not to act as the agent of the shareholders, ruthlessly enforcing shareholder interests at the expense of the employees, creditors and other stakeholders. The corporate directors, acting more as administrators of the corporation, must balance the competing interests of stakeholders so that all of them are sufficiently satisfied. Under these circumstances, a coalition of stakeholders will hold together. The social significance of the stakeholder model lies in the fact that corporations should be beneficial to society.[197]

The question of the pursuit of stakeholder interests is connected with the doctrine of *ultra vires*, and also with the issue of whether the sole purpose and objective of a corporation is to reach a profit and to satisfy the investment requirements of shareholders. The proponents of the stakeholder model point out that corporations play an important economic role, and have the power and resources which enable them to diverge from the pursuit of achieving profit as their sole goal. In the context of such broader goal, the fiduciary duties of directors and officers should be considered as well, and should not be judged only in relation to shareholder interests.

Critics of the stakeholder model argue that it is not functional. *Michel C. Jensen* explained that a corporation must pursue its individual object of interest as a course indicator of meaningful and rational conduct. It is impossible to maximize the satisfaction of multiple interests simultaneously. Requiring corporate directors to increase profits, market share, future growth or anything that may please some, will deprive them of their ability to make reasonable decisions.[198]

The concept of the stakeholder model also became discredited during the financial crisis when drawbacks of corporate management showed that it was necessary to make legal corrections and adjustments in supervisory regulation.[199]

Combining the long-term pursuit of shareholder interests with sustainable growth and responsible care of stakeholder interests is reflected in the concept of *enlightened shareholder value (ESV),*[200] an intersection of the shareholder model and the stakeholder model. This

196 BAINBRIDGE, S. M. *Director Primacy: The Means and Ends of Corporate Governance*, p. 23. Available online at: HEINONLINE.
197 RICK, A. *Benefit Corporation Law and Governance: Pursuing Profit with a Purpose*. ProQuest Ebook Central, p. 24 available online at http://ebookcentral.proquest.com/lib/pitt-ebooks/detail.action?docID=4854326.
198 JNESEN, M. C. *Value Maximization, Stakeholder Theory, and the Corporate Objective Function*, p. 235-256.
199 SPINDLER, G., STILZ, E. *Kommentar zum Aktiengesetz*. 4th edition, p. 1084
200 The traditional shareholder value principle became modified in the UK by introducing the *principle of enlightened shareholder value*, under Section 172 Subsection 1 of the Companies Act of 2006, assigning the

approach has only prevailed in the case of a short-term, limited focus on the value of dividends, which negatively affects stakeholder interests. It is precisely the combination of the long-term sustainable concept of value coupled with the acknowledgment of the importance of stakeholder interests that correspond with the notion **of corporate social responsibility**. [201]

Chapter 5.2 The Purpose of Establishing a Company under Slovak Law

According to § 56 (1) of the Commercial Code, a company is a legal entity formed for the purposes of conducting business. *Csach* writes that "*the purpose is one of the main distinctive criteria when deciding on the type of legal entity through which a certain objective is to be reached.*"[202]

Under Section 2 of the Commercial Code, conducting business denotes systematic activities carried out independently by an entrepreneur in their own name and upon their own responsibility (i) to make a profit or (ii) to achieve a material/measurable positive social impact as laid down in a special law, i.e. Act 112/ 2018 on Social Economy and Social Enterprises ("Social Economy and Social Enterprises Act"). For the purposes of this Act, a positive social impact is the fulfilment of public or community interests. By including the achievement of a measurable social impact in the definition of business, the legislators subsumed these activities under economic activities to which the statutory provisions concerning business apply, to ensure that no non-profit activity is left out of the regulation. Thus, social enterprises, being equal to business entities, are subject to the Commercial Code. [203] Subsuming the activities of social enterprises under business in line with the Commercial Code has additional consequences, namely the fact that not only the revenues arising out of economic activities conducted for profit, but also those conducted for the purpose of achieving a positive economic impact are subject to taxation under Act 595/2003.[204] Subject to meeting the criteria set by the Social Economy and Social Enterprises Act, a business company may be included among admissible forms of social enterprises.

Under Section 56 (1) of the Commercial Code, a limited-liability company and a joint stock company may also be formed for purposes other than conducting business, unless prohibited by a special law. The other purposes refer to social dimension activities to which the Social Economy and Social Enterprises Act does not apply, since achieving a measurable positive impact under the Act is regarded as conducting a business or business activities. Such other purposes include the areas of culture and the environment among others.

company directors to take into account the stakeholder interests; for more details see KEAY, A., ZHANG, H. *An Analysis of Enlightened Shareholder Value in Light of Ex Post Opportunism and Incomplete Law*, p. 445-475.

[201] MILLON, D. K. *Enlightened Shareholder Value, Social Responsibility, and the Redefinition of Corporate Purpose Without Law*. Available online at SSRN: https://ssrn.com/abstract=1625750 or http://dx.doi.org/10.2139/ssrn.1625750

[202] OVEČKOVÁ O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 371.

[203] See: Explanatory memorandum to the Act no. 112/ 2018 Coll. on Social Economy and Social Enterprises as amended.

[204] Ibid.

Although a limited liability company and a joint-stock company are formed for a purpose other than conducting business, they still remain in the category of entrepreneurs. This is the case of **entrepreneurs classified by their form**, for which legal form is decisive and not the criterion of entrepreneurial activities.[205]

5.2.1 Company Established for the Purpose of Conducting Business

A company established for the purpose of conducting business will pursue economic activities (i) as systematic activities (ii) conducted independently (iii) in its own name, and (iv) upon its responsibility. We can speak of business/entrepreneurial activities, provided that all of the characteristic elements given below are present. **Systematicity** relates to conducting business and not business-related activities[206] (such as translations, clerical work). The seasonal systematic character of recurring activities (such as operating swimming pools, ice rinks, selling Christmas trees) is no bar to a business run systematically. The **independence** of a company in running its business activities is manifested in the system of decision-making and management. As shown by *Patakyová,* the requirement of independence will be satisfied also in cases of controlling and controlled companies, franchises, commercial representations/trade agencies, agency/mandate contracts, etc.[207] A company conducts business **in its own name**, where "*the business is not run for the benefit of another."*[208] A company conducts business through legal acts carried out under its business name. It is conducted at its own responsibility as a result of running the business independently and in its own name.[209] The responsibility relates to business risks related to dealing with the positive as well as negative consequences of the actual business activities.

According to Section 2 (1) of the Commercial Code, a company may be established for the purpose of conducting business to achieve (i) a profit or (ii) a measurable positive social impact.

5.2.1.1 Company Established for the Purpose of Conducting Business to Achieve a Profit

In the case of a company established for the purpose of conducting business for profit, all of the following elements of the definition must be present, i.e. the business activities must be carried out (i) systematically (ii) independently, (iii) in the company's name, (iv) at its responsibility and (v) **for the purpose of achieving a profit**. However, the purpose of doing business and achieving a profit does not mean that a profit must always be reached; the point here is that the activities as such are directed towards that aim. The profit must be a motivating factor of such business activity. The facts (both subjective and objective) due to which a profit is not ultimately achieved are not decisive.[210] This is expressed by Fischer's definition of a business company: "*A business company, an association of two or more persons, is formed*

[205] MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1 zväzok*, p. 183.
[206] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 11.
[207] Ibid.
[208] OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I.*, p. 55.
[209] OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I.*, p. 56.
[210] MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1 zväzok*, p. 7.

upon a contract with the intention to carry out business deals to jointly share in the profits and losses of the venture."[211] Profits denote a positive economic result, while losses denote a negative economic result.

The definition of business enterprising/trading is also contained in the Small Trades Licensing Act, which, in addition to the five definition elements stipulated by the Commercial Code, as mentioned earlier, i.e. systematic and independent activities carried on under the entrepreneur's name and upon his responsibility for the purpose of achieving profit, the following is inserted: under the conditions set forth by the Small Trades Licensing Act. As shown by Ovečková: "*This means that a small trade business differs as to the activities stipulated by the Small Trades Licensing Act, i.e. defined in a narrower sense than in the case of a business run in compliance with the Commercial Code. Nevertheless, any sole trader under the Small trades Licensing Act is an entrepreneur under the Commercial Code*."[212] The same also applies to business companies.

5.2.1.2 Company Established for the Purpose of Conducting Business to Achieve a Measurable Positive Social Impact

A company established for the purpose of conducting business to achieve a measurable positive social impact must meet the following elements of the definition, the company business activities are carried out (i) systematically (ii) independently, (iii) in the company's name, (iv) upon its responsibility, and (v) **for the purpose of achieving a measurable positive social impact**. However, this does not apply to any kind of economic activities, but only to economic activities of a social enterprise registered under the Social Economy and Social Enterprises Act. This refers to business companies – social enterprises pursuing aims other than achieving a profit; their main purpose is not to generate financial revenues for their owners, but to provide goods and services for their members or otherwise engaged persons, or for the broader community.[213] The purpose of such business companies may overlap with the purpose of forming a cooperative. The activities of such companies pertain to the general term of *social economy*.[214]

Positive social impact is defined in Section 2 (1) of the Social Economy and Social Enterprises Act as the achievement of public or community interests. Achieving public interests implies providing socially beneficial services to the society as a whole or to an unlimited number of individuals, disadvantaged persons and vulnerable persons, as well as providing for the accommodation, administration, maintenance and repair of residential buildings. Accomplishing community interests implies the provision of a socially beneficial service to a group of persons which may be limited or identified by some objective criteria (concerning territory, membership, interest preference), with the exclusion of socially beneficial services

[211] Cited from: ELIÁŠ, K., POKORNÁ, J., DVOŘÁK, T. *Kurs obchodního práva. Obchodní společnosti a družstva*, p. 7.
[212] OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I.*, p. 56.
[213] Explanatory Report to the Act 112/ 2018 Coll. on Social Economy and Social Enterprises as amended.
[214] Ibid.

provided to disadvantaged persons, vulnerable persons, and exclusive of the provision of the accommodation, management, maintenance and repair of residential buildings. The Explanatory Report on the Social Economy and Social Enterprises Act shows an actual example of community interests implemented by a non-profit cinema to be used for cultural purposes by a small municipality situated far from any large settlement/town, where, otherwise, the people would enjoy no other social and cultural events. Non-profit energy production from renewable resources contributing to the mitigation of climate change is an illustration of the achievement of public interests.[215]

A company is a social enterprise oriented not toward profit but toward a positive social impact. Such company may not be majority controlled or funded by the government; however, it is not prohibited from receiving general government subsidies. Thus, a social enterprise is a subject/entity of social economy (i) which conducts an economic activity, (ii) the main aim of which is to achieve a measurable positive impact, (iii) in which the achievement of a positive social impact is assisted by the production, supply or distribution of its goods or services, (iv) over 50% of the profit in which is used for the achievement of a positive social impact (*profit socialization*), and (v) in which the stakeholders (e.g. employees, customers, volunteers, etc.) participate in the management.

Under the Social Economy and Social Enterprises Act, special conditions relative to the Commercial Code are set for granting a social enterprise the status of a registered social enterprise, e.g. as regards the creation of an advisory committee or the implementation of a democratic administration. The powers of the advisory committee also affect issues related to the company management. The conditions of democratic management are set forth in special requirements governing the company ownership structure in which a share must be owned by the majority of its employees, and the majority of shareholders must be employees of the company. Another significant interference in the shareholder democracy of such business company is the legal requirement that when voting at the general meeting or a similar body, each shareholder is entitled to one vote, irrespective of their share size. At the same time, the company's internal regulations must provide for any employee who has been working at the company for at least five years with the right to vote at the general meeting or a similar body, or the right to express their views on any matter on which a vote is taken.

Granting the statute of a social enterprise is within the authority of the Ministry of Labour, Social Affairs and Family which also keeps a record of registered social enterprises, which is public.

In connection with companies established for the purpose of achieving a material/measurable positive social impact, the question of its connection with the concept of corporate social responsibility (CSR) arises. Social enterprises may be considered just a part of CSR because this concept is broader than the concept of social enterprise, and the same is also relevant for companies conducting business for a profit. With regard to the responsibility of the company

[215] Ibid.

directors/members of statutory bodies, however, the concept of corporate social responsibility should be included in the codes of management and administration or decision-making in these companies. [216] [217]

5.2.2 Company Established for Another Purpose

A company established for a purpose other than conducting business may have the form of a limited liability company or a joint-stock company, unless prohibited by a special law. Where a limited liability or a joint-stock company has been established for a purpose other than conducting business, due to their legal form, both still remain in the entrepreneurial category. The condition of the admissibility of another purpose for the existence of the company is that of lawfulness, i.e. the purpose must not be reserved to other specific legal forms (such as a church, a political party, etc.).

Unless the purpose is reserved to other legal forms, these companies may also be permitted to be formed for a combined purpose, or the activities of a limited liability company may be legally adjusted to activities traditionally pertaining to the activities of a non-profit organization or a civil association (e.g. providing for humanitarian care, social assistance, environmental protection, cultural enhancement).

Chapter 5.3 The purpose of forming a cooperative

A cooperative may be established for the purpose of doing business, but also for meeting the economic, social or other needs of its members. This cooperative feature dates back to the Austro-Hungarian period when cooperatives were based in societies that evolved from associations (Roman societas) and were therefore subject to special legislation separate from companies. In countries of continental law based on Roman law, cooperatives take the form of a company chosen by members of the cooperative. This different concept is also reflected in the name of the European form of Societas Cooperativa Europeae, i.e. a European cooperative society (taking into account the definition of company in Article 54 TFEU). Apart from this supranational European form, the rules on cooperatives within the European internal market are not harmonized and are not expected to be harmonized even in the medium term.

In Slovak conditions, a cooperative can also be characterized as a legal entity (a company under the Treaty on the Functioning of the EU) with open membership and variable capital. The particular feature of the cooperative lies mainly in self-government (membership of cooperative bodies is conditional on membership in the cooperative), the principle of cooperative democracy (one member's share - one vote) is regulated dispositionally. The explicitly adjusted variability in the number of deposits of cooperative members (Sections 223 (2) and (3) of the

[216] PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. In: HUSÁR, J., CSACH, K. *Konflikty záujmov v práve obchodných spoločností*, p. 44.
[217] More details also in: LUKÁČKA, P. *Kategória zodpovednosti a zodpovedné podnikanie v právnom prostredí Slovenskej republiky v kontexte výkonu funkcie štatutárneho orgánu spoločnosti s ručením obmedzeným*.

Commercial Code) directly points to the possibility of eliminating this particularity of the cooperative and will be linked to the purpose of establishing a cooperative.

The Commercial Code contains a uniform regulation of cooperatives regardless of their subject of activity. The necessary differentiation of the internal organization, the content of membership rights and obligations, the number of deposits, the amount of the indivisible fund from which the cooperative members may not provide performance during the duration of the cooperative, other forms of equity participation, are usually contained mainly in the articles of association, which allow a relatively broad framework given the disposable nature of many provisions on cooperatives, such as Section 230 of the Commercial Code and Section 232 (2) of the Commercial Code and for agricultural cooperatives Section 234(2) the Commercial Code.

A cooperative is registered in the Commercial Register and always has entrepreneurial status [Section 2(2)(a) of the Commercial Code, Section 27(2)(a) Commercial Code]. This also applies if the purpose of establishing a cooperative, i.e. the motivation of a cooperative's activity is not to make a profit, but to ensure the economic, social or other needs of its members. Unlike trading companies mainly engaged in business activities for profit, cooperatives historically originated as so-called self-help communities ensuring certain common economic and social interests of their members, be they entrepreneurs (economic cooperatives) or consumers (consumer cooperatives). However, the cooperative form is also widely used mainly in European countries for organizing production activities, activities of savings banks, ensuring the mass purchase of needs for individual entrepreneurs associated in a cooperative, and eventually for organizing the sale of their products.

A cooperative is a legal person governed by private law, separate from the system of public authorities, and the State may, in the case of a cooperative providing certain social needs of its members (e.g. job opportunities for people with reduced working ability, meeting housing, recreational needs) provide assistance, especially in the form of tax credits, subsidies, direct material assistance, etc. The State may determine the conditions under which such aid is granted, but it may not directly interfere with the cooperative's own activities and its property relations, unlike the administrative system of State economic management in force before 1989.

Revision questions:

1. *For what purpose may be a company established? Who should serve the company?*
2. *What interest model theories prevail in relation to pursuing the interests of different interest groups? What model does the Slovak legislation follow in Sections 135a and 194 of the Commercial Code?*
3. *How is a business defined under the Commercial Code?*
4. *Define the involvement of social enterprise governance in the corporate governance of capital companies.*
5. *Propose a solution to the legal requirement to exercise voting rights at the general meeting of a social enterprise (each shareholder has one vote, irrespective of the share size).*
6. *How would you define Corporate social responsibility?*
7. *For what purpose may a cooperative be established?*

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Part VI. Defining characteristics of a company

Chapter 6.1 Definition of a company

6.1.1 Definition of a company under the Slovak law

Section 56(1 and 2) of the Commercial Code represent the basis or starting point for defining a company under the Slovak law. [218] Section 56(1) of the Commercial Code defines a company as a legal person established for the purpose of conducting business activities. Thus, the fact that companies are legal persons constitutes one of the main characteristics of companies stipulated in the Commercial Code. However, we have to search Sections 18 – 21 of the Civil Code to find the general legal regulation of legal persons. These provisions do not provide a complete definition of the legal person. Section 18[219] of the Civil Code only enumerates the individual types of legal persons and Sections 19 – 20 of the Civil Code supplement some characteristics/defining features of legal persons. The Civil Code gives legal persons the competence to have rights and obligations and to conduct legal acts. [220]

The enumeration of individual types of legal persons may be found in Section 56(1) of the Commercial Code. They include *an unlimited company, a limited partnership, a limited liability company, a joint stock company, and a simple joint stock company.* This enumeration constitutes an exhaustive enumeration of companies which may be established under the Commercial Code due to the mandatory character of Section 56 of the Commercial Code. [221] Moreover, legal entities established under the law of the European Union have a position similar to the position of companies.[222]

An unlimited company is regulated by Sections 76 -92 of the Commercial Code and represents one of the legal forms of companies within which at least two persons (either natural or legal persons) pursue their entrepreneurial activities under a joint business name. An unlimited company is responsible for the breach of its obligations with its entire property. Partners are jointly and severally liable for obligations of the unlimited company with their entire property. An unlimited company is not under the obligation to create legal capital. Every partner is entitled to manage (govern) the company. Partners may fully or partially entrust the management of the company to one or several partners, while in such case, the other non-entrusted partners lose the entitlement to manage the company in this scope. Every partner of

[218] Section 56 Subsection 2, the Commercial Code: *"A company (hereinafter referred to as "company") is a legal entity established for the purpose of conducting an entrepreneurial activity. The term company refers to an unlimited company, a limited partnership, a limited liability company, a joint stock company and a simple joint stock company. A limited liability company and a joint stock company may also be established for another purpose, unless prohibited by a special Act",* Section 56(1), the Commercial Code. *"Legal entities established under the law of the European Union have a position similar to the position of companies."*

[219] Section 18 Subsection 2, the Civil Code: *"Legal persons are: a) associations of natural or legal persons, b) special-purpose property associations, c) local governments units, d) other subjects pursuant to a legal act"*.

[220] Section 18 Subsection 1, the Civil Code.

[221] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 156-157.

[222] Section 56 Subsection 2, the Commercial Code.

an unlimited company is entitled to act on behalf of the partnership independently if the foundation document does not state that only one or several partners are entitled to act on behalf of the company or that they may only act together.

A limited partnership is a company established by one partner with the status of a limited partner and one partner with the status of an unlimited partner. The maximum number of partners is not set by law. Limited partners of a limited partnership are under the obligation to make a minimum contribution to the company of EUR 250. A limited partnership is responsible for the breach of its obligations with its entire property. Partners of the limited partnership are not responsible for the partnership's obligations. Limited partners are liable for the partnership's obligations up to the amount of their unpaid contribution registered in the Commercial Register. However, limited partners are liable for the partnership's obligations with their entire property if the business name of the partnership contains their name. Unlimited partners are liable for the partnership's obligations with their entire property. The legal regulation of the limited partnership is covered by Sections 93 – 104 of the Commercial Code. Unless stated otherwise, the provisions of the Commercial Code covering an unlimited partnership will primarily apply to a limited partnership and the provisions regulating a limited liability company will apply to the unlimited partners of a limited partnership.

A limited liability company is a legal form of a company with an obligation to create legal capital in the minimum amount of EUR 5 000 while the minimum amount of the contribution of one shareholder is EUR 750. Shareholders are liable for the obligations of the company during its existence up to the amount of their unpaid contribution registered in the Commercial Register. The amount of a shareholder's unpaid contribution is registered in the Commercial Register. The business share of a limited liability company represents the rights and obligations of its shareholders and their corresponding participation in the company. The amount of the business share is determined as a proportion of the shareholder's contribution to the legal capital unless the foundation document states otherwise. The legal regulation of a limited liability company is covered by Sections 105 – 153 of the Commercial Code.

A joint stock company is a company whose legal capital is allocated to a certain number of shares with the specific nominal value. A joint stock company is responsible for a breach of its obligations with its entire property. It may be a private joint stock company or a public joint stock company. The articles of association of the joint stock company shall determine the specific nominal value of all types of shares which are supposed to be issued by the company. The total nominal value of all of these shares must correspond to the amount of the company's legal capital. The nominal value of a share must be expressed as a whole number unless a specific legal act states otherwise. A public joint stock company is considered a company, some or all of whose shares are publicly traded on a regulated market located in one of the member states of the Agreement on the European Economic Area. A joint stock company is regulated by Sections 154 – 220g of the Commercial Code. Pursuant to Act No. 361/2015 Coll. amending Act No. 203/2011 Coll. on Collective Investment, as amended the joint stock company with variable legal capital was transposed into our national legislation (Sections 220b – 220g of the Commercial Code). The legal capital of such joint stock company is allocated to a certain

number of shares without a nominal value. The minimum amount of the legal capital of a joint stock company with variable legal capital is EUR 125 000 unless a specific act stipulates otherwise. A joint stock company with variable legal capital may only be established for the purpose of undertaking a collective investment.

The legal capital of a simple joint stock company is allocated to a certain number of shares with a specific nominal value. The minimum amount of the legal capital which a simple joint stock company must create is EUR 1. The company may not be established based on a call for a subscription of shares. Before the company is incorporated, the entire amount of the company's legal capital must be subscribed and all of the shareholders' contributions to the company must be paid. A simple joint stock company is responsible for a breach of its obligations with its entire property, while shareholders are not responsible or liable for them. Shares of a simple joint stock company may only be issued in book-entry form and as registered shares. The foundation document or the articles of association of the company may state that the nominal value of shares is expressed in eurocents or in a combination of eurocents and euros. Shareholders of a simple joint stock company may agree on an ancillary arrangement, specifically known as a drag-along right, a tag-along right, or a right of shout out. The legal regulation of a simple joint stock company is set by Sections 220h – 220zl of the Commercial Code, while, under legal conditions, the provisions regulating the joint stock company, in the alternative, apply to a simple joint stock company.

A cooperative is not one of the legal forms of companies; on contrary, it is a society of an unrestricted number of persons established for the purpose of performing business activities or meeting the economic, social or other needs of its members. A cooperative is a society established on the principle of membership. The minimum number of members of a cooperative is 5, however, this does not apply if at least two of its members are legal persons. The cooperative is responsible for a breach of its obligations with its entire property. Members of a cooperative are not liable for the cooperative's obligations. A cooperative is obliged to create legal capital in the minimum amount of EUR 1 250. The legal capital of a cooperative is comprised of the sum of all of the contributions which the members have committed to pay. Every member of a cooperative is obligated to pay a membership or entrance contribution in the amount set by the cooperative's articles of association. The legal regulation of a cooperative is contained in Sections 221 – 260 of the Commercial Code.

Section 56(2) of the Commercial Code sets the position of legal persons established under European Union law similar to the position of Slovak companies. The legal regulation for the recognition and full adaptation of legal persons established under European Union law was incorporated into Slovak company law by the amendment to the Commercial Code effective as of 1 October 2004. [223]

European Union law introduced three new legal forms which may be established as legal persons – *a European economic interest grouping, a European company, and a European*

[223] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 157.

cooperative society. Their legal regimes in the Slovak Republic are primarily covered by regulations and secondarily covered by implementing legal acts. [224]

The legal basis of a European economic interest grouping may be found in the Council regulation on the European Economic Interest Grouping (EEIG). Pursuant to this regulation, the Act on European Economic Interest Grouping was enacted. This legal act stipulates that a European economic interest grouping is a legal person registered in the Commercial Register. The European economic interest grouping was introduced in order to simplify the cross-border cooperation of entrepreneurs and the legal regulation as such was inspired by or arose from the French legal form *Groupement d´intérêt économique*.[225]

Another legal person which may be established under European Union law is the European company. The legal basis of a European company is covered by the Council Regulation on the Statute for a European company. In the Slovak Republic, the European Company Act was adopted. Under this act, a European company is a legal person registered in the Commercial Register.[226] A European company is a supranational form of a company which may be established under European Union law. The main purpose of introducing this legal form was to provide a suitable legal form that eliminates potential obstacles for entrepreneurial activities arising from the cross-border operations of entrepreneurial legal entities. [227]

The last but not least legal person which may be established under European Union law is the European cooperative society. The legal basis of this society is provided for by the Council Regulation on the Statute for a European Cooperative Society. In the Slovak Republic, the European Cooperative Society Act was adopted. Under this act, a European cooperative society is a legal person registered in the Commercial Register.[228] The regulation of a European cooperative society is similar to the regulation of a European company. [229]

Another subject of discussion is another European legal form – the European private company which was proposed by the European Commission and submitted to the European Parliament. The proposal was designed to ensure better competitiveness for small and medium size enterprises within the European Union by the modification of the mechanism for the establishment and functioning of these companies.[230] However, this proposal was withdrawn.

The following provisions that provide a complete definition of a company are contained in Chapter II of the Commercial Code – Business of Foreign Persons. These provisions clarify the possibilities and options of foreign persons operating within the territory of the Slovak

[224] PATAKYOVÁ, M. et al. *Obchodný zákonník*. Komentár. 3rd edition, p. 157.
[225] HODÁL, P., ALEXANDER, J. *Európské právo obchodních společností (in English: European company law)*, p. 37.
[226] Section 4, the Act no. 562/2004 Coll. on European Company, as amended.
[227] HODÁL, P., ALEXANDER, J., *Európské právo obchodních společností (in English: European company law),* p. 126.
[228] Section 4, the Act no. 91/2007 on European Cooperative Society, as amended
[229] HODÁL, P., ALEXANDER, J., *Európské právo obchodních společností (in English: European company law)*, p. 38.
[230] Proposal for Council Regulation on the Statute for a European private company, p. 2.

Republic. Slovak legislation recognizes the principle of reciprocity regarding entrepreneurial activities performed by foreign persons within the territory of the Slovak Republic. Thus, foreign persons conduct their entrepreneurial activities under the same conditions as Slovak legal persons (the principal of national treatment). [231]

For the purposes of the Commercial Code, a foreign person is a natural person whose permanent residence is outside the territory of the Slovak Republic or a legal person whose registered seat is outside the territory of the Slovak Republic.[232] In other words, the location of the permanent residence or registered seat of the person is the decisive criterion. In the case of the registered seat, the registered statutory seat will be assessed, whereas the Slovak Republic follows the theory of incorporation. [233]

The entrepreneurial activity of a foreign person on the territory of the Slovak Republic means that this person has an enterprise or a branch on the territory of the Slovak Republic.[234] In the context of European Union law, the establishment of an enterprise and a branch, represent the establishment of a foreign person.[235] In the Slovak Republic, the enterprise and the branch are legal entities registered in the Commercial Register. As of the date of their registration, the foreign person acquires the entitlement to perform entrepreneurial activities in the Slovak Republic.[236]

Sections 22 and 23 of the Commercial Code also stipulate that "*a foreign person other than a foreign natural person has the same legal capacity under Slovak law as under the law under which such person was established …. the law under which such person was established also governs the foreign person's internal legal relations and their members' or shareholders' liability for the person's obligations*"[237] and "*foreign persons having the right to conduct entrepreneurial activity abroad are considered to be entrepreneurs under this act*."[238] These provisions declare the recognition of the legal personality of any entity differing from natural persons in the light of law under which was established. It follows that the legislation will respect the legal personality given by the home state to a specific entity.[239] This regulation enables the foreign law's penetration of the Slovak Republic's law. The second sentence of Section 22 of the Commercial Code declares the theory of incorporation as the legal basis for the determination of a legal person's personal status in the Slovak Republic.[240]

To provide a full picture of the company concept, it must also be interpreted in the context of Section 24 of the Commercial Code. This provision deals with the equity participation of foreign persons in Slovak legal persons. In other words, although a foreign person does not

231 PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 54.
232 Section 21 Subsection 2, the Commercial Code.
233 PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 54.
234 Section 21 Subsection 3, the Commercial Code.
235 PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 54.
236 Section 21 Subsection 4, the Commercial Code.
237 Section 22, the Commercial Code.
238 Section 23, the Commercial Code.
239 PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 55.
240 PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 56.

have an established enterprise or branch registered in the Commercial Register in the Slovak Republic, its presence in our territory exists through its equity participation in Slovak legal persons.

Under the provisions of the Commercial Code, and for the purpose of its entrepreneurial activity, a foreign person may *(i) participate in the founding of a Slovak legal person (together with other founders), (ii) become the sole founder of a Slovak legal person, (iii) participate as a shareholder or a member in an already existing Slovak legal person, or (iv) become the sole shareholder of an already existing Slovak legal person*.[241] In both cases of acquiring the participation (original participation[148] as well as derivative participation[149] of foreign legal persons in Slovak legal persons, under Section 24(3) of the Commercial Code, foreign persons have the same rights and obligations as Slovak persons.[242] The Commercial Code also states that a Slovak person may only be established under Slovak law unless a legal act or European Union law states otherwise. In such case, Section 24 Subsection 2 of the Commercial Code refers to the possibility of establishing a company under European Union law.

6.1.2 Definition of company under European Union law

European Union law stipulates a separate and uniform definition of the company. Article 54 of the TFEU constitute a legal basis of the company and provides the following: "*Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States. 'Companies or firms' means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making.*"

According to the first sentence of Article 54 of the TFEU, companies having their registered seat, central administration or principal business within the territory of any Member State, may rely on the freedom of establishment. These three types of connecting factors enable the companies to use the freedom of establishment guaranteed by European Union law in the same way as natural persons having the nationality of one of the Member States. These connecting factors determine the personal status of the company, therefore, determine the national law applicable to this company.[243]

The second sentence of this article refers to national laws of the Members States regarding the definition of the company. Under European Union law, the company means a company constituted under civil or commercial law including cooperative societies, and other legal persons established under public or private law, excluding non-profit-making entities.

[241] Section 24 Subsection 1, the Commercial Code and PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 58.
[242] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 58.
[243] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 3rd edition, p. 56.

According to the stated, the company must fulfil the characteristics required by national law of a Member State to become a company under European Union law.

Considering the previous descriptions, it may be concluded that the concept of the company under European Union law is broadly defined, whereas the freedom of establishment guaranteed by European Union law depends on the national laws of the Member States which may significantly differ. Broad interpretation of the company is also confirmed by case law of the Court of Justice of the European Union, mainly by its decision in *Cartesio*.[244]

Cartesio was a company established under Hungarian law - an entity with a similar status as the limited partnership under Slovak law.[245] This kind of company was not a separate legal entity, however, it had a legal personality in the same extent as legal persons.[246] The Court of Justice of the European Union in its decision *Cartesio* declared that despite of the specific status of this company, the matter in question concerns Hungarian companies having its own legal personality, and therefore, it is essential to interpret the concept of the company in a broad way.[247]

Chapter 6.2 Categorization of companies and their characteristic features

Legal theory categorizes companies as personal and capital. The typical features of personal companies mainly include partners' joint and unlimited liability for obligations of the company and partners' entitlement to act on behalf of the company arising from their position as partners. The existence of a company usually depends on the existing partners' participation in the company. The obligation to provide a contribution to the company and the obligation to create registered capital are not required for a company's establishment. On the contrary, capital companies are characterized by the limited liability or non-liability of shareholders for the company's obligations. Moreover, the shareholders' participation in a company as such does not entitle them to act on behalf of the company. The obligation to make a contribution to a company in a set amount, by which the registered capital of the company is created is one of the conditions for a shareholder's participation in the company. The minimum amount of the shareholder's contribution to the joint stock company is not legally set, the Commercial Code stipulates the minimum amount of the shareholder's contribution for the limited partnership and limited liability company. An unlimited company belongs to the group of personal companies. A limited liability company, a joint stock company, and a simple joint stock company are categorized as capital companies. A limited partnership has a combined character because it has features of a personal and capital type of a company. In general, a company may only be established for the purpose of entrepreneurial activity. However, a limited liability

[244] KARAS, V., KRÁLIK, A. *Právo Európskej únie (in English: European company law)*, p. 301 and PATAKYOVÁ, M. *Cartesio and its impact on processes of the registering courts in the Slovak Republic*, p. 178 and PATAKYOVÁ, M. *Legal Regulation of Companies – Unified or Variants?*, p. 276.
[245] Decision of the European Court of Justice in case *Cartesio*, para 21.
[246] PATAKYOVÁ, M. *Legal Regulation of Companies – Unified or Variants?*, p. 276.
[247] PATAKYOVÁ, M. *Legal Regulation of Companies – Unified or Variants?*, p. 276.

company and a joint stock company are exceptions, as they may also be established for other purposes than entrepreneurial activity, unless a specific act states otherwise.

6.2.1 Characteristic features of capital companies

The modern capital company did not find its place in individual legal systems until much later; however, its historical foundations can be found in the Roman period. As time went by, authors dealt with the question of the characteristic features of a capital company. Kraakman et al. identifies these five characteristic features of the modern capital company: (i) separate legal personality, (ii) limited liability or non-limited liability of partners /shareholders, (iii) transferability of business shares and shares, (iv) centralized management governed by directors/members of the board of directors, and (v) (residual) ownership of the company based on legal capital contributions.[248] *Ferran* includes the following characteristics: (i) separate legal personality, (ii) limited liability or non-liability of partners/shareholders, (iii) separation of the contribution to the company's equity from managing responsibility.[249] Eliáš considers the following characteristics: (i) obligation of contribution, (ii) obligation to create and retain the legal capital, (iii) statutory internal organization, (iv) consideration of partners/shareholders democracy, (v) transferability of shares, (vi) independence of partner's/shareholder's existence from the company, and (vii) limited liability for the company's obligations.[250] Havel, affected by the modification of company law and by the suppression of the meaning of the legal capital doctrine, inclines toward the characteristic features of the capital company defined by Kraakman et al. The above-defined characteristic features of a capital company can be found in the regulation of companies to a various extent in individual countries depending on the type of the company.

In the following text, the following defining features of a capital company will be described in detail (i) legal personality, (ii) limited liability of shareholders, (iii) transferability of business shares, (iv) separation of ownership from management (the separation of ownership from management and actions conducted on behalf of the company toward external entities).

6.2.1.1 Legal personality of a capital company

The character of a capital company depends on its legal personality, which represents one of its main features. The legal personality of a capital company is separate from the legal personality of its founders, partners/shareholders. According to Kraakman et al., equity autonomy ensuring the protection of (the equity of) the company against the claims of the company's creditors (*entity shielding*) is the core of its legal personality.[251]

[248] KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 5. *Ferran* categorizes the transferability of shares or business shares as the limited liability or non-liability of partners/shareholder and delegated management perceives as a separation of ownership and control, FERRAN, E. *Company Law and Corporate Finance*, p. 13-26.
[249] FERRAN, E. *Company Law and Corporate Finance*, p. 13.
[250] ELIÁŠ, K. *Obchodní společnosti (in English: Companies)*, p. 38.
[251] The protection of (the property) the company (*entity shielding*) arises from (i) the right of priority of company creditors if they assert claims against the property of the company, and (ii) the protection of liquidation which

In general, the legal personality allows the company: (i) to enter into contractual relationships in its own name, (ii) to own movable and immovable assets, (iii) to sue and be sued in its own name, (iv) to empower other persons to act on its behalf, and others.[252] The above-provided substantive fulfilment of the legal personality concept is only illustrative and depends on the specific law of the individual country providing the legal regulation.

The most significant theories dealing with the essence of the character of a company and its legal personality are: *(i) the theory of fiction, (ii) the theory of contract, and (iii) the theory of reality*.[253]

6.2.1.2 Limited liability of shareholders

The limited liability of a company's partners/shareholders is one of the defining features of the modern capital company. The core of this defining feature is the fact that the company's creditors may only assert claims against the property of the company and not its partners/shareholders.[254] Limited liability has not been always taken for granted,[255] but nowadays constitutes a fundamental feature of capital companies. The concept of limited liability ensures the protection of the property of partners/shareholders against the claims of the company's creditors (*owner shielding*) and represents a mirror concept for the protection of (the property) the company against the claims of the company's creditors (*entity shielding*). The concept of partners/shareholders protection (*owner shielding*) as the basis of the limited liability and the concept of the protection of (the property) the company (*entity shielding*) as the basis of the legal personality together represent the regime of the equity separation (*asset partitioning)* of partners/shareholders and the company.[256]

The defining feature of a limited liability company is its equity autonomy built on the basis that the company is responsible for its obligations with its entire property.[257] In other words, the

constitutes the absence of the possibility that the partner may require the return of its contribution and causes the liquidation of the company. KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 6 and HANSMANN, H., KRAAKMAN, R. *Organizational Law as Asset Partitioning,* p. 390.

252 KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd Edition,* p. 8 and SCHANE, S. A. *The Corporation is a Person: The Language of a Legal Fiction,* p. 563 and RIPKEN, S. K. *Corporations are People too: a Multi-dimensional Approach to the Corporate Personhood Puzzle*, p. 5.

253 See Chapter 4.1.

254 KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 8.

255 Political changes were a driving force for the incorporation of the limited liability of partners/shareholders of the capital company (a fight for protection of workers and middle class) that occurred in England in the 19th century, whereas, at that time, a limited liability was a concept perceived only on a contractual basis. The above-mentioned political pressure could have been reflected in the limited liability concept with a legal basis. The aim of this change was to popularize companies also for the middle class by limiting of the risk of investing in companies. MAHONEY, P. G. *Concept or Concession? An Essay on the History of Corporate Law*, p. 891-892.

256 KRAAKMAN, R. et al. *The Anatomy of Corporate Law: A Comparative and Functional Approach, 3rd edition,* p. 9.

257 Section 106, the Commercial Code.

company's creditors shall assert their claims primarily against the limited liability company and its property, whereas contractual relationships are concluded between a company and a specific creditor.[258]

The liability of partners/shareholders is established by law. They are liable for the company's obligations in the amount of their unpaid contribution registered in the Commercial Register as stipulated by Section 106 of the Commercial Code.[259] The partner/shareholder is liable but not responsible for the company's obligations, whereas it represents an entity separate and differentiated from the company.[260] The concept of limited liability established directly by law arises from the fact that the partner/shareholder has not fulfilled its contribution obligation to the company. The above-mentioned legal provision establishes the liability of the partners/ shareholders if they have not totally fulfilled their contribution obligation, and therefore, the partner/shareholder is in a liability relationship with the company's creditors. They are liable for the company's obligations in the amount of their unpaid contributions registered in the Commercial Register.[261] As Hanes declares, it is not possible to make a uniform theoretical justification of the limited liability concept applicable to a limited liability company; however, the basis of this justification is "*the necessary balance between the level of corporate governance and the level of responsibility*" and "*the idea of limited liability is built on the mutual direct relationship between the extent of responsibility and the level at which the partner controls assets constituting the responsibility.*" [262]

Shareholders of a joint stock company (Section 154(2) of the Commercial Code) and a simple joint stock company (Section 220h(1) of the Commercial Code) are not liable for the company's obligations during its existence.

The defining feature of capital companies (the limited liability of partners of a limited liability company and the non-liability of shareholders of a joint stock company and a simple joint stock company) is disturbed by the concept of piercing the corporate veil[263] established by Section 66aa of the Commercial Code. This concept establishes the responsibility of the controlling

[258] HANES, D. *Spoločnosť s ručením obmedzeným (in English: The limited liability company)*, p. 22-23.
[259] For details regarding the question about the limited liability of partners of a limited liability see: BLAHA, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 469-472; PALA, R. – FRINDRICH, J., PALOVÁ, I., MAJERIKOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 758-764; SUCHOŽA, J. et al. *Obchodný zákonník a súvisiace predpisy. Komentár*, p. 365-366 and MAMOJKA, M. In: MAMOJKA, M. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 425-432.
[260] SUCHOŽA, J. et al. *Obchodný zákonník a súvisiace predpisy. Komentár*, p. 366.
[261] HANES, D. *Spoločnosť s ručením obmedzeným*, p. 24.
[262] HANES, D. *Spoločnosť s ručením obmedzeným*, p. 25.
[263] Piercing the corporate veil is a concept within which (in most court cases) the concept of limited liability or non-liability is disturbed and the partners/shareholders become responsible for the obligations of the company. The doctrine of piercing the corporate veil is conducted (should be conducted) in special cases, because two main defining features of the company (i) separate legal personality of the company, and (ii) limited liability or non-liability of partners/shareholders, are disturbed. The piercing of the corporate veil may occur if a company as a legal form is abused as a masque. FERRAN, E. *Company Law and Corporate Finance*, p. 15 and KOSTOHRYZ, M. *Doktrína Piercing the Corporate Veil (in English: The Doctrine of the Piercing the Corporate Veil)*, p. 22.

person for the bankruptcy of the controlled person, and was introduced into Slovak company law by Act No. 264/2017, Coll. [264]

At the same time, Section 56(7) of the Commercial Code regulates the liability of partners /shareholders after a company ceases to exist – "*After the dissolution of the company, partners/shareholders are liable for obligations of the company in the amount of their share in the liquidation balance (Section 61(4) of the Commercial Code), however, at least in the amount to which they were liable during the existence of the company*."[265] If a company ceases to exist without liquidation, the partners/shareholder will be liable to the same extent as their liability during the existence of the company. If a company ceased to exist with liquidation and the partners /shareholders are entitled to a share in the liquidation balance, they are jointly and severally liable to the company's creditors at least in the amount of this share, even if they were liable to a lesser extent or not at all liable during the existence of the company.[266]

6.2.1.3 Transferability of business share/shares

The transferability of a business share (shares), which is one of the main characteristics of a capital company, allows a company to conduct its business continuously, although its ownership (shareholders) may change; in other words, the company as a legal entity is an autonomous entity from its shareholders who are only residual owners. However, this does not mean that a business share (shares) may be transferable without restrictions. The full transferability of a shareholder (i) supports liquidity for shareholders, (ii) allows them to diversify their investments in different companies and (iii) maximizes the acquisition of own funds. There are various forms of the limitation to or exclusion of the transferability of business shares (shares) among capital companies and their individual forms. Depending on the degree of limitation of the transferability of the shares, we can speak of open companies or closed companies, and with regard to the possibility of the public trading of shares, we can classify them as private companies or public companies.

A joint-stock company is by nature an open-ended capital company; its shares may also be traded on a public market, and the transferability of the shares may be limited, but not prohibited. According to the de lege lata status (the Securities Act), a share as a security is a money-valued record in the form stipulated by law (Section 2 of the Securities Act). This entry shall be recorded on the deed or in the register kept by the Central Depository. Shares issued

[264] For details regarding the question of the piercing of the corporate veil under Section 66aa of the Commercial Code see: MAŠUROVÁ, A. *Zodpovednosť štatutárov, faktických štatutárov a tieňových štatutárov kapitálových spoločností voči veriteľom spoločností podľa novej úpravy Obchodného zákonníka a zákona o konkurze a reštrukturalizácii (in English: Responsibility of members, de facto members and shadow members of a capital company statutory body against company creditors under the new regulation of the Commercial Code and the Bankruptcy and Restructuring Act)*.

[265] For more details regarding the question of shareholder liability after a company ceases to exist see: CSACH, K. In: OVEČKOVÁ, O. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 375-376; SUCHOŽA, J. et al. *Obchodný zákonník a súvisiace predpisy. Komentár*, p. 204ł ĎURICA, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 239-240 and KUBINEC, M. In: MAMOJKA, M. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 188.

[266] CSACH, K. In: OVEČKOVÁ, O. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 375-376.

by a Slovak joint-stock company to be traded on an exchange must be in the form of a book-entry security (Section 29(1) of the Stock Exchange Act) and their transferability may not be limited. The Stock Exchange may grant an exemption within the meaning of Section 29(3) of the Stock Exchange Act: *"For registered shares whose transfer is subject to the consent of the issuer's bodies, the condition of unrestricted transferability shall be deemed to be fulfilled if the requirement for approval of the issuer's bodies (Section 156(8) of the Commercial Code) does not hinder trading in the relevant stock exchange."* However, such a possibility is prohibited by the Commercial Code itself, which stipulates that the transferability of shares admitted to trading on a stock exchange may not be restricted (Section 156(9) of the Commercial Code). Upon the transformation of a private joint stock company to a public limited company, any restriction of the transferability of registered shares in the private joint stock company on a day of trading on the stock exchange becomes void. Restrictions on the transferability of shares are entered in the Commercial Register.

The transferability of shares can be completely prohibited in a simple stock company, i.e. the circulation function of a share as a security can be completely suppressed. Such prohibition or limitation of the transferability of shares of a simple company is entered in the Commercial Register.

A limited liability company is a private company with a (mainly) closed nature. The transferability of a business share in a limited liability company is primarily addressed in Section 115 of the Commercial Code. Pursuant to Section 115(1) of the Commercial Code, the transfer of a business share within a limited liability company requires the approval of the company's general meeting. However, the shareholders may avoid the need for the general meeting to approve such transfer in its articles of association. The consent of the general meeting when transferring a business share to another shareholder can prevent the disturbance of ownership as well as other relations between shareholders in the company. On the other hand, the transfer of a shareholding within a limited liability company to a person other than another shareholder must be expressly provided for in the articles of association, with the requirement that such a transfer be subject to the prior consent of the general meeting. The above causes the classification of a limited liability company as a closed company, as the default provision tends to exclude the transfer of a shareholding to a third party. The transferability of a share may be limited by law or by an agreement of the shareholders with respect to the rights that affect the transferability of shares.

6.2.1.4 Separation of ownership from control of a company

The separation of ownership from the management/control of a company (*separation of ownership and control*) is another defining feature of a capital company. The partner/shareholder is in the position of residual owner, whereas it achieves benefits from the company only if the claims of the company's creditors, employees, state and of other entities are met. The company's statutory body interpreting the will of the company to external entities, acts on behalf of the company towards such external entities, whereas the company as a legal

entity does not have "*hands and mouth.*"[267] The mechanism creating the will of the company depends on the specific form of the company. The concept of the separation of ownership and control was described in detail by Berle and Means who determined that the governance and control of a company are in the hands of those persons who do not own the company and are not its majority partners/shareholders.[268]

The control and ownership of a capital company are separated. In the context of Slovak company law, it means that the ownership of the company is separated from the management of the company and from acting on behalf of the company towards external entities, whereas it is a capital and not personal company.[269] Only a natural person may be the statutory body of a limited liability company,[270] but this person does not have to be a partner.

The management of a company may be determined as an internal competence,[271] within which the will of the company is created and subsequently reflected in legal acts taken by the company's directors as statutory bodies or by other persons acting on behalf of the company on the basis of a legal or contractual empowerment. Although the management of a company is the main element of the company's conduct towards external entities, not every company's management is reflected in legal acts conducted towards external legal entities.

It is not possible to define management in the context of companies. Its content varies depending on the size of the company or the size of the company's enterprise, the subject of the entrepreneurial activity, the organizational structure, and others, and therefore, it constitutes an open concept of company law.[272] To define and precisely determine the concept of the company's management would lead to the limitation of the necessary openness of this concept which is essential with regard to the various creations of the will within a company.

Pursuant to Section 134 of the Commercial Code, the management of a limited liability company is in the hands of its directors. This provision also establishes the fundamental criteria for the performance of decisions handled by directors within the management of the

267 FERRAN, E. *Company Law and Corporate Finance*, p. 11 and PETRIN, M. *Reconceptualising the Theory of the Firm – from Nature to Function*, p. 4.
268 BERLE, A. A., MEANS, G. C. *The Modern Corporation and Private Property*, p. 5.
269 For more details regarding the question of corporate governance of a limited liability company see: PATAKYOVÁ, M., GRAMBLIČKOVÁ, B., BARKOCI, S. *Obchodné vedenie a jeho (potenciálne?) vplyvy na právne úkony v mene spoločnosti (in English: Corporate governance and its (potential) effects on legal acts on behalf of a company).*
270 Section 133 Subsection 2, the Commercial Code.
271 For more details regarding the question of corporate governance of a limited liability company see: BLAHA, M. In: PATAKYOVÁ, M. et al. *Komentár: Obchodný zákonník. 5th edition*, p. 589-590; PALA, R., FRINDRICH, J., PALOVÁ, I., MAJERIKOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 958-961; SUCHOŽA, J. et al. *Obchodný zákonník a súvisiace predpisy. Komentár*, p. 415-416 and MAMOJKA, M. In: MAMOJKA, M. et al. *Obchodný zákonník: Veľký komentár. Zväzok I (§ 1-260)*, p. 531-533.
272 HAVEL, B. *Obchodní korporace ve světle proměn: Variace na neuzavřené téma správy obchodních korporací*, (in English: Companies in the light of changes: Alternative on unclosed topics of the corporate governance) p. 79.

company.[273] At the same time, a company may be managed by (i) the general meeting pursuant to Section 125(1)(k) or Section 125(3) of the Commercial Code and specified in the foundation document, the articles of association or in a non-corporate document, (ii) the supervisory board, according to stipulations in the foundation document, the articles of association or a non-corporate document, or (iii) another body created within the company based on specification provided in the foundation document, the articles of association or a non-corporate document.[274] If the management of the company is performed by the general meeting, the criteria for such performance is established by Section 127 of the Commercial Code. If a company is managed by the supervisory board, Section 66(8) of the Commercial Code shall apply. If the management of the company is in the hands of another body, the criteria for such management should be specified by the foundation document, the articles of association or a non-corporate document.[275]

However, the essential moment is the expression of the created company's will to the external world in the form of its conduct towards external entities. The statutory body – director(s) is responsible for acting on behalf of a limited liability company towards external entities. As stated above, only a natural person may be the director of a limited liability company, but this person does not have to be a partner. Pursuant to Section 135a(1) of the Commercial Code, directors are under the obligation to carry out their duties with professional care and in compliance with the interests of the company and all of its partners. Thus, it may be concluded that in the case of a limited liability company, the characteristic feature of a capital company is manner of the separation of ownership and control, and thus giving rise to the separation of ownership from company management and the company's conduct towards external entities. However, potential interventions into the management of directors by the general meeting or other company bodies cannot not be rule out.

The issues of "governance", i.e. decision-making in a joint-stock company, are among the key aspects of its management (governance and control). The statutory setting of the decision-making and control mechanisms in this company corresponds to the essence of the company as a corporation with the highest degree of internal organization, but without distinction between a public and a private joint-stock company (Section 154(3) of the Commercial Code). The general meeting, as the body representing all shareholders, decides on the most important issues in the life of the company. The competence of the general meeting is defined by law as obligatory [Section 187(1) (a-j) of the Commercial Code]. However, the general meeting of a joint stock company is not entitled to decide on *ad hoc* matters (as opposed to Section 125 (3) of the Commercial Code in a limited liability company); the discretionary extension of the

[273] PATAKYOVÁ, M., GRAMBLIČKOVÁ, B. - BARKOCI, S. *Obchodné vedenie a jeho (potenciálne?) vplyvy na právne úkony v mene spoločnosti (in English: Corporate governance and its (potential) effects on legal acts on behalf of the company)*, p. 19.
[274] PATAKYOVÁ, M., GRAMBLIČKOVÁ, B., BARKOCI, S. *Obchodné vedenie a jeho (potenciálne?) vplyvy na právne úkony v mene spoločnosti (in English: Corporate governance and its (potential) effects on legal acts on behalf of the company)*, p. 19.
[275] PATAKYOVÁ, M., GRAMBLIČKOVÁ, B., BARKOCI, S. *Obchodné vedenie a jeho (potenciálne?) vplyvy na právne úkony v mene spoločnosti (in English: Corporate governance and its (potential) effects on legal acts on behalf of the company)*, p. 21-23.

scope of the general meeting must be determined by the articles of association in a sufficiently specific manner. Decisions on amendments to the articles of association do not need to be exclusively within the competence of the general meeting if so provided by law. The provisions of the Commercial Code imply this change from the regulation of cross-border mergers (Section 218lf of the Commercial Code). In cases stipulated by law, the general meeting is entitled to delegate power to other bodies of the company to decide on certain issues. The legal framework implies an implicit prohibition on the delegation of powers to other matters and to authorities other than in explicitly defined cases. The express statutory authorization relates to the election of the members of the board of directors and their remuneration by the supervisory board (Section 194(1) of the Commercial Code, Section 66(3) of the Commercial Code, Section 187 of the Commercial Code) and the entitlement to increase the registered capital by the board of directors (Section 210 of the Commercial Code).

In addition to the authority to act on behalf of the company, members of the board of directors have decision-making power on strategic issues (compare to *Societas Europeae*) and management, manifesting itself in corporate governance; i.e. in business management. Corporate governance is reflected in the power of the board of directors to make decisions on all matters that are not reserved by law or by the articles of association to the competence of the general meeting or the supervisory board. The decision-making powers of the board of directors are defined in a general manner and in relation to other statutory bodies. The powers of the supervisory board to decide on company matters are explicitly permitted by law. The decisions of the board of directors as the company's governing body are, in principle, subordinated to the decisions of the general meeting of a joint-stock company as the company's supreme governing body. For this reason, they have an internal character and courts are not authorized to intervene in these decisions due to the absence of specific substantive provisions. In statutory cases where a company is authorized by its autonomous regulation in its articles of association to delegate the powers of the general meeting to the board of directors (Section 194 of the Commercial Code, Section 210 of the Commercial Code) it is implicitly permissible to apply by analogy the legislative invalidity of a resolution of the general meeting (Section 183 of the Commercial Code, Section 131 of the Commercial Code) concerning decisions taken by the board of directors while exercising the powers of the general meeting.

Revision questions:

1. *How does Slovak law define a company?*
2. *What types of companies can be incorporated under Slovak law?*
3. *Do companies established under European Union law have a status similar to that of Slovak companies?*
4. *How does the law of the European Union define a company?*
5. *Which companies are classified as personal companies?*
6. *Which companies are classified as mixed companies?*
7. *Which companies are classified as capital companies?*
8. *What are the basic characteristics of capital companies?*
9. *Describe the limited liability of shareholders in the context of the characteristics of capital companies.*
10. *Describe the transferability of the business share / shares in the context of the characteristics of capital companies.*
11. *Describe the separation of ownership from corporate governance in the context of the characteristics of capital companies.*

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Part VII. Definition and characteristics of cooperatives

Chapter 7.1 Basic characteristics of a cooperative

The basic attributes of a cooperative are the openness of membership and the related variability in the amount of the membership contribution of cooperative members. Unlike shareholders in companies, a cooperative member has the right to unilaterally terminate their participation in the cooperative. As far as cooperative bodies are concerned, the specificity of a cooperative lies mainly in the mandatory cooperative self-government and cooperative democracy, which is *de lege lata* regulated by default provisions.[276] Cooperative democracy consists mainly in the fact that resolutions at members' meetings are passed by a majority of votes, where, unlike the system in companies, each cooperative member has one vote regardless of the amount of their contribution.[277]

A cooperative may be established for the purpose of doing business, but also for meeting the economic, social or other needs of its members. A cooperative should not be confused with a company. Its primary purpose is not the creation of a business entity but an organization that serves its members. In addition, the cooperative's legislation allows for the smooth entry and exit of its members, which is not possible in most companies.[278]

It is therefore typical for a cooperative to easily exchange members without changing its corporate documents or affecting its existence, provided that the minimum number of members is maintained.[279] The basic characteristics and purpose of a cooperative are stipulated in Section 221(1) of the Commercial Code: *A cooperative is an association of an unrestricted number of parties that is founded for the purpose of entrepreneurial activity or securing the economic, social or other needs of its members.* It is clear from the above definition that, unlike most trading companies that are established solely for the purpose of making a profit, a cooperative may have both an entrepreneurial and a social character. Such cooperatives prevail in practice.[280]

A cooperative can be categorized according to various criteria. From a functional point of view, we distinguish between housing, consumer, production and agricultural cooperatives, for which the law partially regulates specific provisions. In terms of organizational structure, the Commercial Code distinguishes between cooperatives and small cooperatives. Finally, reference should be made to the transnational form of cooperative which is governed by Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative

[276] Compare NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 975; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1610.
[277] HELEŠIC, F. *Základy teorie evropského a českého družstevního práva*, p. 227.
[278] PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1610.
[279] Compare JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1007; PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 820.
[280] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1006.

Society (SCE) as well as European Cooperative Act No 91/2007 Coll. of 6 February 2007. However, this legislation is not covered by this Chapter.

Pursuant to Section 260 of the Commercial Code the general provisions of the Commercial Code shall apply to cooperatives unless special provisions on cooperatives provide otherwise.

Chapter 7.2 Legal personality of a cooperative

Pursuant to Section 222(1, first sentence) of the Commercial Code, a cooperative is a legal entity. The founding meeting of the cooperative replaces the agreement (memorandum) of association or the deed of association, which is a condition for the establishment of a company.[281] According to Section 225(1, first sentence) of the Commercial Code, a cooperative, as a legal entity, is founded on the day of its registration in the Commercial Register. Like a joint stock company and a limited liability company, a cooperative has entrepreneurial status within the meaning of Section 2(2a) of the Commercial Code regardless of whether in a particular case it conducts business activities, due to the fact that the legislation of the Commercial Code applies the formal principle of the status of entrepreneur.[282] The board of directors is obliged to file the application for registration.[283] The application for registration must be signed by all of the members of the board of directors. Under Section 221(2) of the Commercial Code, the business name of a cooperative must contain the designation '*družstvo*' (cooperative).

Pursuant to Section 254(1) of the Commercial Code, a cooperative is dissolved upon its deletion from the Commercial Register. The deletion must be preceded by the winding-up of the cooperative with or without liquidation. Pursuant to Section 254(2) of the Commercial Code, a cooperative is wound up:
a) by a decision of the members' meeting stating whether the cooperative is being wound up with liquidation or without liquidation and with a legal successor in accordance with Section 255 of the Commercial Code;[284]
b) upon the cancellation of bankruptcy after the fulfilment of the distribution decision, upon the cancellation of bankruptcy because the bankrupt's property is insufficient to pay the expenses and remuneration of the bankruptcy trustee, upon the dismissal of a petition in bankruptcy due to a lack of property, upon the discontinuation of bankruptcy proceedings due to a lack of property, upon the cancellation of bankruptcy due to a lack of property, or upon the cancellation of bankruptcy after the fulfilment of the final distribution of the proceeds;
c) by a court decision;[285]

[281] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1014.
[282] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1007.
[283] Section 225 Subsection 2, the Commercial Code.
[284] Pursuant to Section 254(3) of the Commercial Code, the decision of the members' meeting on winding-up must be certified by a notarial deed.
[285] Upon a petition by a state authority, body or member of the cooperative, or upon a petition by a person able to prove a legal interest, or on its own initiative, according to Section 257(1) of the Commercial Code, the court shall decide on the winding-up of the cooperative if

d) upon the lapse of the period for which the cooperative was established; or
e) upon achieving the purpose for which the cooperative was established.
According to Section 258(1) of the Commercial Code, the members' meeting may decide that a cooperative established for a definite period of time shall continue its activity even after the expiry of such period of time. However, under Section 258(2) of the Commercial Code, this decision must be made before the distribution of the liquidation balance begins.

Chapter 7.3 Separation of ownership of a cooperative from the ownership of its members

7.3.1 Legal Capital

As in the case of commercial companies, the property of a cooperative is separated from the property of its members after the formation of the cooperative. Like a company, a cooperative is obliged to create legal capital, which together with the indivisible fund represents its *primary assets*. According to Section 223(1) of the Commercial Code, the cooperative's legal capital consists of the aggregate of membership contributions which the members of the cooperative have committed to pay.

The (real) legal capital of the cooperative within the meaning of Section 223(1) of the Commercial Code must be differentiated from the legal capital which is entered in the Commercial Register (registered legal capital). The articles of association determine the amount of the cooperative's legal capital, while, in accordance with Section 223(3) of the Commercial Code, the registered legal capital must be at least EUR 1,250. Before the incorporation of a cooperative, the founding meeting of the cooperative determines the registered legal capital and approves the Articles of Association.[286] The distinction between the (real) legal capital and the

a) the number of cooperative members has declined to less than the number determined in Section 221(3) of the Commercial Code;
b) the total membership contributions has declined to less than the sum stipulated in Section 223(2) of the Commercial Code (here Section 223(3) of the Commercial Code should stand, compare NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 1022);
c) six months have passed from the expiration of the termination date of office of the cooperative's bodies and new bodies have not been elected, or if the obligation to convene the members' meeting of the cooperative was not fulfilled within such period, or if the cooperative has not conducted any activity for a period of more than six months;
d) the cooperative has breached the obligation to create an indivisible fund;
e) the cooperative has breached the provision of Section 56(3) of the Commercial Code, i.e. if a cooperative has an activity registered as a subject of business that under special regulations may only be carried out by natural persons, such activity may only be carried out by a company through the persons qualified to do so under special regulations (the legal provision here incorrectly refers to Section 56(3) of the Commercial Code instead of Section 56(4) of the Commercial Code);
f) the foundation or merger of the cooperative was in breach of the law; or
g) the cooperative has not fulfilled the obligation to deposit individual financial statements in the Collection of Documents for at least two accounting periods.
If the court decides on the winding-up of a cooperative, prior to the decision on winding-up, in accordance with Section 257(2) of the Commercial Code, the court shall determine a period for rectifying the grounds on which the winding up was proposed, provided it is possible to rectify such grounds.
286 Section 224 Subsections 2a and 2b, the Commercial Code.

registered legal capital is another specific feature of a cooperative, which is related to the fact that, in contrast to company law, cooperative legislation provides for a much more flexible possibility for the exit and exclusion of its members. While, unless there is a change in the articles of association, the registered legal capital constitutes a fixed value, the (real) legal capital, which consists of the sum of membership contributions, will vary depending on the number of members of the cooperative.[287] The relatively easy possibility of changing members of a cooperative is related to the possibility of flexibly changing its legal capital, as each entry of a new member (without a legal predecessor) entails the obligation to provide a membership contribution to settle the property, and with each termination of membership (without a legal successor) the cooperative is obliged to make a property settlement with the former member (or his heir).[288] Entry into a cooperative is not subject to a change in the legal capital, as opposed to the original acquisition of shareholding in companies after their formation.[289]

Pursuant to Section 225(1, second sentence) of the Commercial Code, before filing an application for registration, at least half of the registered legal capital must be paid. Pursuant to Section 223(9) of the Commercial Code, the articles of association of a cooperative or a members' meeting may authorise the board of directors to decide on the increase of legal capital to a certain amount from the net profit or from other resources of the cooperative's equity that are not earmarked in an indivisible fund or other funds. The cooperative members participate in the increase according to the amount of their existing investment contributions, unless the articles of association stipulate otherwise. Since the *real* legal capital is not entered in the Commercial Register or in the articles of association, there is *de facto* only an accounting update of the value of the legal capital.[290]

If necessary, in order to cover a loss of the cooperative which cannot be covered from other resources, a members' meeting may decide on the reduction of the legal capital and on the proportional reduction of membership contributions.

7.3.2 Membership contributions

Ownership interest which a member has contributed to a cooperative in the form of a monetary or non-monetary membership contribution become the property of the cooperative.[291] Pursuant to Section 223(2, fourth and next sentence) of the Commercial Code, the amount of membership contribution may be determined differently for individual members, but each amount must be expressed in a positive integral number, unless the law stipulates otherwise. The total sum of the nominal values of membership contributions to the cooperative must equal the nominal

[287] PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 825.

[288] NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 979; PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 820.

[289] PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1610.

[290] NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 983.

[291] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1035; NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 1001; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1617.

value of the cooperative's legal capital. As in the case of companies, both monetary and non-monetary contributions may be invested in the cooperative's legal capital.

Non-monetary contributions are appraised in the manner determined in the articles of association or as agreed by all of the members during the foundation of the cooperative. If the object of a non-monetary contribution comprises participation certificates issued by the cooperative under a special Act, they are to be included in the member's investment contribution in their nominal value. Unlike companies, Section 59(3, second sentence) of the Commercial Code does not apply to a cooperative,[292] i.e. the value of the non-monetary contribution need not be determined by an expert opinion.[293]

If permitted by the articles of association, pursuant to Section 223(5) of the Commercial Code, members of a cooperative may commit themselves to an additional membership contribution and an additional asset participation in the cooperative's entrepreneurial activity under the conditions determined by the articles of association. According to Section 223(7) of the Commercial Code, a member is obliged to pay the membership contribution exceeding the entry contribution within three years, unless the articles of association determine a shorter period.[294] The articles of association may determine that members are obliged, if required by the cooperative's loss, to pay the unpaid part of their membership contribution even before its due date, based on a decision of the members' meeting.

According to Section 223(8) of the Commercial Code, a cooperative may not return membership contributions to their members or pay interest on the members' contributions, unless the law provides otherwise.

Chapter 7.4 Legal status of cooperative members

7.4.1 Membership principle

The basic principles of membership in a cooperative are the principles of voluntariness and equality, both at the beginning and at the end of membership.[295] The principle of voluntariness is manifested not only in connection with the establishment of membership in a cooperative, but unlike commercial companies, in connection with the unrestricted exit right provided for in Section 231(2) of the Commercial Code. The principle of equality applies *de lege lata* only in a limited form because the default legislation allows different amounts of ownership interest of cooperative members and permits the regulation of the articles of association regarding the

[292] Section 223 Subsection 6, the Commercial Code.
[293] See also JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1012.
[294] The Act does not explicitly regulate when the period in question begins to run. In the event that the beginning of the period is not expressly provided for in the articles of association, we consider that the period will begin at the moment of the formation of the cooperative or at the moment the member joins the cooperative, compare JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1012.
[295] PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 838.

weighting of members' votes according to the size of their ownership interest; this makes the cooperative closer to companies.[296]

According to Section 221(3) of the Commercial Code, a cooperative must have at least five members; this shall not apply if at least two of its members are legal entities. The joining of additional members or the termination of membership of existing members shall not affect the existence of the cooperative, provided that it fulfils the conditions of the previous sentence.

Pursuant to Section 227(1) of the Commercial Code, the members of a cooperative may be natural persons and legal entities. If, under the articles of association, membership is conditional upon an employment relationship with the cooperative, a natural person who has completed mandatory school attendance and attained 15 years of age may become a member. The Commercial Code does not stipulate any other restrictions on membership in a cooperative.[297]

Under Section 228 of the Commercial Code, a cooperative shall keep a list of all of its members, but it is not deposited in the Collection of Documents of the Commercial Register and it has no effect on the formation of the cooperative membership or on the creation of rights associated with membership.[298] In addition to the name and registered office of a legal entity or the name and residential address of a natural person as a member, the list shall also contain the amount of their membership contribution and the amount which has been paid. All changes to the registered facts must be made in the list without undue delay. The board of directors must allow any party that proves a legal interest to inspect the list.[299] A member of the cooperative has the right to inspect the list, and the cooperative is obliged, upon the member's request, to issue them a confirmation of membership and of the content of their entry in the list.

Members of a cooperative are not registered in the Commercial Register. Only the notarial deed of the founding meeting of the cooperative, which is attached to the application for registration of the cooperative in the Commercial Register and which, among other items, contains the names of the founding members and the total amount of the contributions to which they have committed shall be deposited in the Collection of Documents. Other changes in the membership base and members' ownership interest are not registered.[300]

The body in which the members of the cooperative are associated and which constitutes the platform for the exercise of the membership property and non-property rights is the members' meeting. For more information on the rules of the members' meeting and the conditions for exercising the non-property rights of cooperative members, see Chapter 7.6. Responsible management of the cooperative. For the individual property rights of cooperative members, see chapter 7.4.5. Property rights resulting from membership in a cooperative.

296 Ibid.
297 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1019.
298 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1021.
299 For example, a person who wishes to acquire membership rights by transferring membership and therefore wants to verify that the transferor is really a member of the cooperative. See JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1020.
300 PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1632.

7.4.2 Membership share

According to Section 223(2, first to third sentences) of the Commercial Code, the membership share constitutes the extent of a member's participation in the cooperative. Its amount is determined based on the proportion of the membership contribution to the cooperative's legal capital, unless the articles of association determine otherwise. Each member may have only one membership share in the cooperative.

Based on default legislation, the amount of the contribution of a cooperative member has an impact on the amount of the share in profit pursuant to Section 236(2) of the Commercial Code, on participation in the share in the increase of the legal capital pursuant to Section 223(9) of the Commercial Code, on the amount of the settlement share pursuant to Section 233(2) of the Commercial Code, as well as on the amount of the liquidation balance pursuant to Section 259(3) of the Commercial Code, but not on the number of votes at the members' meeting pursuant to Section 240(1) of the Commercial Code.[301] Despite the default nature of the above provisions, in the event of derogation in the articles of association it is necessary to comply with Section 56a of the Commercial Code on the prohibition of disadvantages for individual cooperative members in an abusive manner.[302] Another possible corrective instrument in this respect is the legal arrangement of good manners pursuant to Section 39 of the Civil Code and the prohibition of the abuse of rights pursuant to Section 265 of the Commercial Code.[303]

In the event of the death of a natural person who is a member of the cooperative, the cooperative shall reduce the legal capital by the contribution of such member, unless the membership has passed to an heir or, if applicable, to another legal entity or natural person. In the event of the dissolution of a legal entity that is a member of the cooperative, the cooperative shall reduce the legal capital by the contribution of such member, unless the membership has passed to another natural person or legal entity.[304] Thus, unlike companies, the Commercial Code does not allow for the creation of the legal arrangement of a 'free' membership share in a cooperative which would be transferred to the cooperative.[305]

[301] Compare PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1618 and 1620.
[302] NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 978; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1645 and 1649.
[303] Compare JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1009; PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 823.
[304] Section 223 Subsection 10, the Commercial Code.
[305] NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 982; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1617.

7.4.3 Establishment of membership

7.4.3.1 General

Upon fulfilment of the conditions arising from the law and articles of association, pursuant to Section 227(2) of the Commercial Code, membership in a cooperative is established in the following cases, while more detailed regulation of the membership, its establishment and termination are regulated in the Articles of Association:[306]
a) during the foundation of the cooperative, on the date of establishment of the cooperative;
b) during the existence of the cooperative, by accepting a member based on a written membership application;
c) by transfer of membership; or
d) in another manner stipulated by law.

The cooperative's articles of association must stipulate the regulations for the establishment and termination of membership, the rights and obligations of members towards the cooperative and the rights and obligations of the cooperative towards its members. The articles of association must also stipulate the amount of the basic membership contribution, and the amount of the entry contribution, if applicable, the manner of payment of membership contributions and settling the membership shares upon termination.[307] If, under the articles of association, a condition for membership is the member's employment relationship with the cooperative, in accordance to Section 226(2) of the Commercial Code, the articles of association may contain the regulation of such relation. This regulation must not be contrary to labour law regulations, unless it is more favourable for the member. If the articles of association do not contain any special regulation, labour law regulations shall apply. If, under the articles of association, a condition of membership is the member's employment relationship with the cooperative and if it does not follow otherwise from the articles of association, under Section 227(3) of the Commercial Code the membership is established on the agreed date of establishment of the employment relationship, and is terminated on the date of termination of the member's employment relationship with the cooperative. It is important to point out that membership in a cooperative shall not be established in any way before the payment of the entry contribution.[308]

306 Section 227 Subsection 5, the Commercial Code.
307 Section 226 Subsections 1c and 1d, the Commercial Code.
308 Section 227, Subsection 4, the Commercial Code.

7.4.3.2 Establishment of membership upon the formation of a cooperative

According to Section 224(1) of the Commercial Code, the founding meeting of a cooperative must be held. The founding meeting shall adopt decisions by a majority of persons in attendance.[309] Persons who have filed an application to the cooperative are entitled to vote at the founding meeting of the cooperative.[310] According to Section 224(4, second sentence) of the Commercial Code, a membership applicant may withdraw their application immediately after voting on the articles of association, if they voted against their adoption. The founding meeting of the cooperative shall lead to the foundation thereof, provided that, in accordance with Section 224(5, first sentence) of the Commercial Code, the membership applicants have committed themselves at the meeting to membership contributions attaining the determined sum of the registered capital. The course of the founding meeting of the cooperative is certified by a notarial deed which also contains the list of members and the amount of individual membership contributions to which the members committed themselves at the cooperative's meeting. The approved wording of the articles of association forms an annex to the notarial deed.[311]

The condition for establishing membership upon the formation of a cooperative is in accordance with Section 223(4) of the Commercial Code, and the payment of the membership contribution (entry contribution) or a certain part of the basic membership contribution (basic membership contribution) is determined by the articles of association. The articles of association may determine different amounts of the basic membership contribution or entry contribution for natural persons and for legal entities. The basic membership contribution or entry contribution must be paid to the designated member of the board of directors in the manner determined by the members' meeting within 15 days from the founding meeting of the cooperative.[312]

7.4.3.3 Establishment of membership during the existence of a cooperative

7.4.3.3.1 Establishment of membership by admission on the basis of a written membership application

The condition of the establishment of membership after the submission of the application by the applicant is its acceptance by the board of directors of the cooperative, if pursuant to Section 239(5) of the Commercial Code, the articles of association do not determine that the acceptance of applications is within the competence of the members' meeting. A cooperative may refuse an application without stating a reason,[313] unless the articles of association provide otherwise in that regard and unless such refusal is not discriminatory to a particular group of persons.[314]

309 Section 224 Subsection 4 first sentence in fine, the Commercial Code.
310 Section 224 Subsection 3 first sentence, the Commercial Code
311 Section 224 Subsection 6, the Commercial Code.
312 Section 224 Subsection 5 second sentence, the Commercial Code.
313 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1020; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1631.
314 PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 825.

7.4.3.3.2 Establishment of membership by transfer of membership rights and obligations

This is a method of acquiring membership from a legal predecessor. For more on this, see chapter 7.5. Transfer of membership rights and duties.

7.4.3.3.3 Establishment of membership in another manner stipulated by law

The Act regulates, in particular, the acquisition of membership on the basis of a transfer pursuant to Section 232(4) of the Commercial Code, as a result of the mergers or division of a cooperative under Section 256(1) of the Commercial Code or as a result of the change of legal form of a company into a cooperative under Section 69b of the Commercial Code.[315]

7.4.4 Termination of membership

7.4.4.1 General

In addition to the termination of membership on the basis of the transfer of membership rights and obligations to a third party, the membership is terminated primarily by written agreement, resignation, expulsion, declaration of bankruptcy against the member's property, dismissal of a petition in bankruptcy due to a lack of the member's property or by the dissolution of the cooperative,[316] as well as in certain cases by the death or dissolution of the cooperative member.[317] A special case of membership termination is governed by Section 227(3) of the Commercial Code, according to which the membership terminates on the date of termination of the employment relationship of the member with the cooperative, if, under the articles of association, a condition of membership is the member's employment relationship with the cooperative and if it does not follow otherwise from the articles of association.

Pursuant to the older case law of the Supreme Court of the Slovak Republic, the statutory means of termination of membership cannot be extended by other reasons in the articles of association.[318]

7.4.4.2 Termination of membership by transfer of membership rights and obligations to a third party

For more on this possibility, see chapter 7.5. Transfer of membership rights and duties.

315 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1020; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1631.
316 Section 231 Subsection 1, the Commercial Code.
317 Section 232 Subsections 1 to 4, the Commercial Code.
318 Decision of the Supreme Court of the Slovak republic, case 7 Obdo V 29/95.

7.4.4.3 Termination of membership by written agreement

This is an agreement between a member and a cooperative, the content of which is the agreement to terminate the member's membership in the cooperative. The agreement must be concluded in writing. The membership ceases to exist upon the entry into force of the membership cessation agreement, which also results in a reduction in the *real* legal capital by the membership contribution of the outgoing member.[319]

7.4.4.4 Termination of membership by resignation

According to Section 231(2) of the Commercial Code, the membership is terminated by resignation within the period determined by the articles of association, but at the latest six months from the date on which the member notified the cooperative's board of directors in writing of their resignation. This is a unilateral legal act of a member addressed to the cooperative in writing. This right of a member cannot be taken away by the articles of association.[320]

7.4.4.5 Termination of membership by expulsion

Pursuant to Section 231(3) of the Commercial Code, a member may be expelled if they repeatedly breach membership obligations despite being warned, or for other material reasons stated in the articles of association, such as a member's failure to pay the rest of the membership contribution within the deadline.[321] A natural person may also be expelled if they were lawfully convicted of an intentional criminal offence committed against the cooperative or a member thereof. Unless determined otherwise by the articles of association, the board of directors shall decide on the expulsion, of which the member must be notified in writing. The member is entitled to appeal the decision on expulsion at the members' meeting. Upon a petition of the member affected by the decision, the court shall declare the decision of the members' meeting on expulsion to be invalid if it is contrary to the law or the articles of association.[322]

Expulsion is a unilateral act by a cooperative addressed to a member. Unless otherwise provided in the articles of association, the effects of the termination of membership shall take effect upon the delivery of the decision on expulsion to the cooperative member. In the event that the member's meeting declares the decision to expel a member invalid, that decision would have an *ex tunc* effect. If the articles of association do not provide for a time limit for filing an appeal to the member's meeting,[323] for reasons of legal certainty, the general limitation period according to Section 397 of the Commercial Code should apply. In the event that an application

[319] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1026.
[320] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1027; PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1638.
[321] PEKÁREK, M., ŠTENGLOVÁ, I. In: ŠTENGLOVÁ, I., PLÍVA, S., TOMSA, M. et al. *Obchodní zákoník. Komentář*. 13th edition, p. 825.
[322] Section 231 Subsection 4, the Commercial Code.
[323] According to decision of the Supreme Court of the Czech Republic, sp. zn. 32 Cdo 2230/99, the Articles of Association cannot determine a specific time limit in that context.

for a decision of a member's meeting on expulsion from a cooperative is lodged with the court and the relevant time limit cannot be specified in the articles of association, the general limitation period according to Section 391(2) and Section 397 of the Commercial Code shall apply.[324]

7.4.4.6 Termination of membership by declaration of bankruptcy against the member's property and dismissal of a petition in bankruptcy due to the member's lack of property

The purpose of the provision in question is to enable the creditors of a member to obtain satisfaction of their claims, since upon the termination of membership in the event of the bankruptcy of a member's property, the member is entitled to a settlement share, which becomes part of the bankruptcy estate. The term *dismissal of a petition in bankruptcy due to a lack of the property* is not covered by the Bankruptcy and Restructuring Act; however, the term *suspension of bankruptcy proceedings due to the member's lack of property* corresponds to this term.[325]

7.4.4.7 Death of a member

Pursuant to Section 232(1) of the Commercial Code, the membership of a natural person is terminated upon their death, and the heir to the membership rights and obligations of the deceased person may request membership from the cooperative. The law or the articles of association may determine when the board of directors must not refuse membership to the heir or when the consent of the board of directors to the acquisition of membership rights and obligations by the heir is not required. If membership is transferred to the heir, the heir acquires the membership rights and obligations of membership at the date of the deceased's death (*ex tunc*).[326] The consent of the board of directors is not required under Section 232(2) of the Commercial Code if the heir has acquired the rights and obligations attached to membership in a housing cooperative. In this case, the heir acquires the membership rights and obligations of membership in the cooperative on the date of the deceased's death *ex lege*.[327] According to Section 232(3) of the Commercial Code, an heir who does not become a member of the cooperative is entitled to the settlement share of the member whose membership has been terminated.

7.4.4.8 Dissolution of a member who is a legal entity

Pursuant to Section 232(4) of the Commercial Code, the membership of a legal entity in a cooperative is terminated by its entry into liquidation or declaration of bankruptcy, or its dissolution, if applicable. If the legal entity has a legal successor, the successor enters into all of its existing membership rights and obligations. Contrary to the transfer of membership upon

[324] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1028 *et seq.;* PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1640.
[325] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1026; NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. Zväzok*, p. 996.
[326] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1033.
[327] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p.. 1032.

the death of a natural person, a cooperative cannot in any way affect the acquisition of membership by a legal entity when it is transferred from the legal entity being dissolved to the successor legal entity.[328]

In the event of the dissolution of a legal entity with liquidation or upon the declaration of bankruptcy of its property, the membership of the legal entity in the cooperative terminates before its dissolution. The legal regulation in question makes it possible, within the framework of liquidation or bankruptcy, to dispose of the assets of a legal entity in liquidation or bankruptcy.[329] If a bankruptcy order for the property of a member whose participation in the cooperative was terminated has been revoked by a final court decision due to reasons other than following the fulfilment of the resolution or due to a lack of assets, the participation of the member in the cooperative shall be renewed. If the cooperative has already paid the settlement share, it is entitled to its reimbursement. This shall also apply, as appropriate, if execution under the Execution Act was terminated by a final decision of the court.[330]

7.4.4.9 Termination of membership by dissolution of the cooperative

By its nature, membership in a cooperative ceases to exist upon the deletion of the cooperative from the Commercial Register, since membership in a cooperative is linked to its very existence.

7.4.5 Property rights resulting from membership in a cooperative

7.4.5.1 Right to the share in profits

Unless otherwise stipulated in the articles of association, pursuant to Section 236(2) of the Commercial Code, the member's share in profits designated for distribution among members is determined by the proportion of their paid contribution to the paid contributions of all members. For members whose membership has lasted only a part of the year in the relevant year, this share shall be curtailed proportionally. The cooperative's articles of association or, if the Articles of Association permit, a decision of a members' meeting may determine a different manner of defining the member's share in profits that is to be distributed among members.[331] Pursuant to Section 236(1) of the Commercial Code, the members' meeting decides on determining the profits to be divided among members during the discussion on the individual financial statements. Decisions on the use of profits fall within the exclusive competence of the members' meeting. The articles of association may not entrust this authorization to another body of the cooperative.[332] Members of the cooperative are not entitled to a share in profits directly

328 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1033 a seq.
329 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1033.
330 Section 232 Subsection 5, the Commercial Code.
331 Section 236 Subsection 3, the Commercial Code.
332 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1038.

by law, but only after the adoption of the relevant decision of the members' meeting.[333] The entitlement to a share in profit arises only for the period in which the membership is valid.[334]

According to Section 235(2) of the Commercial Code, the indivisible fund may not be used for distribution among members during the existence of the cooperative.[335] The indivisible fund may only be used to the extent to which it is compulsorily created by law for economic purposes determined by the cooperative's articles of association in order to surmount any unfavourable course of events in the cooperative's financial management or to cover the cooperative's losses, unless a special Act stipulates otherwise. The cooperative's board of directors shall decide on the use of the indivisible fund.

7.4.5.2 Right to the settlement share

According to Section 233(1) of the Commercial Code, upon the termination of membership during the cooperative's existence, an existing member is entitled to a settlement share. The settlement share is determined by the proportion of the paid membership contribution of the existing member multiplied by the number of completed years of their membership to the total paid membership contributions of all members multiplied by the number of completed years of their membership.[336] Pursuant to Section 233(3) of the Commercial Code, the cooperative's net worth balance according to the individual annual financial statements for the accounting period preceding the accounting period in which the membership was terminated is decisive in determining the settlement share. If stipulated in the articles of association, when determining the amount of the settlement share, assets that are in the indivisible fund and in other security funds shall not be taken into account. Likewise, the investment contributions of members whose membership has lasted less than one year before the date as of which the annual financial statements are drawn up shall not be taken into account. According to Section 233(4) of the Commercial Code, the right to the payment of a settlement share shall be due upon the lapse of three months after the approval of the individual annual financial statements for the accounting period preceding the accounting period in which the shareholder's/member's participation in the company terminated, or if no such annual financial statements were approved, upon the lapse of three months after the date on which such annual financial statements should have been approved.

While the actual duration of membership in the year for which the share in profits is paid is decisive for the entitlement to the share in profit, the number of completed (not calendar) years of membership is decisive for calculating the settlement share under statutory provisions.[337]

[333] PATAKYOVÁ, M. In: OVEČKOVÁ, O. et al. *Obchodný zákonník. Veľký komentár. Zväzok I*, p. 1649.
[334] Section 233 Subsection 4 in fine, the Commercial Code.
[335] Pursuant to Section 235(1) of the Commercial Code, during its foundation, the cooperative is obliged to establish an indivisible fund at least in the amount of 10% of the entered registered capital. The cooperative supplements this fund by at least 10% of its annual net profits until the amount of the indivisible fund attains an amount equal to half of the registered legal capital of the cooperative. The articles of association may determine that a higher indivisible fund or additional security funds shall be created.
[336] Section 233 Subsection 2, the Commercial Code.
[337] JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1035.

The legislation on the calculation of the settlement share is of a default nature as, according to Section 233(5) of the Commercial Code, and the provisions of Section 233 (2 through 4) shall apply only if the articles of association do not determine otherwise. However, the articles of association may not preclude the payment of a settlement share or infringe on the principle of equal treatment when regulating the conditions for its payment.[338] The period for the payment of the settlement share laid down in the articles of association by way of derogation from Section 233(4) of the Commercial Code must be adequate.[339]

Pursuant Section 234(1) of the Commercial Code, the settlement share shall be paid in money, unless the law or articles of association determine another manner of settlement. The articles of association may determine that in cases where the membership contribution consisted entirely or in part of the transfer to the cooperative of an ownership right to real estate, the member may request settlement by having such real estate returned to them in the value registered in the cooperative's property at the time when their membership was terminated. At the same time, this legal possibility can be regarded as an exception to the principle of prohibition on the return of a contribution.[340] If the amount of the settlement share is lower than the value of the returned real estate, the acquiring member is obliged to pay the cooperative the difference in money. The articles of association may determine that a similar procedure shall also be followed in cases where the membership contribution consisted of the provision of a different material performance. The cooperative is liable to the member if it disposes of the cooperative's property in a manner that would make such return impossible. The entitlement to the return of agricultural land contributed to the cooperative shall belong to a member even if not stipulated in the articles of association.[341]

7.4.5.3 Right to transfer membership rights and obligations

The right to transfer membership rights and obligations is a special property right. For more details on this right, see chapter 7.5. Transfer of membership rights and duties.

7.4.5.4 Right to the liquidation balance

Unless the law stipulates otherwise, a wound-up cooperative shall, in accordance with Section 259(1) of the Commercial Code, enter into liquidation, and the liquidators are appointed in the manner stated in the articles of association, or by the members' meeting.

Pursuant to Section 259(2) of the Commercial Code, before distributing the liquidation balance, liquidators are obliged to draw up a proposal for its distribution which shall be discussed by the

338 Ibid.
339 In the opinion of the Supreme Court of the Czech Republic, a ten-year period as well as a seven-year period of payment of settlement share is contrary to good morals. See here decisions of the Supreme Court of the Czech Republic, case 29 Cdo 1633/99 and case 29 Odo 433/2004.
340 NÉMETHOVÁ, M. In: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 981.
341 Section 234 Subsection 2, the Commercial Code.

members' meeting. The proposal for distribution must be submitted to each cooperative member upon request.

Pursuant to Section 259(3) of the Commercial Code, the liquidation balance shall be distributed among the members in the manner determined in the articles of association. Unless the articles of association determine otherwise, the members shall be paid the paid part of their membership contribution. The remainder of the liquidation balance shall be distributed among members whose membership as of the date of the winding-up of the cooperative has lasted at least one year. Unless the articles of association stipulate otherwise, the remainder of the liquidation balance shall be distributed among these members according to the extent to which they participated in the registered capital of the cooperative. The provision of Section 234(1) of the Commercial Code shall apply accordingly to the return of non-monetary contributions. Within three months from the date on which the relevant members' meeting was held, each cooperative member or other authorised persons may propose that the court declare the decision of the members' meeting on the distribution of the liquidation balance invalid due to its inconsistency with the legal regulations or articles of association. If the court grants the petition, it shall simultaneously decide on the distribution of the liquidation balance. The liquidation balance may not be distributed until the lapse of a period of three months or until the issuance of a final decision of the court.[342]

7.4.6 Liability of cooperative members and payment obligations

According to Section 222(1, second sentence) of the Commercial Code, a cooperative is liable for the breach of its obligations with its entire property. Pursuant to Section 222(2) of the Commercial Code, the members are not liable for the cooperative's obligations. The articles of association may determine that based on a decision of the members' meeting, all or some of the cooperative members have payment obligations towards the cooperative up to a certain amount that exceeds the membership contribution to cover the cooperative's losses. The payment obligations may also be stipulated in the articles of association at a time when the cooperative does not show any losses, provided these funds are earmarked in a special reserve fund.[343]

Chapter 7.5 Transfer of membership rights and duties

To pick up on the part of this textbook dedicated to the commencement and termination of membership in a cooperative, in this chapter we will try to specify the fundamental provisions of the issue of transferring membership rights and duties that are an inseparable part of the cooperative membership.

From the comparative point of view, it is important to mention that, unlike the case of a business entity, the transfer of shares in a cooperative does not require the formal procedure required in the case of the transfer of a business share in any kind of business entity. Specifically, a change

342 Section 259 Subsection 4, the Commercial Code.
343 JABLONKA, B. In: PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1009.

in the ownership of membership rights and duties does not need to be reflected in terms of a petition for a change in the Commercial Register, which represents some sort of flexibility for cooperation membership. Subject to change is the membership share, which is defined as follows in Section 223(2) of the Commercial Code as subsequently amended: *"A membership share represents the member's share of the cooperative. Its level is determined by the ratio of the member's contribution to the basic capital of the cooperative, unless the articles of association provide otherwise. A member of a cooperative can only have one-member share. The membership contribution can differ among members, but it must always be expressed as positive integral number, unless the law provides otherwise. The total sum of members' monetary contributions to a cooperative must equal the monetary value of the basic capital of the cooperative."* The above stated argument that the subject of change in a share is determined by the membership share of the cooperative, applies according to our opinion, despite the fact that the Commercial Code and its provisions which regulate the terms of transfer of membership, does not recognize such term. Specifically, the provisions of Sections 229 and 230 of the Commercial Code, work in this context with the term membership rights and duties (Sections 229 of the Commercial Code) or more precisely, the rights and duties associated with membership (230 of the Commercial Code). This situation is explained as follows: *"This term (member share – author annotation) was not known in the original version of the Commercial Code. It was adopted by Amendment No. 19/2007 of the codex."*[3441] This amendment to the Commercial Code was not reflected in other norms regulating its assignability which resulted in valid enactment, which in the context of changes in the members of the cooperative, i.e. the transfer of member share in a cooperative does not use the term member share, but only deals with the transfer of membership rights and duties. The statement above does not change the fact that in the case of norms stipulating the conditions of such a transfer, it is understood as a transfer of a membership share and nothing else.

In light of the previously mentioned facts, we agree with the opinion that *"From the nature of the matter, when transferring membership rights and duties, it is not possible to transfer only some of these rights and duties, since it would deny the fundamental elements of membership in a cooperative, i.e. the acquirer would not be a member of the cooperative with the range of rights and duties arising from membership."*[345]
The specific requirements for membership transfers are stated in Sections 229-230 of the Commercial Code. In this respect, aspects of stipulating the statutory requirements of such a transfer leads to the formation of three main categories:

1. The transfer of membership rights and duties to another member of the cooperative;
2. The transfer of membership rights and duties to a third party (non-member of the cooperative); or
3. The transfer of rights and duties associated with membership in a housing cooperative.

[344] MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 991.
[345] PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1022.

7.5.1 Transfer of membership rights and duties to another member of the cooperative

The conditions for the transfer of membership rights and duties to another member of the cooperative are regulated by Section 229(1) of the Commercial Code, which states that such transfer is not subject to the approval of a cooperative body (e.g. board of directors), unless this competency is specifically stipulated in the articles of association of the cooperative, or if the internal regulations of the cooperative do not prohibit the possibility of the transfer of membership rights and duties (instrument of free transfer of membership rights and duties). The transfer of membership rights and duties (not only in the case of a transfer to another member of the cooperative) is executed through an innominate contract according Section 269(2) of the Commercial Code while the mode of this contractual relationship falls under Section 261(6) of the Commercial Code, under *absolute trades* and therefore its mode would always be regulated by commercial law. If the parties cannot sufficiently identify the subject of their obligation (Section 269(2) of the Commercial Code), the contract shall be deemed void. Although, the Commercial Code does not specify the content of the contract, in our opinion, it should at least define the rights and duties associated with membership, the value of the membership share, and whether it is a payment or non-payment transfer.[346] The Commercial Code does not stipulate the date of effectiveness of the transfer of membership rights and duties to another member of the cooperative or specifically define the obligation to deliver this contract to the cooperative. Taking into consideration the fact that this is a *free transfer*, where, aside from certain instances, it is not necessary to fulfil special conditions or obtain the approval of the body of the cooperative, in order to establish the defining moment of effectivity of the transfer towards the cooperative, the analogy legis from the relevant article of the Commercial Code must be followed. This amends the closest situation possible, which is the transfer of rights and duties associated with membership in a housing cooperative according Section 230 of the Commercial Code. By course of this law, the transfer becomes effective in relationship to the cooperative upon the date of presentation of the contract on the transfer of membership to the cooperative. This conclusion is also supported by opinions in specialized literature.[347]

7.5.2 Transfer of membership rights and duties to a third party or a non-member of the cooperative

As in the abovementioned case, the transfer of membership rights to a non-member of the cooperative is regulated by Section 229 of the Commercial Code, but legislation pays more attention to it from the point of stipulating specific provisions, than the *free transfer*. It means that such a transfer is subject to approval by the board of directors (hereinafter, the board), unless excluded by the articles of association. The articles of association may describe instances, in which the board cannot reject the transfer of the rights and duties of a member, or instances in which approval of the transfer by the board is not required. This results in legislation which by default is stricter than legislation ruling the transfer of membership rights

[346] See also: Decision of the Supreme Court of the Czech Republic, case 29 Cdo 1402/99.
[347] See: MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 991 and similarly PATAKYOVÁ, M. et al. *Obchodný zákonník. Komentár*. 5th edition, p. 1024.

and duties of the cooperative, while also enabling the cooperative to flexibly adjust these rules as needed.

This type of transfer of membership rights and duties becomes effective at first by the date of approval of the contract of transfer membership rights and duties by the board or the members' meeting. In the event that the transfer of membership rights does not require fulfilment of this condition (e.g. approval of the board), it is advisable to consider the effectiveness of the contract as in the case of a *free transfer* and therefore, present the contract to the cooperative in order to activate its effects towards it. The Commercial Code allows the relevant member to appeal to the members' meeting if the transfer is rejected by the board (if subject to approval by the board). The members' meeting has the competence to make the final decision on the matter.

7.5.3 Transfer of membership rights and duties associated with membership in a housing cooperative

From our point of view, the transfer of membership rights and duties associated with membership in a housing cooperative is the most frequent and from the financial point of view the most valuable transfer of membership rights in a cooperative. As a result, the legislation for this type of transfer is based on the principle of its non-restricted ability, and therefore restricts the housing cooperative from basing the effectiveness of the contract upon the approval of the board, or members' meeting. In this sense, it is up to a member of the cooperative to decide with whom and under which conditions the contract will be concluded. To become effective, the contact must be presented to the cooperative, or a written notice by the current member of cooperative about the transfer of membership together with the written approval of the acquirer of the rights and duties associated with the membership (membership share in housing cooperative) must be presented.

Chapter 7.6 Responsible management of the cooperative

The management of a cooperative is determined by the enforcement of the law regarding particular rights and duties by the cooperative body, which determines whether it will be accountable or not. The responsible managing of the cooperative is brought about by implementing requirements for particular assignments in the cooperative as provided by law and by pursuing the fulfilment of the purpose for which the cooperative was established.[348] In this sense, it is essential to appoint competent personnel to fill critical positions regarding the management of the cooperative. This is strictly in the competence of the members of the cooperative and can be carried out at the members' meeting. The differences between appointing persons to these offices in a cooperative as opposed to business entities are as follows: only members of a cooperative and representatives of legal entities that are members of a cooperative who are 18 years of age or older may be appointed; and the term of office of

[348] See also: LUKÁČKA, P. *Category of accountability and responsible business in the legal system of the Slovak Republic in the context of the execution of the appointment of a statutory body of a limited liability company*, p. 33 – 45.

members of cooperative bodies may not exceed five years. The articles of association of the cooperative permit the appointment of a substitute member. The substitute member shall take over the office from the withdrawing member according to the prescribed order.

Pursuant to Section 237 of the Commercial Code, the statutory bodies[349] of a cooperative include the following:

1. the members' meeting;
2. the board; and
3. the audit committee.

A cooperative may also create other cooperative bodies contemplated in the articles of association or in resolutions of members' meetings according to its needs. However, their establishment and scope may not interfere with the authority of the members' meeting, the board or the audit committee.[350] It is vital to distinguish this from the situation in which there is a director of the cooperative pursuant to Section 243(7) of the Commercial Code, which states that the articles of association may stipulate that the day-to-day business shall be organized and managed by a director to be appointed and removed by the board. Such a situation, which is not rare among cooperatives, is not considered as another body of the cooperative. It is a person, whose relationship to the cooperative is based on a contract of employment and it is not the same person as the chair of the board of directors of the cooperative. A director who has been entrusted to perform on behalf of a cooperative can be subsumed according to Section15 of the Commercial Code (person entrusted to perform certain tasks).

7.6.1 Members' meeting

The members' meeting is the supreme body of the cooperative, and, like the general meeting of a limited liability company or corporation, it makes decisions concerning the most important matters. Besides the powers of the members' meeting stipulated in Section 239(4) of the Commercial Code, the members' meeting (like the general meeting in a limited liability company Section 125(3) of the Commercial Code) may also take decisions on other matters concerning the cooperative and its business if so stipulated by the Act, the articles of association or if the members' meeting has reserved the right to decide on certain matters. Since the powers of the members' meeting to decide on particular matters are not limited, it can interfere in the powers of others, including the statutory bodies of the cooperative (e.g. the board). On the other hand, the members' meeting should use this competency with due care and in line with the context of the possible discharge of the board, that was performed by the members' meeting according to Section 243a(2) of the Commercial Code.

The frequency of members' meetings is stipulated in the articles of association, but a members' meeting must be held at least once a year, or if requested in writing by no less than one third of

[349] There can be an exception regarding the obligation to create bodies of the cooperative that are given by Section 237 of the Commercial Code. Such an exception is the case of a *small sized cooperative* (less than 50 members) where the powers of the board and audit committee may be vested in the members' meeting

[350] See also: SUCHOŽA, J., HUSÁR, J. et al. *The Commercial Code*, p. 634.

all of the members of the cooperative or by the audit committee, as well as in other cases referred to in the articles of association. The legislation regarding the arranging of members' meetings generally defers to the articles of association of the cooperative; however, the meeting must be called by the board. The law does not specify the time frame within which the invitation for the meeting should be delivered to the members of the cooperative or the timeframe for holding the members' meeting if one third of the members or audit committee request it. We assume that this matter shall be regulated in line with *de lege ferenda.*

The members' meeting can be arranged as follows:

a) a members' meeting (at one place and one time); or
b) a partial members' meeting – when passing a resolution, the votes cast at such partial members' meeting shall be summed up. A partial members' meeting may not take decisions concerning the winding-up of the cooperative, the change of its corporate form, or other matters referred to in the articles of association.

The Commercial Code also enables provisions for the specific relationship to the administration of the powers of the members' meeting. If it is impossible to convene the members' meeting due to the size of the cooperative, the articles of association may stipulate that to the extent determined therein, an assembly of delegates shall replace the members' meeting. Each delegate shall be elected by an equal number of votes. The articles of association may depart from the rule above if this is necessary in view of the organization of the cooperative.

Taking into account the high attendance of members of a cooperative, the given options to provide the functionality of the decision making process seem to be adequate, since a *substitute members' meeting* serves the same purpose. The substitute members' meeting must be held within 3 weeks, from the date on which the originally convened meeting, which did not achieve a quorum according to Section 238(3) of the Commercial Code, should have taken place. The substitute members' meeting makes decisions based on the majority vote of the members in attendance. This also applies to a partial members' meeting and an assembly of delegates.

7.6.2 The board

The board is the statutory body[351] of the cooperative. It manages the activities of the cooperative and takes decisions concerning any matters which are not reserved to the authority of another body by the Act, or the articles of association. The board implements the resolutions of the members' meetings and is responsible for its actions to the latter. Unless the articles of association stipulate otherwise, the board shall be represented by its chairman or vice-chairman. However, if an action taken by the board requires a written form, the signatures of at least two members of the board shall be necessary. The board shall elect the chairman from among its members, and the vice-chairman as appropriate, unless the articles of association stipulate their election by the members' meeting. Like the statutory body of a limited liability company and

[351] A statutory body is defined in Section 20(1) of the Civil Code.

corporation (Section 135a of the Commercial Code, Section 194(5 to 9) of the Commercial Code), the board members of a cooperative shall perform their duties with due care and in line with the interests of the cooperative and all of its members. In particular, they shall collect and in their decision making take into account any available information concerning such a decision; and they shall maintain confidentiality regarding any information and facts whose disclosure to third parties could cause damage to the cooperative or prejudice its interests or the interests of its members. When discharging their duties, they shall not place their own interests or the interests of certain members or third parties before the interests of the cooperative. Performing duties with professional care is the basic requirement for members of the board of a cooperative, when taking into consideration the acts performed by the members. Board members who are in breach of their duties (except for exonerating reasons), including the duty of loyalty, are liable for damage caused by such breach. For the avoidance of doubt, professional care is not a specific duty leading to a particular result, but it should be an attribute of all acts performed by the board member.[3529] When it comes to responsibility for damage caused by a breach of duties, while acting as a board member, the following applies: "…*responsibility for damage will be regulated by the Act on Compensation for Damage and Section 373 and the following of the Commercial Code, which is modified by a special adaptation resulting from annotated assessments (Section 243a of the Commercial Code – author's note)."*[353] As can be seen, appointing responsibility towards a member of the Board is based on the fulfilment of fundamental provisions regarding responsibility for damage (breach of duties, damage caused and the connection between the breach and damage). In addition, the existence of exonerating reasons will be investigated.

In particular, this applies to a case where a board member caused damage to the cooperative, but has discharged their duties with due care (it is up to the member to submit evidence) or if the damage has been caused to the cooperative due to the implementation of a resolution of the members' meeting, if such a resolution is not contrary to the law, the articles of association or if it their conduct has been due to the obligation to file a motion for bankruptcy.

7.6.3 The audit committee

The supervisory body of the cooperative (similar to the supervisory board in a limited liability company and corporation) is the audit committee, which shall have the power to monitor the activities of the cooperative, and deal with complaints lodged by cooperative members. The audit committee is liable only to the members' meeting and is independent of the other cooperative bodies. It shall have no less than three members and shall meet as necessary, however at least once every three months. The audit committee shall elect its chairman and vice-chairman from among its members, unless the articles of association provide that they shall be elected by the members' meeting. The audit committee is not authorized to represent a cooperative or to conduct managerial duties.

[352] See also: LUKÁČKA, P. *The category of accountability and responsible business in the legal system of the Slovak Republic in the context of the execution of appointments to a statutory body of a limited liability company*, p. 62 – 64

[353] MAMOJKA, M. et al. *Obchodný zákonník. Veľký komentár. 1. zväzok*, p. 1011-1012

The audit committee shall give its opinions concerning the ordinary and extraordinary individual financial statements and the proposal for the distribution of the profits or the coverage of losses. The audit committee shall be entitled to demand from the board any information concerning the financial management of the cooperative. The board shall be obliged to disclose to the audit committee without undue delay any facts which may have a material impact on the finances or the status of the cooperative and its members.

When it comes to responsibility for damage caused by a breach while discharging duties as an audit committee member, the abovementioned rules regarding breach of duties applicable to Board members also apply to members of the audit committee. The main criteria for the activity of members of the audit committee is to discharge their duties with due care and in line with the interests of the cooperative and all of its members.

Revision questions:

1. *List the basic characteristics of a cooperative that distinguish it from companies.*
2. *Define the terms 'cooperative self-government' and 'cooperative democracy'.*
3. *How is the legal capital in a cooperative created?*
4. *Comment on the liability issues of cooperative members for cooperative obligations.*
5. *What property rights does a cooperative member have?*
6. *Define the membership transfer requirements in a cooperative.*
7. *Define the competences of the statutory bodies of a cooperative.*
8. *List the basic prerequisites for the liability of the board of directors and the audit committee.*
9. *Under what conditions can a member of the board of directors or audit committee be exonerated?*

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