

CAPITAL DOCTRINE IN THE EUROPEAN UNION – A LESSON TO LEARN FROM FINLAND?

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Abstract: *The aim of this article is to analyse the legal capital doctrine in the European Union with a comparative method of analysis. Slovak legal system represented by the Slovak Commercial Code served us as the traditional model of the capital doctrine in the European Union. On the other hand, Finland and its Finnish Limited Liability Companies Act served us a model jurisdiction for enlightened model of the capital doctrine in the European Union. The analysis was conducted on the public limited liability companies, as the scope of the Capital Directive covers only this type of company. The main aim of the article was to analyse the specificities of the Finnish capital system which introduced the capital system with shares without nominal value through the company law reform in 2006. Moreover, the article deals with inconsistencies in the Slovak legal system caused by the inexact transposition of the Capital Directive into the Slovak Commercial Code.*

Keywords: *Capital doctrine, Capital system, Price of the shares, Equity, Restricted equity, Unrestricted equity, Reserves, Capital*

1. INTRODUCTION

The aim of this article is to analyse the concept of legal capital doctrine in the European Union. The analysis was conducted on the Slovak legal system representing the traditional capital system and the Finnish legal system, which underwent a major reform in 2006, served us as a model jurisdiction of the capital system with shares without nominal value. The legal capital doctrine was analysed on the public limited liability companies as the scope of the Capital Directive¹ only covers this type of company. Moreover, in the process of the analyses of the Slovak capital system we came across major inconsistencies with the Capital Directive which were caused by the wrong transposition of this directive into the Slovak Commercial Code². Thus, we pointed out the main inconsistencies within the Slovak legal system in this article to open a discussion among scholars and legislators.

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¹ Directive 2012/30/EU of the European Parliament and of the Council of 25 October 2012 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 54 of the Treaty on the Functioning of the European Union, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent. (hereinafter referred to as “**Capital Directive**”).

² Act no. 513/1991 Coll. Commercial Code as amended (Zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov) (hereinafter referred to as “**SCC**”).

2. CAPITAL DOCTRINE IN THE EUROPEAN UNION

Legal capital³ is a concept covering issues of raising capital, maintenance of the capital and legal return of the value to the shareholders.⁴ Legal capital can be seen as a bonding knot between shareholders and creditors – on one side the legal capital represents (i) shareholders' participation rights (voting rights), (ii) their right to dividends and (iii) their right to participate on the liquidation process as a residual claimant, on the other hand the legal capital represents, for creditors, a guarantee.⁵

Rules regulating capital of companies emerged in the Europe in the second half of the 19th century.⁶ However, legal capital rules were not homogenous in the Europe – for example in the Netherlands formation and maintenance of the legal capital was obligatory just at the time of incorporation and in the UK the no minimal legal capital rules were applicable and the legal capital was regulated through disclosure of information.⁷

Harmonization of the legal capital doctrine on the European level was conducted by Directive 77/91/EEC⁸. This directive introduces regulation on legal capital to the public limited liability companies.⁹ Directive 77/91/EEC was adopted by Council in 1976 and it was part of the first intense phase of the harmonisation process of company law.¹⁰ This directive was aimed at regulation of foundation of public limited liability companies and maintenance and alteration of their minimum capital.¹¹ This directive was repealed by the Directive 2012/30/EU. Moreover, Directive 2006/68/EC¹² needs to be taken into account when analysing the issue of legal capital in the European Union as it provided major amendments to the Directive 77/91/EEC based on the SLIM actions^{13, 14}

³ "Capital is a word of many meanings, but in company law it is used in a very restrictive sense. It connotes the value of the assets contributed to the company by those who subscribe for its shares. By and large, the value of what the company receives from investors in exchange for its shares constitutes its capital." DAVIES, P. L. *Principles of Modern Company Law*. London: Sweet & Maxwell, 2012, p. 272.

⁴ FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 72.

⁵ SANTELLA, P., TURRINI, R. Capital Maintenance in the EU: Is the Second Company Law Directive Really That Restrictive? *European Business Organisation Law Review*. 2008, No. 9, p. 429.

⁶ PAYNE, J., SMITH, T. Legal Capital and Creditor Protection in UK Private Companies. *European Company Law*. 2008, No. 5, p. 220 and ARMOUR, J. Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law. *The Modern Law Review*. 2000, No. 63, p. 361.

⁷ DORRESTEIJN, A., MONTEIRO, T., TEICHMANN, CH., WERLAUFFE, E. *European Corporate Law*. Alphen an den Rijn: Kluwer Law International, 2009, p. 54.

⁸ Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent.

⁹ Moreover, many of the European Union Member States imposed even stricter regulations of the legal capital in their legal systems. ENRIQUES, L., MACEY, J. R. Creditors versus Capital Formation: The Case against the European Legal Capital Rules. *Cornell Law Review*. 2000–2001, No. 86, p. 1174.

¹⁰ MÄHÖNEN, J. Capital maintenance and distribution rules in modern European company law. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 120.

¹¹ HODÁL, P., ALEXANDER, J. *Jevropské právo obchodních společností*. Praha: Linde, 2005, pp. 30–31 and WOUTERS, J. European Company Law: Quo Vadis? *Common Market Law Review*. 2000, No. 37, p. 259.

¹² Directive 2006/68/EC of the European Parliament and of the Council of 6 September 2006 amending Council Directive 77/91/EEC as regards the formation of public limited liability companies and the maintenance and alteration of their capital.

¹³ Actions recommended by SLIM Working Group – Working Group on the Simplification of the First and Second Company Law Directives, Conclusions Submitted by the Company Law SLIM Working Group.

Capital Directive regulates mainly these issues: (i) obligation to disclose information about the capital so the external person can observe the capital composition of the particular company, (ii) creation of the minimal legal capital, (iii) maintenance of the legal capital, (iv) equal treatment of shareholders (who are in the same position) and (v) procedures regulating the creditor protection if the legal capital is altered.¹⁵

Capital doctrine in Europe is seen as a set of default rules, which shall provide creditors with de minimis protection against opportunistic behaviour of shareholders.¹⁶ Legal capital rules serve as a regulatory strategy in order to eliminate the costs arising from the agency problem between creditors and shareholders¹⁷.

Regulation of the creditor protection is needed based on the arguments that the markets are not perfect¹⁸. Thus, protection of voluntary creditors through covenants is not always ideal. The same is true for the protection of interests of involuntary creditors¹⁹ who

¹⁴ Report from the Commission to the Council and the European Parliament on the Results of the Second Phase of SLIM and the Follow-up of the Implementation of the First Phase Recommendations, Brussels COM (97) 618 and Actions recommended by SLIM Working Group – Working Group on the Simplification of the First and Second Company Law Directives, Conclusions Submitted by the Company Law SLIM Working Group.

¹⁵ DORRESTEIJN, A., MONTEIRO, T., TEICHMANN, CH., WERLAUFF, E. *European Corporate Law*. Alphen aan den Rijn: Kluwer Law International, 2009, p. 54 and WERLAUFF, E. *EU-Company Law (Common business law of 28 states)*. Copenhagen: DJØF Publishing, 2003, p. 77.

¹⁶ Preamble of the Capital Directive and SANTELLA, P., TURRINI, R. Capital Maintenance in the EU: Is the Second Company Law Directive Really That Restrictive? *European Business Organisation Law Review*. 2008, No. 9, p. 435.

¹⁷ Presence of the agency problem between shareholders and creditors has negative impact on the whole efficiency of company to function because agency costs can be detected. Agency costs can be described as costs of the creditors to monitor the shareholders in order to eliminate the opportunistic behaviour of shareholders, which may result in decreasing of the entire surplus that was created in the company. Such behavioural feature of shareholders may lead to an outcome of overall destruction of the value of the company with increased probability for bankruptcy. The actions threatening the creditor and the company's assets in a long run are not just against the main interests of creditors, the same is true for the goals of the shareholders. Thus, elimination of their opportunistic behaviour is crucial. Reduction of the costs resulting from the agency problems is essential for aggregation of the social welfare. Legal strategies as basic set of rules are the core tool for the elimination of the undesired costs arising from the opportunistic behaviour of the agent. Different types of legal strategies – regulatory as well as governance strategies – are suitable to mitigate the agency problems in the company. Each type of the strategy can be suitable for each type of agency problem and, at the same time they, they can overlap and their simultaneous application can mitigate the tension between agent and principal the best. FERRAN, E. *Company Law and Corporate Finance*. Oxford: Oxford University Press, 1999, p. 118; SCHMIDT, K. M. The Economics of Covenants as Means of Efficient Creditor Protection. *European Business Organisation Law Review*. 2006, No. 7, p. 91 and ARMOUR, J., HANSMANN, H., KRAAKMAN, H. Agency Problems and Legal Strategies. In: ARMOUR, J., HANSMANN, H., KRAAKMAN, H. (eds.). *The Anatomy of Corporate Law. A Comparative and Functional Approach*. Oxford: Oxford University Press, 2009, pp. 37–39.

¹⁸ If we take into consideration perfect market with perfect competition and perfect information there will be no need for a regulator to step in. However, in real world that is not correct and we do experience market failures, which are considered to be reasons for the intervention of the regulative tool of legislator. As it was stated by Armour and his quotation of the Strategic Framework document: “Markets and informal pressures combined with transparency cannot be expected to work; this may happen because the participants lack the market power, skill or resource to contract effectively.” PACCES, A. M., VISSCHER, L. Methodology of Law and Economics. *Series Politika*. 2011, No. 4, p. 1 and ARMOUR, J. Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law. *The Modern Law Review*. 2000, No. 63, p. 357.

¹⁹ Involuntary creditors are not a homogenous group. Kuhner describes the non-contractual relationships as “claims from compensation for damages and claims from fiscal and regulatory authorities.” Therefore, non-adjusting creditors are mainly tort victims, tax and environmental claimants. FLEISCHER, H. Legal Capital: A navigation System for Corporate Law Scholarship. *European Business Organization Law Review*. 2006, No. 7, p. 31 and DENOZZA, F. Different Policies for Corporate Creditor Protection. *European Business Organisation Law Review*. 2006, No. 7, p. 410; KUHNER, CH. The Future of Creditor Protection Through Capital Maintenance Rules in European Company Law. *European Company and Financial Law Review Special*. 2006, No. 1, p. 6 and ARMOUR, J. Legal Capital – an Outdated Concept? *European Business Organisation Law Review*. 2006, No. 7, p. 11.

do not possess the position to negotiate the entrance into the relationship with the company/shareholders. Therefore, regulatory strategies in creditor protection are considered to: (i) eliminate the contracting costs occurring during the contractual specification of the protection of voluntary creditors through covenants²⁰, (ii) mitigate the market failures occurring in the negotiation process of covenants that can happen due to the information asymmetries and different market power²¹ and (iii) provide protection to involuntary creditors who cannot negotiate with the company the covenants that would provide them protection.

3. CAPITAL SYSTEMS IN THE EUROPEAN UNION

It is possible to recognize two main capital systems in the Europe Union in the light of the Capital Directive: (i) capital system with shares with nominal value and (ii) capital system with shares without nominal value. Legal basis of this determination is Article 8 of the Capital Directive:

“Shares may not be issued at a price lower than their nominal value, or, where there is no nominal value, their accountable par...”

The above mentioned classification of the capital systems in the European Union is not that common as it is claimed that there is no “true” capital system without nominal values of shares applied in the Member States of the European Union.²² In the following analysis, we would like to elaborate this common misunderstanding more deeply, as the Finnish Limited Liability Companies Act²³ used the concept of accountable par in a rather unique way.

3.1 Traditional capital system with nominal value of shares

Traditional capital system can be described as following: *“as well as stating the total amount of the authorized share capital, the memorandum must also state the division of the share capital into shares of a fixed amount... the stated fixed amount of each share is known as the nominal or par value²⁴ of the share.”*²⁵ To sum up, traditional capital system

²⁰ ARMOUR, J. Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law. *The Modern Law Review*. 2000, No. 63, p. 361 and SANTELLA, P., TURRINI, R. Capital Maintenance in the EU: Is the Second Company Law Directive Really That Restrictive? *European Business Organisation Law Review*. 2008, No. 9, p. 435.

²¹ SCHMIDT, K. M. The Economics of Covenants as Means of Efficient Creditor Protection. *European Business Organisational Law Review*. 2006, No. 7, pp. 91–92 and ARMOUR, J. Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law. *The Modern Law Review*. 2000, No. 63, pp. 358–362.

²² FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 74.

²³ Finnish Limited Liabilities Companies Act as amended (hereinafter referred to as “*FLICA*”).

²⁴ Difference between nominal value of shares and par value of shares is that the information about the nominal value of shares must be included on the declaration on the capital, which is filed with the register. On the other hand, par value shall be a monetary amount but this amount does not need to correspond to the amount that is likely to be paid in a legal tender. The par value concept rather refers to a fraction or percentage of a monetary amount. The par values is according to *Davies and Worthington* a doubtfully useful concept to be applied. In this article we refer to capital system with nominal value of shares as Slovakia applies this capital system, therefore we do not analyse the par value concept in a deeper way. FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 71 and DAVIES, P. L. *Principles of Modern Company Law*. London: Sweet & Maxwell, 2012, p. 274.

with shares with nominal value can be described as system in which legal capital is created with shares with nominal value and the nominal value of the shares must be determined in the articles of association/memorandum of association.²⁶ Moreover, every time new shares are issued the amount of the nominal value of shares must be credited to the share capital.²⁷

Slovak legal system purely recognizes just the traditional capital system with shares with nominal value. Affiliation to this system can be found in the Section 154 and 157 of the SCC that reads as following:

“A joint stock company is a company whose registered capital is distributed into a certain number of shares with a certain nominal value.” (Section 154 of the SCC)

“The articles of association must determine the nominal value of all types of shares which are able to be issued.” (Section 157 of the SCC)

On the other hand, the FLLCA from 2006 allows and encourages companies to follow the capital system without nominal value of shares. However, the FLLCA allows companies to form a traditional capital system with shares with nominal value and legal basis can be found in Chapter 3: Section 5: Subsection 2 of the FLLCA:

„It may be provided in the Articles of Association that the shares of the company have a nominal value. In this event, all shares in the company shall have the same nominal value.“

If company opts for capital system without nominal value of shares under the FLLCA the company will just not refer to the nominal value in its articles of association.²⁸

Both of the legal systems describe the *“traditional nominal value based structure.”*²⁹ Under this capital system shares cannot be issued for price that would be less than their nominal value.³⁰ The sum of the nominal values of the shares must correspond to the legal capital, which is registered into the commercial register.³¹

3.2 Capital system without nominal value of shares

In capital system without nominal value of shares each share is valued *“by reference to the shareholders’ proportionate shares of the total value of the enterprise, which will correspond to the value of its net assets and goodwill.”*³² Therefore, shares are not required to have nominal value and their value equal to the portion of the value of company’s assets.³³

²⁵ FERRAN, E. *Company Law and Corporate Finance*. Oxford: Oxford University Press, 1999, p. 282.

²⁶ FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 71.

²⁷ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 314.

²⁸ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 314.

²⁹ *Ibid.*, p. 313.

³⁰ Prohibition of issuing shares for less than their nominal value is stipulated in Article 8 of the Capital Directive which was implemented into the legal system of the Slovak Republic – Section 157 of the SCC and into the legal system of Finland – Chapter 3: Section 5: Subsection 3.

³¹ SCC, Section 157.

³² SANTELLA, P., TURRINI, R. Capital Maintenance in the EU: Is the Second Company Law Directive Really That Restrictive? *European Business Organisation Law Review*. 2008, No. 9, p. 444.

³³ *Ibid.*

Issuing shares without nominal value is allowed by the wording of Article 8 and Article 3 (c) of the Capital Directive. Shares issued under this capital system do not have nominal value, the Capital Directive describes this concept as “*accountable par*.”³⁴

As Ferran and Chan Ho stipulate that shares without nominal value under the Capital Directive cannot be considered a “*true*” as this term is generally understood outside the Europe – for example in New Zealand or in Australia.³⁵ On the other hand, Article 8 of the Capital Directive introduces a concept of shares with accountable par of shares.³⁶ Thus, it is possible to claim that the possibility to create capital systems with shares without nominal value in the European Union by the Capital Directive is a compromise and not a full adoption of capital system without nominal values of shares as it is known in the world. However, the Finnish legislation does not support this statement, as the accountable par under the FLLCA was used in a unique way as accountable par can be zero.

Introduction of the “*true*” capital system with shares without nominal value was highly recommended by the SLIM group report³⁷ and by the Giovannini Group which resulted in the report on the Impact of the Introduction of the Euro on Capital Markets.³⁸ Later on, this issue was reopened and more deeply analyzed by the High Level Group of Company Law Experts. High Level Group Report³⁹ stipulated that financial industry and legal profession expressed a wide demand for the implementation of non-nominal value capital system.⁴⁰ The group stated that the Capital Directive allows application of shares without nominal value but these shares have fractional value referred to as “*accountable par*” in the directive⁴¹, thus it is not possible to claim that true non-nominal value capital system is allowed in the European Union under the Capital Directive. This report opened a debate whether an introduction of a true non-nominal value capital system will require substantial changes of the Capital Directive. According to this report, answers are not consistent among scholars. One group of scholars claimed that the only inconsistency of this alternative regime with the Capital Directive is the prohibition to issue shares at discount to the nominal value, on the other hand, other claimed that the directive will require more changes in order to be compatible with the introduction of true non-nominal value capital system.⁴²

³⁴ Capital Directive, Article 8.

³⁵ FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 74.

³⁶ *Ibid.*, p. 73.

³⁷ SLIM Report – Report from the Commission to the Council and the European Parliament on the Results of the Second Phase of SLIM and the Follow-up of the Implementation of the First Phase Recommendations, Brussels COM (97) 618.

³⁸ Communication from the Commission, The Impact of the Introduction of the Euro on Capital Markets, Brussels II/338/97, pp. 21–22.

³⁹ Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, Brussels 2002.

⁴⁰ Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, Brussels 2002, p. 82.

⁴¹ Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, Brussels 2002, p. 82.

⁴² Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, Brussels 2002, p. 83.

Commission issued Action Plan 2003⁴³ shortly after compiling the report from the High Level Group of Company Law Experts. In this communication the Commission took into consideration suggestions presented in the High Level Group Report and as well as the SLIM Report. However, the Commission pointed out the necessity to punctually evaluate any steps in the possible introduction of the alternative regime with “true” non-nominal value capital system.⁴⁴ According to the Commission detailed characteristics of this alternative regime departing from the capital legal doctrine established by the Capital Directive should be created and the effectiveness of this alternative regime in relation to protection of shareholder, creditors and other constituencies should be measured.⁴⁵ Commission announced in this document to launch a study about the feasibility of an alternative to the capital maintenance regime, which should provide a deeper analysis of this issue.⁴⁶ The feasibility study for the Commission on the question of alternative capital systems was conducted by KPMG⁴⁷.

The Action Plan 2012⁴⁸ which was created by the Commission and focused on the issues of Company Law and Corporate Governance has no reference about the introduction of the true non-nominal value capital system into the European Company Law.

Finland introduced the non-nominal value capital system in compliance with the regulation of the Capital Directive in 2006. Shares issued by a company do not need to have nominal value. As it is stated by Article 8 of the Capital Directive in such a case the shares do need to have accountable par. Under the FLLCA this accountable par indicates the sum that should be credited to the share capital⁴⁹, which can even be zero if the share capital is already created.

4. PRICE OF SHARES AND NOTION OF EQUITY BASED ON THE CAPITAL SYSTEM

Concept of price of shares is different in the capital system with nominal value of shares and capital system without nominal value of shares. Therefore, it is crucial to describe the main differences.

⁴³ Communication from the Commission to the Council and the European Parliament, Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward, Brussels, COM (2003) 284.

⁴⁴ Communication from the Commission to the Council and the European Parliament, Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward, Brussels, COM (2003) 284, pp. 17–18.

⁴⁵ Communication from the Commission to the Council and the European Parliament, Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward, Brussels, COM (2003) 284, pp. 17–18.

⁴⁶ Communication from the Commission to the Council and the European Parliament, Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward, Brussels, COM (2003) 284, p. 18.

⁴⁷ Feasibility study on an alternative to the capital maintenance regime established by the Second Company Law Directive 77/91/EEC of 13 December 1976 and an examination of the impact on profit distribution of the new EU accounting regime – KPMG, January 2008.

⁴⁸ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions, Action Plan: European company law and corporate governance – a modern legal framework for more engaged shareholders and sustainable companies, Strasbourg COM (2012) 740.

⁴⁹ FLLCA, Chapter 3: Section 5: Subsection 1.

4.1 Price of shares in capital system with nominal value of shares

In the capital system with nominal value of shares it is possible to distinguish between the nominal value and their subscription price. The difference is caused by the difference between the sum of money stipulated on the share during their allotment and the money received by the company.⁵⁰

Nominal value of share

Under the capital system with nominal value of shares each share's value must be determined in the articles of association or memorandum of association. As it stems from de lege lata regulation the determination of the nominal value of shares is essential as sum of the nominal values of shares constitutes the amount of the share capital of the company that is filed in with the register.⁵¹ If shares all allotted without stipulation of their nominal value such allotment will be void.⁵²

Nominal value of the company is a decisive constituency in the process of determination of (i) right for the dividend, (ii) voting rights of the company and (iii) proportion on the residual rights.⁵³ Proportion between the nominal value of share and the total sum of all nominal values of shares can be disturbed by preferential shares.⁵⁴ Additionally, this proportion can be disturbed by the wording of articles of association regarding the voting rights and the proportion of the residual rights.⁵⁵ Nominal value must be determined under the Slovak legislation as a positive integral number.⁵⁶

Subscription price of share

Subscription price is price determined by the issuer of the security that the investor (future shareholder) undertakes to pay for the share in the process of subscription.⁵⁷ The subscription price of shares cannot be lower than the nominal value.⁵⁸ Traditionally, when company issues new shares part of the subscription price that stands for the nominal value of the share is credited to the share capital of the company. In case that there is price difference between the subscription price and the nominal value the amount that exceeds the nominal value is credited to the share premium account.⁵⁹ However, under the new FLLCA⁶⁰, no share premium account is created even in a scenario that a company would opt for traditional nominal

⁵⁰ DAVIES, P. L. *Principles of Modern Company Law*. London: Sweet & Maxwell, 2012, p. 274.

⁵¹ PATAKYOVÁ, M. Commentary on Section 157 of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck. 2013, p. 643.

⁵² FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 72.

⁵³ *Ibid.*

⁵⁴ *Ibid.*

⁵⁵ PATAKYOVÁ, M. Commentary on Section 157 of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck. 2013, p. 644.

⁵⁶ SCC, Section 157: Subsection 1.

⁵⁷ FERRAN, E. *Company Law and Corporate Finance*. Oxford: Oxford University Press, 1999, p. 304 and PATAKYOVÁ, M. Commentary on Section 157 of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck. 2013, p. 645.

⁵⁸ Capital Directive, Article 8 and SCC, Section 157.

⁵⁹ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 313.

value capital system – if subscription price is higher than nominal value the premium is credited either to the share capital or to the reserve for invested unrestricted equity.⁶¹ Therefore, companies will usually credit the share premium to the reserve for invested unrestricted equity that allows its distribution back to shareholders without consent of creditors.⁶²

The Capital Directive allows Member State to determine whether the share premium and the created share premium account will be considered as restricted or unrestricted equity.⁶³ Considering the share premium as unrestricted equity can help Member States to relax the legal capital rules and to leave companies a small reserve that is created by contributions of shareholders and is not falling under the strict rules distribution of restricted equity.⁶⁴

SCC does not directly stipulate whether the share premium account shall be considered as restricted or unrestricted equity. Academics claim that share premium account shall be treated in the same way as the legal capital of the company and the use of this account shall be limited to (i) creation of the reserve fund within the legally required limits during the process of incorporation, (ii) increase of the share capital and (iii) cover the losses occurred in business.⁶⁵ Therefore, the share premium should be considered as part of the contribution made by shareholders into the company and thus cannot be returned to shareholders based on the core company law rule on prohibition to return the contributions to shareholders.⁶⁶

4.2 Price of shares in capital system without nominal value of shares

Under the capital system without nominal value of shares it is possible to distinguish between accountable par and subscription price of the share.

Accountable par of share

The Capital Directive stipulates the concept of accountable par in Article 8. It is possible to claim, that under the Capital Directive, if the share does not have nominal value its accountable par should be stipulated in order to indicate the sum, which should be credited to the share capital. According to *Rickford* denomination of the share is calculated through a fraction of the aggregate of the legal capital.⁶⁷ Due to this interpretation, this capital system is sometimes described as no true capital system without nominal value of shares as

⁶⁰ The previous Finnish legislation considered the share premium as restricted equity and its maintenance followed the same rules as the share capital protection. MAHONEN, J. Capital maintenance and distribution rules in modern European company law. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 124.

⁶¹ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, pp. 314–315.

⁶² MAHONEN, J. Capital maintenance and distribution rules in modern European company law. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 125 and FLLC, Chapter 8: Section 1: Subsection 1.

⁶³ SANTELLA, P., TURRINI, R. Capital Maintenance in the EU: Is the Second Company Law Directive Really That Restrictive? *European Business Organisation Law Review*. 2008, No. 9, p. 437.

⁶⁴ *Ibid.*

⁶⁵ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition. 2012, p. 88.

⁶⁶ *Ibid.*, p. 87.

⁶⁷ RICKFORD, J. Reforming Capital, Report of the Interdisciplinary Group on Capital Maintenance. *European Business Law Review*. 2004, No. 4, p. 929.

accountable par is compared to have the same role as nominal value.⁶⁸ However, after analysing the Finnish legislation the outcome is different.

Non-nominal value capital system was introduced into Finnish legislation in 2006 by FLLCA. Under the FLLCA company can issue shares that do not have nominal value. Therefore, the traditional link between nominal value and the share capital is displaced.⁶⁹ The amount to be credited to the share capital is called accountable par.⁷⁰ Under the Finnish regulation it is permissible that the accountable par of share will be zero and the subscription price will be fully credited to the reserve for invested unrestricted equity or other reserves created by the company voluntarily.⁷¹ This may happen when the requested share capital of 80.000 EUR required under Chapter 1: Section 3: Subsection 1 the FLLCA is created so the company is not required to credit any part of the subscription price of the share to the share capital anymore. This example proves that the capital system without nominal value of shares is under the Finnish legislation the “true” one as the accountable par definitely cannot be considered a replacement for the nominal value.

Subscription price of share

Under the FLLCA the subscription price of share shall be credited to the share capital unless the memorandum of association/articles of association/share issue decision stipulate that a part of it will be credited to the reserve for invested unrestricted equity.⁷²

As the connection between nominal value and the share capital was removed under the FLLCA equity investments into the company by shareholders became more flexible. It is up to companies to decide what part of the subscription price of issued shares will be credited to the unrestricted equity of the company (after the minimum amount of the legal capital is created).⁷³ Consequently, share capital of the company does not need to be increased when new shares are issued.⁷⁴

5. EQUITY

Definition of the term “equity” is not homogenous and depends on the context. Equity of the company can be defined through the balance sheet as an amount of the funds which were contributed into the company by shareholders and retained earnings of the company (or losses).⁷⁵

⁶⁸ FERRAN, E., CHAN HO, L. *Principles of Corporate Finance*. Oxford: Oxford University Press, 2013, p. 74 and RICKFORD, J. Reforming Capital, Report of the Interdisciplinary Group on Capital Maintenance. *European Business Law Review*. 2004, No. 4, p. 929.

⁶⁹ VILLA, S. Creditor Protection and the Application of the Solvency Test and Balance Sheet Test under the Company Laws of Finland and New Zealand. *Nordic Journal of Commercial Law*. 2008, No. 1, p. 6.

⁷⁰ FLLCA, Chapter 3: Section 5: Subsection 1.

⁷¹ TOIVAINEN, H. *Introduction to Finnish business law*. Helsinki: Edita, 2008, p. 629.

⁷² FLLCA, Chapter 2: Section 4.

⁷³ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 317.

⁷⁴ *Ibid.*, p. 323.

⁷⁵ <http://www.investopedia.com/terms/e/equity.asp>.

5.1 Notions of restricted and unrestricted equity in general

Equity is usually divided into (i) restricted equity and (ii) unrestricted equity. Restricted equity being that part of the equity that shall be maintained and cannot be distributed back to shareholders at all or just under a specific procedure involving creditors. On the other hand, unrestricted equity being an equity that can be distributed back to shareholders without application of specific rules protecting creditors.

Generally, in capital system with nominal value of shares, restricted equity consist of (i) share capital, (ii) reserve fund and (iii) other funds created under the accounting acts. On the other hand, unrestricted equity under this capital system usually consists of (i) other funds created by the company which distribution is not restricted and (ii) profit from current and previous financial periods. Share premium can be considered restricted equity as well as unrestricted equity.

On the other hand, restricted equity under the capital system without nominal value of shares usually consists of (i) share capital and (ii) reserves and funds created under the accounting act. Unrestricted equity in this capital system consists of (i) other reserves created by the company and (ii) profit from current and previous financial periods.

Basic distinction between restricted and unrestricted equity is the mechanism of their distribution. If the distribution of restricted equity is in question the general rules for unrestricted equity distribution must be followed and, at the same time, specific requirements must be fulfilled to protect creditors (consent of creditors or necessity to maintain the share capital of the company at the required amount).

5.2 Equity in capital system with nominal value of shares

In the SCC equity is defined as “*entrepreneur’s own resources used to finance the entrepreneur’s business property under a special regulation.*”⁷⁶ This wording of the SCC refers to the Slovak Accounting Act⁷⁷ and to the Accounting Procedures for Entrepreneurs^{78, 79} Thus, in the SCC we cannot find a clear definition of the equity and determination of the difference between restricted and unrestricted equity. For the complex picture we need to analyse the wording of the SCC, Slovak Accounting Act and other relevant acts and decrees.

Restricted equity in capital system with nominal value of shares

Under the Slovak legal system as restricted equity shall be considered (i) share capital, (ii) reserve fund, (iii) share premium account and (iv) other funds created based on the Slovak Accounting Act. Share capital of the company is sum that is registered into the commercial register and is at least 25.000 EUR.⁸⁰ Sum of nominal values of shares are mirrored

⁷⁶ SCC, Section 6.

⁷⁷ Act no. 432/2002 Coll. Accounting Act as amended (Zákon č. 432/2002 Z. z. o účtovníctve v znení neskorších predpisov) (hereinafter referred to as “*Slovak Accounting Act*”).

⁷⁸ Accounting Procedures for Entrepreneurs (Účtovné pravidlá pre podnikateľov).

⁷⁹ KALETOVÁ, V. Základné imanie obchodných spoločností. *Poradca Podnikateľa*. 2004, No. 1, p. 2 and KALETOVÁ, V. Vklady do obchodných spoločností, základné imanie a podiely v obchodných spoločnostiach. *Poradca Podnikateľa*. 2008, No. 11–12, pp. 2–3.

⁸⁰ SCC, Section 157 and 162.

in the commercial register as a registered capital.⁸¹ Registered legal capital can be reduced just under a specific regulation of creditor protection based on Section 215 of the SCC.

Creation of reserve fund is stipulated in the SCC in Sections 67 and 217. Reserve fund is created at the time of company's incorporation from the difference between the subscription price and the nominal value of share (share premium) at the amount of at least 10% of the share capital, company is obliged to increase the reserve fund every year at least for 10% of the net profit.⁸² The minimum amount of the reserve fund is 20% of the share capital of the company.⁸³ Reserve fund can be used just for covering losses of the company⁸⁴ and the board of directors decides about the use of the reserve fund.⁸⁵ Therefore, reserve fund shall serve as a shield in case the business of the company is not running in the expected way and the annual accounting report will dispose loss.⁸⁶

When analysing the reserve fund it is crucial to take into consideration Section 215b: Subsection 2 of the SCC. This section of the SCC stipulates the following situation: if registered capital of the company is reduced by the withdrawal of the shares from the circulation and if the shares whose issue price has been fully paid (i) are provided by shareholders without charge in order to reduce the registered capital or (ii) will be withdrawn from circulation for a consideration which may be paid only from the net profit – the reserve fund must be supplemented with the amount of the nominal values of shares withdrawn from circulation.⁸⁷ According our view, such an increase of the reserve fund shall be kept permanently. The possible use of this amount of the reserve fund can be (i) decrease of the legal capital and (ii) cover the losses of the company.⁸⁸

It is crucial to stipulate that under the Slovak Accounting Act and the Accounting Procedures for Entrepreneurs reserve fund is a balancing item on the liabilities side of the balance sheet of the company without any substantial reserve on the side of the assets of the company.⁸⁹ Therefore, the reserve fund is “just” an accounting item which use is not restricted after the incorporation of the company (the same as share capital of the company). Based on the purpose of the reserve fund one could imply that the amount credited to the reserve fund is allocated in a separate bank account which cannot be used for the company, this is however not the case.

Based on the Slovak Accounting Act and the Accounting Standards for Entrepreneurs another fund created by the company is the share premium account. In this account the

⁸¹ PATAKYOVÁ, M. Commentary on Section 157 of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck, 2013, p. 643 and DAVIES, P. L. *Principles of Modern Company Law*. London: Sweet & Maxwell, 2012, p. 274.

⁸² SCC, Section 217.

⁸³ SCC, Section 217.

⁸⁴ SCC, Section 67.

⁸⁵ SCC, Section 217.

⁸⁶ *Obchodný zákonník s rozsiahlym komentárom a judikatúrou po poslednej novele vykonanej zákonom NR SR č. 9/2013 Z. z. a Zákon o obchodnom registri po poslednej novele vykonanej zákonom NR SR č. 9/2013 Z. z. s rozsiahlym komentárom*. Bratislava: Nová práca, 2013, p. 107.

⁸⁷ SCC, Section 215b.

⁸⁸ PATAKYOVÁ, M. Commentary on Section 215b of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck, 2013, p. 850.

⁸⁹ PATAKYOVÁ, M. Commentary on Section 217 of SCC. In: PATAKYOVÁ, M. et al. *Obchodný zákonník (Komentár)*. Praha: C. H. Beck, 2013, p. 853.

difference between the subscription price and the nominal value of shares is accounted in the case when subscription price of shares is higher than their nominal value.⁹⁰ Share premium account is treated in the Slovak Republic in a same way as share capital of the company.

Unrestricted equity in capital system with nominal value of shares

On the other hand, unrestricted equity under the Slovak legislation is (i) other funds created in the company, which are not restricted under the wording of the SCC and the Slovak Accounting Act, (ii) profit from current and previous financial periods and (iii) reserve fund created above the required amount stipulated in Section 217 of the SCC. However, regulation of creation of other funds is not covered by the SCC. The reasoning behind this loophole in the legal regulation of the Slovak Republic can be the inaccurate transposition of the Capital Directive.⁹¹ The inexact transposition was caused by the imprecise translation of some key terms used in this directive.

5.3 Equity in capital system without nominal value of shares

According to the FLLCA the equity in the limited liability company shall be divided into restricted equity and unrestricted equity.⁹²

Restricted equity in capital system without nominal value of shares

Under Chapter 8: Section 1: Subsection 1 of the FLLCA restricted equity shall consist of (i) share capital of the company and (ii) reserve and funds created under the Finnish Accounting Legislation. Share capital of the company is considered to be the traditional restricted equity.⁹³ Distribution of the share capital is dependent on the consent of creditors and rules requiring the maintenance of capital.⁹⁴ Reserves and funds created under the Finnish Accounting Legislation cannot be distributed to the shareholders even with the consent of creditors.⁹⁵

Under the FLLCA no share premium account is created, even if companies opt for traditional capital system with nominal value of shares. The difference in subscription price and nominal value is credited fully or partially to the reserve for invested unrestricted equity or to the share capital.⁹⁶

⁹⁰ CENIGOVÁ, A. *Podvojně účtovníctvo podnikateľov*. Bratislava: CENIGA, s.r.o., 2012, p. 257.

⁹¹ FARKAŠ, R. K článku: Ad: Ostatné kapitálové fondy (účet 413). *Dane a účtovníctvo v praxi*. 2013, No. 3, p. 3.

⁹² FLLCA, Chapter 8: Section 1: Subsection 1.

⁹³ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 315.

⁹⁴ FLLCA, Chapter 14.

⁹⁵ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 316.

⁹⁶ TOIVIAINEN, H. *Introduction to Finnish business law*. Helsinki: Edita, 2008, p. 636 and AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 316.

Unrestricted equity in capital system without nominal value of shares

On the other hand, unrestricted equity shall consist of (i) other reserves especially reserve for invested unrestricted equity and (ii) profit from the current and previous financial periods.⁹⁷ The main unrestricted equity fund under the FLLCA is the reserve for invested unrestricted equity. However, other funds can be created by companies based on the articles of association or the decision made by shareholders on the shareholders' meeting. These funds are created by the company voluntarily and thus they are considered to be unrestricted equity.⁹⁸ The idea behind this is, that the company can voluntarily create funds⁹⁹ to which assets will be transferred for example part of the profit created during the particular year.¹⁰⁰

Reserve for invested unrestricted equity is credited with that part of the subscription price of the shares that is not credited, according to the memorandum of association or the share issue decision, to the share capital or part of the subscription price that is not credited under the Finnish Accounting Legislation into the liabilities or to some other reserves.¹⁰¹ This reserve is credited with other equity income, which is not aimed to be credited to another reserve.¹⁰² Moreover, this reserve shall be credited with an amount of the share capital reduction, unless part of this amount is needed for the covering of the losses or the distribution of assets.¹⁰³

Reserve for invested unrestricted equity can be distributed to the shareholders under similar conditions that the dividend distributions even the fact that the decision on these distributions is kept separate in the FLLCA – separate decision of general meeting is required for distribution of unrestricted equity and dividend distribution.¹⁰⁴

6. INEXACT TRANSPOSITION OF THE CAPITAL DIRECTIVE INTO THE SCC

6.1 Translation of the word “reserves” as “reserve funds”

Term “reserves” mentioned in the Article 15 part 1 letter c) of the Directive 77/91/EEC and the Article 17 part 3 of the Directive 2012/30/EU in the English version was translated into the Slovak version of the directive as “reserve funds”. Such translation causes limitation

⁹⁷ FLLCA, Chapter 8: Section 1: Subsection 1 and Section 2.

⁹⁸ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 316.

⁹⁹ *Toiviainen* stipulates that such funds can have specifically determined purpose such as research fund, product development fund, investment fund, etc. which limits the possible use of the fund even though it falls under the unrestricted equity. If the fund created by the company has no specification regarding its use it can be freely used or distributed following the FLLCA. TOIVIAINEN, H. *Introduction to Finnish business law*. Helsinki: Edita, 2008, p. 637.

¹⁰⁰ TOIVIAINEN, H. *Introduction to Finnish business law*. Helsinki: Edita, 2008, p. 637.

¹⁰¹ FLLCA, Chapter 8: Section 2.

¹⁰² AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 316.

¹⁰³ FLLCA, Chapter 8: Section 2.

¹⁰⁴ AIRAKSINEN, M. The Delaware of Europe? – financial instruments in the new Finnish Companies Act. In: ANDERSEN, P., SØRENSEN, K. (eds.). *Company Law and Finance*. Copenhagen: Forlaget Thomson, 2008, p. 316 and FLLCA, Chapter 13: Section 5 and following.

in interpretation of this word in the context of the Slovak legal system. The use of the reserve fund created in the company within the required amount is limited to regulation that *“such fund may only be used to the extent to which it is created obligatory under this Act, and only for the purpose of covering company losses, unless a special Act stipulates otherwise.”*¹⁰⁵

Amendment of the SCC¹⁰⁶ opened a possibility for broader interpretation of funds created in the company that shall be considered as unrestricted equity. This amendment consisted of change in the wording in Section 179: Subsection 3: Letter b) – *“... shareholders are only entitled to the distribution among/between them of net profit that has been ... b) increased by the retained profit of previous years and funds created from profit whose utilisation is not stipulated by law”* – collocation *“funds created from profit”* was changed into *“other own resources”*. This amendment is a reaction to remarks made by Ministry of Finance of the Slovak Republic, the Slovak Banking Association and the National Union of Employees in the interdepartmental remarking procedure. These entities pointed out the uncertainty of the wording of Section 179: Subsection 4 which causes application and interpretation problems.¹⁰⁷

The roots for this misinterpretation can be found in the above mentioned misleading and narrow transposition of the Directive 77/91/EEC repealed by the Directive 2012/30/EU. Wording of the Article 17: Subsection 3 of the Capital Directive reads in English version as following: *“The amount of distribution to shareholders may not exceed the amount of the profits at the end of the last financial year plus any profits brought forward and sums drawn from reserves available for this purpose, less any losses brought forward and sums placed to reserve in accordance with the law or the statutes.”* In the Slovak mutation of this directive is the collocation *“reserve”* translated as *“reserve funds”* which causes many interpretational problems because the term *“reserve funds”* refer to the legal reserve fund created under Sections 67 and 217 of the SCC and specific reserve fund for the treasury shares under Sections 161d a 215b of the SCC.¹⁰⁸

English word *“reserves”* refers not just to legal reserve fund¹⁰⁹ but as well to other company resources as: (i) issue premium¹¹⁰, (ii) other capital funds¹¹¹ and (iii) revaluation

¹⁰⁵ SCC, Section 67: Subsection 1.

¹⁰⁶ The aim of the act was partial implementation of the Directive 2012/17/EU, implementation of the requests stipulated by the government, amendment of the transposition annexes in the Directive 2012/30/EU and the requirements from the application practice. Explanatory report – general part to the Act no. 357/2013 Coll. which amends the Commercial Code as amended and other acts (Dôvodová správa – všeobecná časť k Zákonu č. 357/2013 Z. z. ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony), p. 1.

¹⁰⁷ Explanatory report – general part to the Act no. 357/2013 Coll. which amends the Commercial Code as amended and other acts (Dôvodová správa – všeobecná časť k Zákonu č. 357/2013 Z. z. ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony), p. 3.

¹⁰⁸ Explanatory report – general part to the Act no. 357/2013 Coll. which amends the Commercial Code as amended and other acts (Dôvodová správa – všeobecná časť k Zákonu č. 357/2013 Z. z. ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony), p. 4.

¹⁰⁹ Account 411 – Legal capital account CENIGOVÁ, A. *Podvojný účtovníctvo podnikateľov*. Bratislava: CENIGA, s.r.o., 2012, pp. 250–257.

¹¹⁰ Account 412 – Issue premium account CENIGOVÁ, A. *Podvojný účtovníctvo podnikateľov*. Bratislava: CENIGA, s.r.o., 2012, pp. 257–258.

¹¹¹ Accounts 413 – Other capital funds account CENIGOVÁ, A. *Podvojný účtovníctvo podnikateľov*. Bratislava: CENIGA, s.r.o., 2012, pp. 258–261.

funds¹¹². These other funds are considered to be own resources of the company and fall under the equity as stipulated in Section 6: Subsection 4 of the SCC which are not stated to be reserve funds. It is necessary to point out that the aim of the Article 17: Subsection 3 of the Capital Directive is not just the distribution of the funds created from the profit, as it is under Section 179: Subsection 3: Letter b) of the SCC, but any other funds created within the company.¹¹³ Therefore, it is possible to conclude that the wording of the Section 179: Subsection 3: Letter b) of the SCC does not correspond to the intentions of the Article 17: Subsection 3 of the Capital Directive even though the word “reserve” is not mentioned directly. Thus, with the change of the wording in the SCC from “funds created from profit” into “other own resources” the stipulation of the Section 179: Subsection 3: Letter b) will be more precise and will correspond to the wording of the Capital Directive.

According to our point of view amendment of the wording in the SCC is at least a small step forward and removes the inconsistency with the Capital Directive. However, the new wording of the Section 179: Subsection 3: Letter b) stays unclear because the definition of the collocation “other own resources” is unknown as there is no explanation for this term in the SCC. We can track this term in Section 179: Subsection 4 of the SCC: “The company may not distribute net profit or other of its own resources ...” Though, there is no definition of the term other own resources of the company. As it stems from the Explanatory report to the Act no. 357/2012 Coll. these other own resources should be (i) issue premium fund, (ii) other capital funds and (iii) revaluation funds. The inconsistency of the interpretation of this term is crucial for the distribution of assets out from the company. The most controversial discussion about the “other own resources” of the company is around the “other capital funds”.

6.2 Other capital funds

“Other capital funds” is a fund characterised in the Slovak Accounting Act and the Accounting Procedures for Entrepreneurs. Creation and use of this fund is a highly discussed topic in the Slovak Republic. It is heavily argued, whether this fund could be created and if yes whether it should be considered as part of the restricted equity in the company or unrestricted equity. The basis for our analysis was the debate between *Farkaš* and *Čarnogurský*.

Under the Accounting Standards for Entrepreneurs this fund is created by monetary as well as non monetary contributions of shareholders which do not result in increase of the share capital.¹¹⁴ According to *Farkaš* contribution of shareholders into this fund is voluntary, such a contribution cannot be considered as part of the share capital as that is not increased by this contribution and it cannot be considered as share premium or a reserve

¹¹² Accounts 414-416 – Revaluation Account CENIGOVÁ, A. *Podvojně účtovníctvo podnikateľov*. Bratislava: CENIGA, s.r.o., 2012, pp. 261–262.

¹¹³ Explanatory report – general part to the Act no. 357/2013 Coll. which amends the Commercial Code as amended and other acts (Dôvodová správa – všeobecná časť k Zákonu č. 357/2013 Z. z. ktorým sa mení a dopĺňa zákon č. 513/1991 Zb. Obchodný zákonník v znení neskorších predpisov a ktorým sa menia a dopĺňajú niektoré zákony), p. 4.

¹¹⁴ DOBŠOVIČ, D. Kapitálové fondy a fondy tvorené zo zisku (účtovné súvzťažnosti). *Dane a účtovníctvo v praxi*. 2009, No. 5, p. 2.

fund.¹¹⁵ *Farkaš* claims that creation of this fund is in line with the principle of protection of creditors as the capital of the company is improved and thus the protection of creditors as well.¹¹⁶ He claims that creation of this fund is therefore in line with the Capital Directive as it maintains the capital of the company because in case of a loss company can use these funds to cover them, without a necessity to decrease the share capital.¹¹⁷ Additional advantage of this fund is flexible increase of the company's equity as burdensome administrative procedures connected with increase of the share capital are avoided.¹¹⁸ *Farkaš* stipulates that the non-monetary contribution does not need to be evaluated.¹¹⁹ Under his argumentation this fund can be used in a same way as other funds created by the company which are not restricted.¹²⁰ From this characteristic, it is possible to incline that *Farkaš* clearly claims that this fund should be considered as unrestricted equity of the company, which can be distributed back to shareholders.¹²¹

On the other hand, *Čarnogurský* had some opposite statements toward the other capital funds. He particularly reacted to the statements made by *Farkaš*¹²² and objected that this fund could be (i) created by contribution of shareholders and (ii) distributed to shareholders as unrestricted equity.¹²³ According to his argumentation this fund cannot be created by contribution of shareholders as the SCC stipulates that “shareholder's investment contribution shall be an aggregate of funds and other assets that may be expressed in monetary term”¹²⁴ and share capital “means the total of all shareholder's monetary and non-monetary contributions.”¹²⁵ Therefore, *Čarnogurský* claims that shareholder can make a monetary or non-monetary contribution just to the share capital of the company.¹²⁶ Therefore, other capital funds cannot be created by contributions of shareholder.

According to our point of view, conclusions and interpretations presented by *Farkaš* are too broad, especially regarding the use of the other capital fund and the possible distribution of this fund back to shareholders. On the other hand, *Čarnogurský* presents too narrow interpretation and the notion of other capital funds¹²⁷. It is possible to agree with

¹¹⁵ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition, 2012, p. 90.

¹¹⁶ *Ibid.*

¹¹⁷ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition, 2012, pp. 90–91 and FARKAŠ, R. *Ostatné kapitálové fondy (účet 413)*. *Dane a účtovníctvo v praxi*. 2013, No. 1, p. 2.

¹¹⁸ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition. 2012, p. 91. and *Farkaš* 2013 (*Ostatné kapitálové fondy*), p. 2.

¹¹⁹ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition, 2012, p. 91 and FARKAŠ, R. *Ostatné kapitálové fondy (účet 413)*. *Dane a účtovníctvo v praxi*. 2013, No. 1, pp. 2–3.

¹²⁰ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition. 2012, p. 92 and FARKAŠ, R. *Ostatné kapitálové fondy (účet 413)*. *Dane a účtovníctvo v praxi*. 2013, No. 1, pp. 4–4.

¹²¹ *Ibid.*, pp. 3–4.

¹²² First reaction was presented in an article *Čarnogurský, Ján* (2013). Ad: *Ostatné kapitálové fondy (účet 413)*. *Dane a účtovníctvo v praxi* and the second (complex) reaction was published in a separate document *Čarnogurský, Ján et al.* (2013). *Ostatné kapitálové fondy*. ČARNOGURSKÝ, J., *ULC PRO BONO 4* as the journal “*Dane a účtovníctvo*” refused to publish the further reactions to this topic by ČARNOGURSKÝ, J.

¹²³ ČARNOGURSKÝ, J. *Dane a účtovníctvo v praxi*. 2013, No. 3, p. 1.

¹²⁴ SCC, Section 59.

¹²⁵ SCC, Section 58.

¹²⁶ ČARNOGURSKÝ, J. *Dane a účtovníctvo v praxi*. 2013, No. 3, p. 1.

¹²⁷ *Ján Čarnogurský* takes into consideration just the SCC and he is not taking into account Slovak Accounting Act and Slovak Tax legislation what is diminishing his argumentation, as it is crucial to analyse the legal system complexly. BALÁŽ, O. K. *Článku*: Ad: *Ostatné kapitálové fondy (účet 413)*. *Dane a účtovníctvo v praxi*. 2013, No. 3, pp. 1–2.

*Kotlárík*¹²⁸ and *Banas*¹²⁹, that such a narrow interpretation of the notion of contribution by *Čarnogurský* diminishes other concepts as creation of reserve fund – reserve fund is as well as created by contributions of shareholders. The whole problem is stemming from the inaccurate transposition of the wording of the Capital Directive – terms “*capital*”, “*reserves*” and “*contributions*”. Stemming from our analyses, it is unquestionable that such fund can be legally created under the Capital Directive. Concept of other capital funds in the Slovak Republic reminds us the reserve for invested unrestricted equity under the FLLCA. The main problem is an unclear Slovak regulation of these funds as which causes that (i) there is no clear qualification whether this other capital funds is restricted or unrestricted equity, (ii) use of this fund is highly uncertain and (iii) distribution to shareholders of this fund doubtful. Additionally, dangerous is the position of *Farkaš* who claims that the non-monetary contribution into this fund does not need to be evaluated¹³⁰ as it is not a contribution to the share capital. Such opinion is decreasing the creditor protection. Evaluation of the non-monetary contribution of shareholders is one of the core rules serving as protection of creditors when the capital of the company is established and it secures that the value of the assets claimed to be in company is fair and true¹³¹. Even though based on the strict interpretation of the Section 59 of the SCC just contributions to the share capital shall be evaluated, according to our point of view these rules shall be applied *mutatis mutandis* to the evaluation of shareholders’ contributions to the other capital funds. If the subscription price is covered with non-monetary contribution under the FLLCA it always needs to be property evaluated.¹³²

7. CONCLUSION

Rules regulating capital of companies emerged in the Europe in the second half of the 19th century and they were heterogeneous among the states. Harmonization of the legal capital doctrine on the European level was conducted by Directive 77/91/EEC. Adoption of the Directive 77/91/EEC was aimed to reduce the agency problems and costs between shareholders and creditors via regulation. This directive introduced the minimum legal capital rules and the maintenance rules and is nowadays heavily criticised as being an outdated concept. First of all, any attempt to design universally applicable rule on the amount of the legal capital necessary for the protection of creditors is arbitrary. Both companies and creditors being heterogeneous dynamic constituencies require that the creditor protection is tailored taking into consideration commercial circumstances.

Finland, as a Member State of the European Union has a unique capital system, which proved that it is possible to have “*true*” capital system with shares without nominal value under the Capital Directive. This capital system provides effective creditor protection and here, We would like to present the core benefits of the legislation:

¹²⁸ KOTLÁRIK, M. Ostatné kapitálové fondy – úvahy de lege lata a de lege ferenda. *Dane a účtovníctvo v praxi*. 2013, No. 4, p. 2.

¹²⁹ BANAS, M. K článku „Ostatné kapitálové fondy (účet 413)“. *Dane a účtovníctvo v praxi*. 2013, No. 4, p. 2.

¹³⁰ FARKAŠ, R. *Vlastné imanie obchodných spoločností Účtovné aspekty*. Bratislava: Iura Edition, 2012, p. 91 and FARKAŠ, R. Ostatné kapitálové fondy (účet 413). *Dane a účtovníctvo v praxi*. 2013, No. 1, pp. 2–3.

¹³¹ This conclusion is based on the Capital Directive.

¹³² FLLCA, Chapter 2: Section 6: Subsection 1 and Chapter 9: Section 12: Subsection 1.

Since 2006, when the FLLCA introduced the possibility to opt for capital system without nominal value of shares the equity under the Finnish legislation became highly flexible and business oriented. The FLLCA clearly states the difference between restricted and unrestricted equity. Under restricted equity falls (i) legal capital and (ii) funds and reserves created under Finnish Accounting Legislation. The minimum amount of the legal capital for public limited liability companies is 80.000 EUR and this sum must be fully paid. Under the FLLCA no reserve fund and no share premium account is created anymore. Articles of association or the share issue decision will stipulate the amount of the subscription price to be credited to the share capital (accountable par). The concept of accountable par as introduced by Article 8 of the Capital Directive is applied in a unique way under the FLCA. After the share capital is formed (at least at the minimum required amount) the subscription price can be fully credited to the unrestricted equity, mainly to the reserve for invested unrestricted equity or other funds created voluntarily by the company. Therefore, accountable par of the share can be in the above described scenario zero. Moreover, based on the fact that accountable par of the share can be zero, it is possible to issue bonus shares to company without payment – bonus share issues. The above described mechanism allows flexible allocation of the equity, which is in favour of the shareholders to conduct further investments or to get the assets from the company.

On the other hand, the Slovak Republic is as a country following the traditional capital system with shares with nominal value. First of all, the share capital does not need to be paid in full – such regulation is criticised even though it is in line with the Capital Directive. Moreover, wrong transposition of the Directive 77/91/EEC caused a problem with creation of “*other capital funds*” which are recognized by the Slovak Accounting Act but not by the SCC. It is unclear whether such funds can be created, and if yes, how they can be assessed, contributed to and used. Additionally, the concept of restricted equity and unrestricted equity is ambiguous and unclear which causes never-ending debates between scholars.