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INSOLVENCY PROCEEDINGS OF INDUSTRIAL COMPANIES IN CZECH REPUBLIC AND SLOVAKIA

In the presented contribution we evaluated the insolvency proceedings in chosen industrial companies in Czech Republic and Slovakia, and we can state that the number of bankruptcy in both countries is gradually increasing year after year. We also analyzed the reasons for insolvency and the ways of solving them. Most often the reasons for insolvency were the consequences of economic crisis. According to the results of analysis we can state that insolvency law is a positive development, but there are still reserves and space for further improvement.

Keywords: *insolvency proceeding; bankruptcy; industrial company; creditor; indebtedness.*

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ПРОЦЕДУРИ ОФОРМЛЕННЯ НЕПЛАТОСПРОМОЖНОСТІ ПРОМИСЛОВИХ ПІДПРИЄМСТВ ЧЕСЬКОЇ РЕСПУБЛІКИ ТА СЛОВАЧЧИНИ

У статті описано процедури легального оформлення неплатоспроможності на прикладі низки промислових підприємств Чеської Республіки та Словаччини. Продемонстровано, що в обох країнах кількість банкрутств зростає з року в рік. Проаналізовано причини неплатоспроможності та способи їх усунення. Більшість випадків оголошеної неплатоспроможності пов'язано з наслідками економічної кризи. Доведено, що зміни в законодавстві значно покращили та прояснили ситуацію, однак все одно лишається простір для пошуку нових рішень даної проблеми.

Ключові слова: *процедура оголошення неплатоспроможності; банкрутство; промислове підприємство; кредитор; заборгованість.*

Рис. 4. Табл. 2. Літ. 18.

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ПРОЦЕДУРЫ ОФОРМЛЕНИЯ НЕПЛАТЁЖЕСПОСОБНОСТИ ПРОМЫШЛЕННЫХ КОМПАНИЙ В ЧЕШСКОЙ РЕСПУБЛИКЕ И СЛОВАКИИ

В статье описаны процедуры легального оформления неплатёжеспособности на примере ряда промышленных предприятий Чешской Республики и Словакии. Показано, что в обеих странах количество банкротств растёт из года в год. Проанализированы причины неплатёжеспособности и способы их устранения. Большинство случаев объявленной неплатёжеспособности связаны с последствиями экономического кризиса. Доказано, что изменения в законодательстве значительно улучшили и прояснили ситуацию, однако всё равно остаётся пространство для поиска новых решений данной проблемы.

Ключевые слова: *процедура объявления неплатёжеспособности; банкротство; промышленное предприятие; кредитор; задолженность.*

Introduction. Business brings not only possibility to get profit, but also potential complications. Problem-solving in companies is influenced by specific business conditions. Companies are exposed to negative impacts of unfavorable economic development in a country. Solution can be various in nature and insolvency management

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is one of possible solutions. Due to the current economic situation we can assume an increased number of companies that atop their activity at various markets. There are cases when companies do not avoid insolvency and bankruptcy as it is the only solution in their situation. Thus, insolvency becomes a topic for discussion not only among experts. In the EU experts and lawmakers are trying to amend laws so that it would be effective in practice and would help debtors.

Theoretical basis. Enterprise insolvency can be considered from two perspectives: insolvency by formal criteria as established by legislation; insolvency defined as the assumed inability to fulfill its obligations in due time. In the first case, possibilities for active management to influence the situation is severely limited. In the second situation, an enterprise is in a position of pre-bankruptcy, but creditors have not yet filed claims on matured obligations and due payments. The main goal of the company on the verge of bankruptcy is to ensure financial stability and balanced cash flow (Elakova, 2014).

Insolvency law adjust solving of bankruptcy or threatening insolvency of debtor in the frame of legal proceedings is directed by the way it could adjust property relationships of persons, touched by debtor's insolvency to the highest possible satisfaction of creditors.

Among basic principles of insolvency proceeding is that it must be carried out so that any participant would not be righteously severed or illegally privileged with the aim of achieving rapid and highest possible satisfaction of creditors. Insolvency proceeding is possible to begin only after an insolvency proposal. Only debtor or creditor is justified to register this insolvency proposal. Execution of judgment, related to property basis, can be prescribed, but not executed. Restraining of debtor to deal with property presents other very important effect, connected with opening an insolvency proceeding. If debtor would violate it, his acts against creditors can be ineffective. Creditors of debtor are justified from the time of insolvency proceeding opening to apply their claims by application. Creditor can send application of claims from the time of notification about the insolvency proceeding opening till the time the court decision on insolvency is stated. Insolvency law states the ways of bankruptcy solving as bankruptcy, discharge of debtors, reorganization, and special ways of insolvency solving.

Current state of insolvency solving in the EU. The current crisis and discussions in the Euro area in particular, show that sovereign debt crises/defaults are no longer confined to developing economies (Stahler, 2013). Today more and more companies are faced with multiple failures, which are the basic problem that crisis management must resolve. Under economic decline, the need for change at the organizational level is imperative to facilitate the recovery of a company (Onofrei and Lupu, 2012). Tracking the risk of "newly incorporated companies" provides a particular challenge since there is very limited publically available data in the time period from incorporation date until the submission of the first accounts. And a large number of these companies fail (via bankruptcy) (Wilson and Altanlar, 2014). Every country has its own legal regulations of insolvency solving. Due to cooperation of individual companies among the states of the European Union, EU Council constituted Regulation No 1346/2000 which is to regulate such relations. Regulation refers to the insolvency proceeding with the basic goal to avoid asset transference or legal proceeding from

one EU country to other, since by this way there could be provided more convenient position of debtors and handicap of creditors. A cross-border insolvency regime involves a trade-off between increased cross-border economic activity and application of less preferred substantive insolvency law (Franken, 2013).

This regulation defines main and secondary proceedings, solved by court, authorized for opening of insolvency proceeding. Main proceedings are in progress of the EU country, where debtor has his main residence and from where he makes his interests. As for corporate entities it means the residence of entity, physical entity is determined by a place of employment or common address. In case opening of insolvency proceeding is in any EU country, such proceeding is immediately approved in all other countries. Administrator of bankruptcy can act also in other EU countries according to decrees of a country, in which proceeding is opened, and must observe them. Possibility to transfer property of debtor or to enter a lawsuit due to invalidity of legal act, when property had been transferred from a country of main proceeding after its opening, which would handicap creditors, belongs among his competences. As for the present situation, M. Schillig (2014) analyses, for example, recent developments in Europe, the rise of pre-packaged administrations and the reformulation of the anti-deprivation principle. M. Bridge and J. Braithwaite (2013) suggest that the use of private law to manage the fall-out to the recent crisis has come at a price, which is the impact on a number of fundamental legal principles that underpin markets. We conclude that the continued robustness of private law requires a more proactive approach. Basic characteristic of German insolvency law means that it does not follow up during companies' insolvency only insurance of authorized claims of creditors, but it emphasizes also the importance of preservation of company' s value and working posts at the same continuing business activity of the company that is in insolvency. Its main goal is to provide support for realization of debtor's activities and by this way to satisfy all unsecured creditors (Wilhelm et. al, 2012).

Similarly, Slovak and Czech law explain the idea of insolvency, where debtor is in insolvency when he is not able to pay or he is indebted. Insolvent debtor is the one that is not able to fill at least two of his monetary liabilities 30 days after a payable period against more than one creditor. Indebted debtor is the one that is obligatory to lead accounting according special decree and that has more than one creditor and value of his payable liabilities exceeds the value of his property (Richter, 2008). In contrast to Czech law, Slovakia insolvency law gives legal entities two possibilities for insolvency solving: bankruptcy and restructuring. Bankruptcy means classical conversion of remaining property of the insolvent company to cash and consequent satisfaction of creditors the goal of restructuring is satisfaction of creditors' demands from profits from further activity of the company (Jakubec and Kardos, 2012). Position of creditors under Slovakian insolvency law is connected with a number of basic decision authorizations. Mainly a creditor can decide the best how to use this property (Richter, 2008).

Table 1 illustrates the scale of chosen countries, with the mentioned lengths of insolvency proceeding in a year, costs for insolvency proceeding (rate on property) and measure of creditor' satisfaction (cents per USD). Czech and Slovak Republic, according to the evaluated criteria, are far off countries, as compared to for example Norway, Great Britain, Germany etc. On the other hand, comparing with such coun-

tries as Poland, Hungary, Greece etc. both countries have significantly better positions.

Table 1. **Evaluation of insolvency proceedings in chosen countries** (www.doingbusiness.org)

Country	Ranking	Time of duration	Costs, % of property	Measure of satisfaction, cents per USD
Japan	1	0.6	4	92.8
Norway	2	0.9	1	91.3
Finland	3	0.9	4	90.2
Netherlands	5	1.1	4	89.2
Belgium	6	0.9	4	89.0
Great Britain	7	1.0	6	88.6
Ireland	8	0.4	9	87.6
Denmark	10	1.0	4	87.0
Island	11	1.0	4	84.5
Germany	13	1.2	8	82.9
Austria	14	1.1	10	82.4
USA	17	1.5	7	81.5
Sweden	20	2.0	9	75.5
Spain	22	1.5	11	72.3
Portugal	23	2.0	9	71.6
Cyprus	24	1.5	15	70.5
Czech Republic	29	2.1	17	65.0
Italy	33	1.8	22	62.7
Israel	35	2.0	23	60.6
Poland	37	3.0	15	54.8
Slovakia	38	4.0	18	54.1
Slovenia	41	2.0	4	50.1
France	46	1.9	9	48.3
Switzerland	47	3.0	4	47.6
Estonia	66	3.0	9	38.9
Hungary	70	2.0	15	38.3
Greece	87	3.5	9	34.0
Bulgaria	92	3.3	9	32.6
Croatia	98	3.1	15	30.3

Insolvency proceedings in chosen industrial companies of Czech and Slovak Republic. Industrial companies are very sensible to influences. Due to their capital intensity they usually use foreign capital. Due to large credits they are also dependable on banks and financial institutions. Industrial companies are using for their production primarily materials, the price of which is determined at world markets is often dependent on global problems, which industrial companies cannot influence. This is why they are exposed to high risk of considerate changes in input prices. They are influenced also by currency stability in other countries, with which they make business.

Property of such companies is usually large in volume. Due to specifics of production such property is hard to sell. Moreover, in many cases it is not effective to sell property in parts, since its value is higher under complex use. Therefore, industrial companies have problems with liquidity of their property.

Due to the mentioned above it is obvious that it would be not effective for industrial companies to resign from the market during greater problems. Therefore, reorganization (restructuring) can become the tool to preserve companies, to renew their activity and minimize consequences for regional unemployment and finally to keep traditional production alive that in case of many industrial companies is very unique. It could also bring chance for small creditors since their claims could be at least partly paid when preserving a company.

Insolvency law is still more of a tool in bankruptcy solving not for commercial subjects, but in case of individuals' bankruptcy. Table 2 illustrates the development of bankruptcy numbers and the chosen ways of their solution in chosen industrial companies in Czech Republic from the time of Insolvency Law came in force.

Table 2. **Bankruptcies of chosen industrial companies in Czech Republic,** *own elaboration from* (Heglasova, 2010)

	Year					
	2008	**2009**	**2010**	**2011**	**2012**	**2013**
Registered insolvency suggestions	5236	9396	16101	24466	32656	37613
Decision about insolvency	1368	3941	8004	14118	20700	25044
Allowed discharge	646	2164	5902	11614	17985	22063
Allowed reorganization	6	16	19	17	14	12
Promulgated bankruptcy	769	1808	2204	2671	3172	4088

After 5 years of Insolvency Law being in force the number of bankruptcy is gradually increasing year after year. One for the reasons of such growth could be the development of general economic situation in recent years. Registered insolvency suggestions are higher than the number of real companies in bankruptcy. This confirms the efforts to solve problems of companies at the market mainly by insolvency proceedings. Difference in insolvency suggestions and decisions on bankruptcy is still increasing.

Development of bankruptcy number in Slovakia. In 2013 there were 394 promulgated bankruptcy in Slovakia, which is 32 cases more against 2012 (362) and about 2 more than in 2011 (392). 317 bankruptcies have been promulgated on the property of legal entities and 77 – on property of physical entities – traders. Business, industry and building were most problematic branches in 2013, as well as in 2012, the highest rate of bankruptcies was in both years promulgated in Bratislava County. From the total number – 394 bankruptcies – 317 bankruptcies (or 80.46%) were promulgated mainly at the property of legal entities (ltd – 273, joint stock companies – 36, cooperatives – 5, limited partnership – 2, state enterprises – 1) and 77 (19.54%) – on property of physical entities (self-employed). Also some of greatest employers ended up in 2013 in bankruptcy, mainly companies with allowed reorganization (Markova, 2013).

The highest rate of reorganizations was in 2013, which was about 12 more than in 2010 (the record year). 108 reorganizations were allowed to legal entities, 1 – to civil consortium and 4 – to physical entities – traders (Figure 2). Similarly as in 2012, the highest rate of reorganizations was allowed in industry, business and construction sector (Statistical Office, 2013).

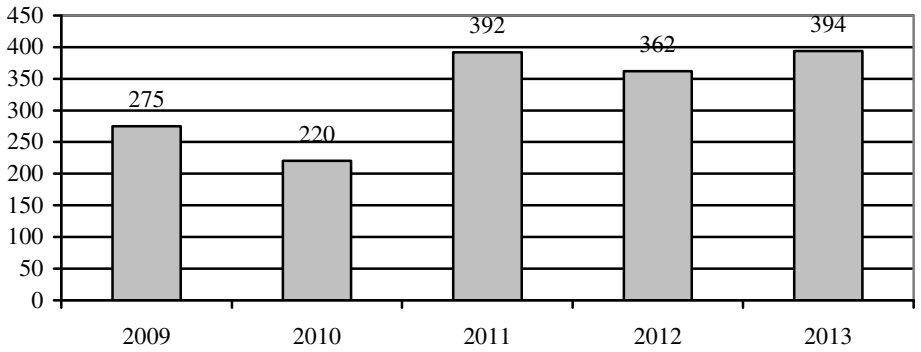

Figure 1. **Development of declared bankruptcies in Slovakia** (Markova, 2013)

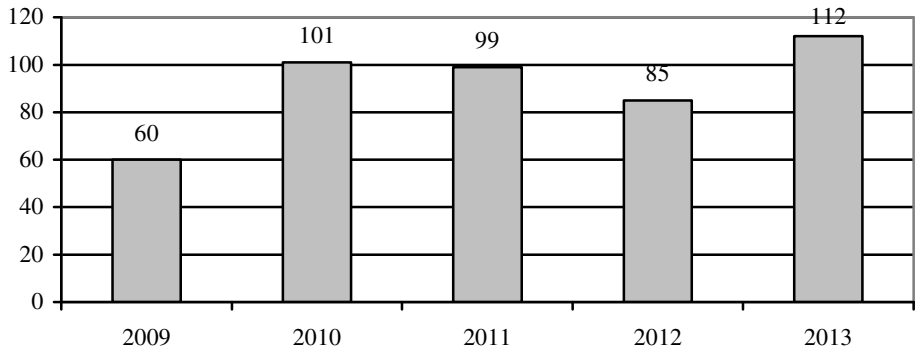

Figure 2. **The number of allowed reorganizations in Slovakia** (Markova, 2013)

Number of bankruptcies in Slovakia in 2013 was higher than in the previous year. It is proved by the analysis of CRIF – Slovak Credit Bureau. Due to problems with financial liabilities, in 2013 there were promulgated 263 bankruptcies, which is 10.04% higher than in the previous year (TASR, 2014). Process of discharging, according to CRIF – Slovak Credit Bureau, due to the poor financial situation of debtors is very long. Bankruptcy as a way of insolvency solving is used by former traders that are notable to pay their liabilities during the performance of trade, so they terminated trade and as physical entities promulgated personal bankruptcy (TASR, 2014). In 2013 there were promulgated 263 personal bankruptcies, which is 24 more than in 2012.

Consequently the reasons behind insolvency have been followed up for chosen industrial companies. Majority of companies mentioned as several reasons for insolvency therefore the number of reasons is higher than the number of searched companies. Figure 3 illustrates the reasons for companies' insolvency in reorganization, as well as what factors caused insolvency and by which measure they participated at the insolvency rising.

Most often mentioned reason of insolvency for industrial companies were the consequences of economic crisis. Although single company cannot influence economic cycles at global level, it can reduce their impacts by several steps, for example, by constructing clients' portfolio. It is very risky to have only one significant con-

sumer and to be dependable only on his demand. Company should diversify such risk and have a portfolio of consumers. If it is possible, it is secure to supply products to various markets. Last but not least it is convenient to diversify clients also from the geographical point of view.

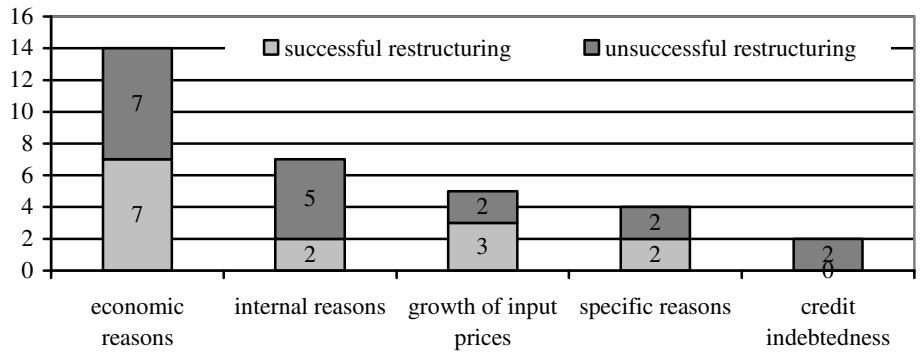

Figure 3. **The reasons behind successful and unsuccessful restructuring of companies,** *authors'*

The second reason of insolvency by frequency was internal reasons. This means mainly managerial mistakes. Companies should not underestimate the personal choices of employees at managing positions and also the quality of their education. Growth of prices for input materials has been mentioned as the third most common reason. Companies mentioned mainly the impossibility to project changes to sales prices in short time due to competition pressure at the market. This risk can be eliminated for example by sufficient profit margin that could compensate for variation of prices. Specific reasons had been mentioned as not too frequent insolvency reason as well as credit indebtedness. It is therefore necessary to plan the volume of credits properly. From the following figure it is obvious that considerate differences between successful and unsuccessful companies appear when it comes to internal reasons. As far as insolvency which happened due to external reasons, company has less chances to overcome problems than in case of internal reasons. Insolvency Law mentions several possibilities how to perform the reorganization of a company. In the analyzed companies the possibility of internal restructuring has been used. Mainly this means internal changes of operational character with the aim to secure long term effective operation of the company. Figure 4 presents the frequency of the mentioned ways of reorganization, used by chosen companies.

The following conclusions result from the mentioned values: majority of the analyzed companies have chosen a combination of several measurements. All companies used insolvency, procedures given by the law, which means restructuring of claims, when a debtor is trying to persuade creditors it is more convenient for them to obtain part of claims in the long term, rather than to have nothing or minimum from bankruptcy. Internal restructuring presented the second most used way, which is a natural step of the company with the effort to improve its economic position. Insolvency is a great test for companies on how they are able to adapt to market changes. Sale of property was the third most common way, applied by companies. The law allows also the sale of the whole company. The last way, as suggested by the law, is companies'

merger. Companies that want to merger with a company under insolvency proceeding, are waiting for finishing of these proceeding, since it is formally more easy to connect with a company, terminated by insolvency. Finding a strong partner is an advantage for a company under restructuring, on the other hand, it is also a disadvantage since it means formal termination of a company.

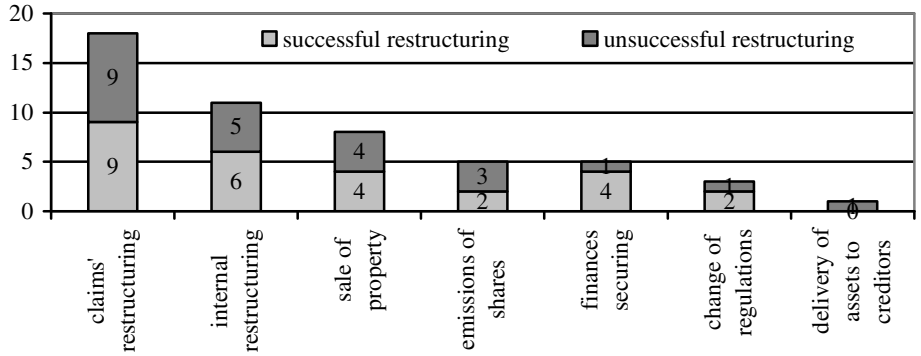

Figure 4. **Successful and unsuccessful ways of restructuring,** *authors'*

In Figure 4 we can see that significant differences between successful and unsuccessful companies were due to the insolvency solving through shares emission and reservation of financing. More successful companies were trying to find possibilities to solve their situation through changes in internal organization, on the other hand, unsuccessful companies tried to move problem in time and to solve it by further indebtedness. Comparing successful and unsuccessful reorganizations we can conclude that finding possibility of change lies in internal organization of a company (internal changes), leading to more successful reorganization. On the other hand, finding new external sources led mostly to unsuccessful reorganization.

Conclusion. Even properly operating company with stable background and a clients list can be threatened by problems, which can put in danger its very existence. Therefore, it is necessary to analyze company's financial situation and to react to changes, influencing company from inside and outwardly. Insolvency Law provides possible and legal, on how to make reorganization with the aim to be successful. Management of companies must therefore find out the most proper and most acceptable ways for insolvency solution, which could bring benefit for themselves, as well as for their creditors. Our analysis of insolvency proceedings in chosen industrial companies from two European countries allow us state that insolvency law leads to positive development in the field, but at the same time there are still reserves and space for further improvement.

Acknowledgement. *The contribution presents partial results of the research projects VEGA No 1/0176/13 "Sustainable development of region, in context of human, capital and natural sources using", VEGA No 1/0310/16 and VEGA No 1/0316/16.*

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Стаття надійшла до редакції 17.09.2015.