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# **SELECTED ASPECTS OF THE CONTRACT FOR THE TRANSFER OF A BUSINESS SHARE [1]**

### **Introduction**

Due to the fact that it is not possible to withdraw unilaterally from a limited liability company on the basis of the Slovak Commercial Code, the most common way to terminate a membership of a shareholder in a company is to transfer a business share. The Slovak Commercial Code regulates the transfer of a business share in Section 115, distinguishing between the transfer of a business share to another shareholder and the transfer of a business share to a third party.

A shareholder may transfer a business share to another shareholder with the approval of the general meeting of a company. A shareholder may transfer a business share to a third party only if admitted by a memorandum of association. However, it must be emphasized that the legal regulation is of an optional nature, so the shareholders may agree otherwise in the memorandum of association. For example, the shareholders may agree in the memorandum of association that when transferring a business share to another shareholder, the approval of the general meeting will not be required or the approval of all shareholders may be required or the transfer of a business share to another shareholder may be excluded. The shareholders may also allow the transfer of a business share to a third party in the memorandum of association or specify the conditions under which this is possible (for example, with the approval of the general meeting, the approval of all shareholders or the shareholders may require that the third party already operates in the same or similar business or has reached certain education, etc.).

However, it should be pointed out that, with the effect from 1 September 2018, a shareholder may not transfer a business share, neither to another shareholder nor to a third party, if the company is being wound up, if the company is wound up by court or by court decision, or if insolvency or restructuring procedures are declared upon the company. The aim of this measure is to prevent unfair business practices.

A business share may be transferred on the basis of the contract for the transfer of a business share. This contract represents a special contractual type

set out in the Commercial Code (Section 115 par. 4 of the Commercial Code). It applies in the case of both the consideration paid and free of charge transfer of a business share, so neither the purchase contract nor the donation contract can be used to the transfer of a business share. This contract is specific as it is a consensual obligation legal act (on its basis the transfer of a business share is realized) and a performance legal act (its effect is the transfer of a business share from the transferor to the transferee).

### **1 Essential elements of the contract for the transfer of a business share**

The Commercial Code is relatively brief as regards the essential elements of the contract for the transfer of a business share. It merely provides that the contract must be in writing and the signatures of the parties must be certified. Besides that, it only enshrines the obligation of the transferee, who is not a shareholder, to declare in the contract that the transferee accedes to the memorandum of association or articles of association, if they have been adopted [2]. In addition to the special elements stipulated in the Commercial Code, a contract for the transfer of a business share as a legal act must also comply with the general elements required for the validity of each legal act [3]. Other minimum elements of the contract for the transfer of a business share have been laid down by case law.

The contract for the transfer of a business share must include the identification of the contractual parties and the company concerned, the characteristics of the business share which is being transferred, and also the expression of will of one party (the transferor) to transfer the business share and the other party (the transferee) to accept the business share. As already stated, if a transferee is a third party, the contract for the transfer of a business share must also include a declaration that the transferee accedes to the memorandum of association or articles of association, if any. It is not excluded that such a declaration, if not enshrined directly in the contract for the transfer of a business share, be made in the form of an amendment thereto. However, such an amendment must also satisfy the requirement of a written form with certified signatures. If the declaration of accession to the memorandum of association constitutes the content of a separate instrument annexed to the contract, such instrument must be declared an integral part of the contract for the transfer of a business share. In the absence of a declaration of accession to the memorandum of association, the contract for the transfer of a business share would be null and void. The Supreme Court of the Slovak Republic stated in its decision that the declaration is a unilateral addressed legal act addressed to persons who at the time of the accession of the third party to the company are shareholders of the company. However, if the entire business share in the

company is acquired by a single person and thereby a single person becomes the sole shareholder, the possible addressee of the declaration is missing and therefore the missing declaration does not render the contract for the transfer of a business share null and void [4]. The opposite opinion was adopted by the Czech Supreme Court [5 when applying the same legal regulation, stating that the declaration of the transferee on the accession to the memorandum of association or articles of association, if any, is an obligatory element of the contract for the transfer of a business share also in a one-member company. The Czech Supreme Court argues, on the one hand, by the purpose of the Section 115 par. 4 of the Commercial Code [6], but also by the legal certainty and protection of the interests of third parties [7]. Although we cannot disagree with the Czech Supreme Court's arguments, we like the approach of the Slovak Supreme Court not to overestimate the potential formal grounds for nullity. It is obvious that when someone buys a business share in a particular company, they are also identified with the company's memorandum of association or articles of association, if any.

Case law has extended the legal elements of a contract for the transfer of a business share by a determination of whether the transfer of a business share is carried out for consideration or free of charge [8], arguing by the requirement of certainty pursuant to Section 37 par. 1 of the Civil Code. In order to make a contract for the transfer of a business share a certain legal act, it must be ascertained from its content whether the parties' intention is to conclude a contract for consideration or free of charge [9]. If the transfer of a business share is to be made free of charge, this must be expressly stated in the contract for the transfer of a business share. The mere fact that the contract does not contain the amount of the purchase price or the method of its calculation does not mean that the transfer is free of charge. If the contractual parties conclude a contract on a future contract, the subject of which is the transfer of a business share, the determination of whether the transfer of a business share is carried out for consideration or free of charge, must already be included in the contract on a future contract [10].

It also follows from the decisions of courts that if the transfer of a business share is for consideration, the purchase price or the method of its calculation must also be determined. Since the Commercial Code does not regulate the method of calculation of the purchase price of a business share, the purchase price is determined by an agreement of the parties, unless the memorandum of association stipulates otherwise. If agreed by the parties, the purchase price may be calculated as the shareholder's settlement share [11]. If there is no agreement on purchase price in the contract for the transfer of a business share,

such a contract is null and void under Section 37 par. 1 of the Civil Code due to its uncertainty and the transfer of a business share will not occur.

The legal practice also raised the question as to whether the agreement on the purchase price could be included in an annex to the contract for the transfer of a business share. The Czech Supreme Court held that this is possible, and such an agreement must be in writing, given the prescribed written form of the contract for the transfer of a business share [12]. Doubts arise with regard to the fact that when the Commercial Code prescribes certified signatures of the contractual parties on the contract for the transfer of a business share, whether it is necessary to certify the signatures on an annex to the contract for the transfer of a business share. We agree with the opinion of the Czech Supreme Court that if the agreement on the purchase price or method of its calculation is contained in the annex to the contract for the transfer of a business share, the requirements for the form of the contract for the transfer of a business share affect also the annex, as the part of the contract, and thus, not only the annex must be concluded in writing, but it must also contain certified signatures of the parties [13]. The Czech Supreme Court also dealt with the question of the moment of signature of the annex and rendered contract for the transfer of a business share null and void, if the annex was concluded later than the main contract [14]. An essential requirement for the annex is therefore that it is concluded at the latest on the date of the signature of the contract for the transfer of a business share.

## **2 Relation of the contract for the transfer of a business share to the purchase contract and to the donation contract**

As the contract for the transfer of a business share is a separate contractual type, the question arises, whether and to what extent the legal regulation of the purchase contract or the donation contract (in case of free of charge transfer of a business share) applies to it. We consider as unfortunate the following decision of the High Court in Prague, in which the court stated that the transfer of a business share for consideration is de facto purchase, therefore, in addition to the provision of Section 115 of the Commercial Code, the Sections 409 to 470 of the Commercial Code regulating the purchase contract will also apply to the contract for the transfer of a business share, and if the transfer is free of charge, in addition to the provision of Section 115 of the Commercial Code, the provisions of Sections 628 to 630 of the Civil Code regulating the donation contract will also apply to the contract for the transfer of a business share [15]. It even follows from the text of the decision that the legal regulation in question is to be applied directly, not only by analogy. In the case of a purchase contract, this reasoning could arise from the provision of Section

261 par. 6 letter a) of the Commercial Code, on the basis of which the third part of the Commercial Code, regulating commercial contractual relations, also regulates relations arising from contracts by which a business share of a shareholder is transferred. However, we are of the opinion that given the fact that the contract for the transfer of a business share is regulated as a separate contractual type in the second part of the Commercial Code within a limited liability company and the second part does not contain general provisions relating to obligations, it follows from the provision of Section 261 par. 6 letter a) that general provisions on contractual obligations (e.g. a contract on a future contract, provisions on conclusion of contracts, the discharge of contracts, etc.) will apply directly to the contract for the transfer of a business share and the provisions regulating the purchase contract will apply only by analogy to the contract for the transfer of a business share. If we were to incline to the outcome of the High Court in Prague, a problem would arise in the case of the transfer of a business share for consideration in determining the purchase price, since the provision of Section 448 par. 2 of the Commercial Code would automatically apply. Pursuant to Section 409 par. 2 in connection with Section 448 par. 2 of the Commercial Code, the contract for the transfer of a business share would not have to include the amount of the purchase price and the so-called usual price would have to be paid. However, in practice it is more or less impossible to establish a usual price for a business share. As mentioned above, both the Supreme Court of the Slovak Republic and the Supreme Court of the Czech Republic have consistently held that the determination of the purchase price is a mandatory part of the contract for the transfer of a business share.

The Czech legislator has managed to solve these problems within the recodification of private law, when it abandoned the legal regulation of the contract for the transfer of a business share as a separate contractual type (as a part of recodification the new Act on Business Corporations was also adopted [16]). Depending on the nature of the transfer of a business share, the purchase contract, the donation contract, the barter contract or any other contract will thus be used for the transfer of a business share and will be governed by the relevant provisions of the Civil Code. The legislator has thus resolved the question of whether and to what extent a contract for the transfer of a business share is to be governed by the legal regulation of individual contractual types. As regards the obligation of a third party to accede to the memorandum of association, the legislator has resolved this in Section 209 par. 1 of the Act on Business Corporations, by providing that the transferee of a business share directly accedes to the memorandum of association of the company by

acquiring the business share [17]. We consider such a solution to be correct and the Slovak legislator could also be inspired by it.

### **3 Transfer of a business share and duty of loyalty**

When transferring a business share, the duty of loyalty must also be honoured. The specificity of this duty is based not only on the absence of its legal regulation but, above all, on the fact that it has nature of the general basis on which other rights and obligations of a shareholder are to be realized and interpreted. Although the principle of loyalty is not explicitly enshrined in the Commercial Code, it can be deduced not only from the case law [18], but also from several provisions of the Commercial Code [19]. By signing a memorandum of association, shareholders of a company undertake to establish and «operate» the company for a specific purpose, and thus commit themselves to faithfulness and loyalty to the company's interests [20]. The duty of loyalty implies a passive obligation to refrain from certain acts that would jeopardize the proper functioning of the company, but also an active duty to contribute to the achievement of the common objective [21]. A shareholder cannot take actions against the company that would adversely affect its business, that is, it must not do actions against the company that are capable of damaging it, both in relation to third parties and in relation to shareholders [22].

The duty of loyalty must also be maintained when transferring a business share. It follows from the duty of loyalty that a shareholder must not unduly and unjustifiably jeopardize the company's further activity and existence. Nor the shareholder can abuse the right to transfer a business share, for example, in order to circumvent the obligations that would otherwise arise to the shareholder from the potential liquidation of a company or insolvency [23]. Breach of the duty of loyalty may be the reason for the nullity of the contract for the transfer of a business share.

### **4 Conclusion of a contract for the transfer of a business share by a proxy**

The application practice also raises the question of whether a proxy may conclude a contract for the transfer of a business share. Although the Section 115 of the Commercial Code does not expressly foresee such a possibility, we consider that it can be inferred from the general legal regulation of the power of attorney contained in Section 31 of the Civil Code. If this possibility is accepted, the question also arises as to whether the power of attorney must then contain a certified signature of the donor of power. The purpose of the requirement to certify signatures on the contract for the transfer of a business share is to increase the legal certainty of the transferee of a business share, the company, but also of third parties, that the contract is concluded by the

person owning a business share. Undoubtedly, it corresponds to this purpose that not only the signature of the proxy on the contract for the transfer of a business share is to be certified, but also the signature on the power of attorney authorizing the proxy to conclude the contract. Only such a procedure can ensure the purpose pursued by the legal regulation, since it ensures that the power of attorney is signed by the shareholder who transfers the business share. It would not be logical to require a proxy to certify its signature, unless it is clear that the person who signed the power of attorney is the person entitled to grant such authorization [24].

### **Conclusion**

The transfer of a business share as well as the contract for the transfer of a business share itself is a topic which has received considerable attention from legal theory and science, because of its undeniable importance in the practical life of limited liability companies. The legal regulation is relatively brief, causing several application problems in legal practice. Many of them have already been resolved by courts in their decision making, but many of them have become more complicated due to contradictory decisions of courts. Therefore, it would be necessary, in the context of the recodification of private law, to return and refine the legal regulation of the transfer of a business share, and hence the contract for the transfer of a business share. Meanwhile, it is important that the shareholders carefully set out provisions on the transfer of business shares in the memorandum of association to avoid the complications that may arise in the transfer of business shares.

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*2 For more details see Section 115 par. 4 of the Commercial Code.*

*3 For more details see Section 37 of the Commercial Code.*

*4 Judgment of the Supreme Court of the Slovak Republic of 29 March 2007, File no. 1 Obdo V 88/2005.*

*5 With regard to the originally identical legal regulation in the Slovak and Czech Republic, it is also possible to take into consideration the decisions of Czech courts.*

*6 The shareholder does not become a participant of the founding document by law, but by an explicit declaration in the contract for the transfer of a business share.*

*7 See the judgment of the Supreme Court of the Czech Republic of 24 April 2002, File no. 29 Odo 264/2001.*

*8 Another possibility is a barter of business shares, however, it is not frequent in practice. As the Commercial Code does not contain any special provisions*

- on the barter contract, the relevant provisions of the Civil Code (Section 611) would apply in the event of a barter of business shares.*
- 9 Judgment of the Supreme Court of the Czech Republic of 7 October 1998, File no. 1 Odon 110/97.
- 10 It follows from the resolution of the Supreme Court of the Czech Republic of 25 February 2015, File no. 29 Cdo 898/2013 that if the subject-matter of a contract on a future contract for the transfer of a business share is to be defined certainly enough, it must already be clear from the contract on a future contract whether the transfer of a business share is to be for consideration or free of charge.
- 11 Judgment of the Supreme Court of the Slovak Republic, File no. 2 Obo 102/2001.
- 12 Resolution of the Supreme Court of the Czech Republic of 5 April 2006, File no. 29 Odo 221/2005.
- 13 Resolution of the Supreme Court of the Czech Republic of 23 June 2015, File no. 29 Cdo 1685/2013.
- 14 Resolution of the Supreme Court of the Czech Republic of 7 February 2006, File no. 29 Odo 1241/2004.
- 15 Judgment of the High Court in Prague of 20 December 2005, File no. 7 Cmo 519/2005.
- 16 Act no. 90/2012 Coll. on Business Corporations and Cooperatives (Business Corporations Act).
- 17 It also resolved the question whether a declaration of accession to the memorandum of association is an essential element of a contract for the transfer of a business share, even if all the business shares in the company are acquired by one shareholder.
- 18 See, for example, the judgment of the Supreme Court of the Czech Republic of 26 June 2007, File no. 29 Odo 387/2006.
- 19 See, for example, Section 56a of the Commercial Code and Section 265 of the Commercial Code.
- 20 ČECH, P. K. (nepsaným) povinnostem společníka společnosti s ručením omezeným aneb potvrzení existence povinnosti loajality společníka v českém právu. Jurisprudence, No. 3, 2006, p. 69.
- 21 OVEČKOVÁ, O. et al. Obchodný zákonník. Veľký komentár. Bratislava : Wolters Kluwer, 2017, p. 380.
- 22 Resolution of the High Court in Prague of 1 March 2010, File no. 7 Cmo 269/2009.
- 23 Judgment of the Supreme Court of the Czech Republic of 26 June 2007, File no. 29 Odo 387/2006.

*24 Resolution of the Supreme Court of the Czech Republic of 23 May 2007,  
File no. 29 Odo 894/2006.*

**Nevolná Z. Selected aspects of the contract for the transfer of a business share**

Limited liability company is the most widespread form of a business company in the Slovak Republic. However, it is not possible to withdraw unilaterally from a limited liability company on the basis of the Slovak Commercial Code. Therefore, the most common way to terminate a membership of a shareholder in a company is by transferring a business share either to another shareholder or to a third party. A business share may be transferred on the basis of a contract for the transfer of a business share, which represents a special contractual type regulated by the Commercial Code. However, its legal regulation is very brief, which causes several application problems in the legal practice. The following contribution is dedicated to the contract for the transfer of a business share, its particulars as well as the problems that we encounter in the legal practice in connection with this contract.

**Keywords:** limited liability company, business share, contract for the transfer of a business share, essential elements of a contract.