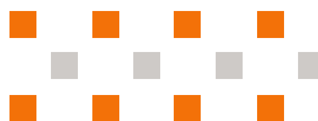

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Contributions to "other capital funds" of a Company

Trading companies often derive their financing from their shareholders' own resources. Making a capital contribution to a company is an effective way of increasing the equity capital of the company without strengthening the shareholder's position. This is significantly simpler than an increase in the registered capital. However, prior to 31 December 2013 the legal regulation of capital contributions was fairly problematic (e.g. the need for notarial certification, expert valuations for contributions in kind, etc.). There have been some substantial changes in effect since 1 January 2014 when Act no. 90/2012 Sb., the Act on Business Corporations (hereinafter the "Act on Business Corporations") came into effect.

Limited Liability Company:

Contributions to limited liability companies are governed by the provisions of Sec. 162 to 166, the Act on Business Corporations. However, the Act on Business Corporations also regulates contributions in Sec. 139 (2), laying down the obligation of shareholders to contribute to the equity capital with monetary contributions over and above the registered capital. Such an obligation is closely linked to the shareholder's interest in the company. The shareholder makes a capital contribution to the company through a contract concluded between the shareholder and the company, thus rendering it impossible to unilaterally make such a contribution. The Act is silent as to the form of the contract. Similar to previous regulation in the Commercial Code, capital contributions are divided into mandatory and voluntary contributions.

Mandatory contributions

Mandatory contributions and their maximum amounts must be laid down in the company's memorandum of association which also specifies which interests the contribution is connected with and whether the shareholders shall make the contributions in proportion to their interests or otherwise. Then, the general meeting decides by a simple majority of the shareholders present at the general meeting on the amount of the mandatory contribution unless otherwise provided in the memorandum of association or the articles of association. One recent development is that now no notarial deed or public deed is required after the resolution of the general meeting is agreed. If a shareholder fails to make a contribution, he is obliged to pay to the company late payment interest on the outstanding amount at twice the rate of late payment interest stipulated by legal regulations unless the memorandum of association provides otherwise. At the same time, proceedings to exclude the shareholder in default may be initiated in which the general meeting may exclude the shareholder from the company. Furthermore, the Act on Business Corporations, Sec. 164, now enables a shareholder to withdraw from the company if it does not agree with the obligation to make a capital contribution to the company and meets the requirements provided by law. After all these requirements are met, the shareholder's withdrawal from the company becomes effective on the last day of the month in which the written notice of withdrawal was served on the company. Similar to the previous legislation, the Act on Business Corporations includes a provision on the repayment of contributions according to which the general meeting may decide that contributions made shall be repaid to the extent that they exceed company losses.

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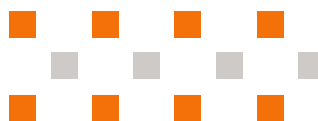

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Voluntary contribution

As before in Sec. 121 (2) the Commercial Code, the shareholder has the opportunity to make a voluntary capital contribution to the company according to the Act on Business Corporations, Sec. 163. Unlike in previous legislation, now the consent of the executive director is sufficient even if the memorandum of association or the articles of association are silent as to this issue. The Act on Business Corporations, Sec. 163 (2), now explicitly allows voluntary contributions in kind. In such cases an expert's opinion on the value of the contribution is required by law and it is now at the discretion of the executive director to choose the expert.

Joint-stock company:

The Act on Business Corporations, like the Commercial Code, does not regulate capital contributions outside the registered capital of joint-stock companies. As this is not explicitly forbidden by law, the provision relating to capital contributions to a limited liability company may be applied to a joint-stock company, like under the Commercial Code.

Accounting and tax consequences

The contribution provided is then reported in the balance sheet as “other capital funds”, which are part of the equity capital. The tax deductibility or non-deductibility of financial expenses for the purposes of corporate income tax in cases of thin capitalisation is a significant tax aspect often motivating companies to increase their equity capitals. If the company has too low an equity capital and, in contract, excessive liabilities against related parties, the interest and other financial expenses arising out of these liabilities are tax non-deductible from the amount by which such liabilities exceed four times the company's equity capital. Granting a contribution to “other capital funds” can directly affect such tax consequences.

Contributions to “other capital funds” were not subject to gift tax according to the tax administration's interpretation. The gift tax was abolished as of 1 January 2014, the taxation of gratuitous income being governed by the Income Tax Act. According to information available to us, there has been no change in this interpretation.

A contribution to “other capital funds” does not affect the amount of the shareholder's investment in the company (as neither its value nor the percentage changes); however, the acquisition value of the shareholder's interest increases according to tax and accounting rules. If the interest is sold, the contribution to “other capital funds” is, along with the investment in the registered capital, included in tax expenditures on the part of the shareholder.

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