

UNDERCAPITALIZATION OF CAPITAL COMPANIES (OOD, AD and KDA)

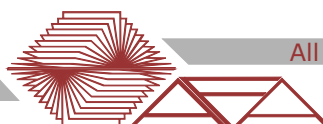
The Law on Amendment and Supplementation of the Commercial Act was published in State Gazette, issue 58. The amendments could be grouped in four main directions: amendments in the general and special provisions referring to companies; improvement of management of joint-stock companies; overall reform of the regulation of companies' reorganizations and amendments referring to bankruptcy. The amendments entered into force since 1 July 2003, with the exception of Chapter XVI on reorganizations, which shall be applicable since 1 January 2004.

In view of the considerable size of the amendments, we will publish detailed comments on the amendments of the first two groups, but before that we prepared a material, in which we emphasize on **undercapitalization of capital companies** and its consequences. Due to the imprecise regulation so far, this issue was not paid the due attention, but actually, it is revealed in a great number of companies and it leads to considerable implications for their normal functioning.

A capital company is considered to be **undercapitalized** when the net value of its property (the value of its equity; the net assets), which is the difference between the rights and liabilities of the company as per its balance sheet (Art. 247à, para. 2 of the Commercial Act), falls below the amount of the registered (authorized) capital. The undercapitalization rules are not applicable to personal companies (SD, KD) due to the lack of registered capital.

Undercapitalization preconditions positive value of the net property (the net assets), which is lower than the amount of the registered capital. Whenever this value becomes negative, the correct term for describing the property status of the company would be overindebtedness and not undercapitalization. **Therefore, distinction should be made between undercapitalization and overindebtedness.**

Undercapitalization of AD for a period longer than one year is an explicit formal ground for the compulsory winding-up of the company by request of the public prosecutor. There is no such explicit provision referring to OOD, nevertheless, both with regard to OOD and AD another risk arises: upon negative value of the equity (the net assets) **bankruptcy proceedings to be initiated against the company due to overindebtedness.** In this case, the bankruptcy proceedings shall be opened by request of the management body or the liquidator of the company within 15 days after the occurrence of the overindebtedness. Upon failure to perform this legal obligation, these persons shall be jointly and severally liable before the creditors with all their property for the damages incurred by the delay.



The competent body for overcoming the undercapitalization is the General Meeting of shareholders, which shall take a decision respectively for: decrease of the capital, reorganization or winding-up of the company. In addition to the recovery means, provided for explicitly by the law, we have set forth in the detailed comments that in some cases additional recovery measures could be applied independently or in combination.

In view of the new legal requirements, the management bodies of capital companies should constantly keep track whether the net value of the company's property falls below the amount of the registered capital, regardless whether it is a positive or negative value, **by immediately convening General Meeting of the shareholders, on which the latter to take recovery measures in due time.**

Should you wish that we provide you with the detailed comments on this issue or you have specific queries on the application of the new provisions, please do not hesitate to contact us on phone: 943 37 00, fax: 943 37 07 or e-mail: office@afa.bg.