

Dishonesty in Discharge of Debts: A Law and Economics Perspective on Czech Insolvency Law¹

JUDr. Ing. Milan VRBA, Ph.D.

milan.vrba@vse.cz

ORCID 0009-0008-5243-1925

Department of Business and European Law, Faculty of International Relations
Prague University of Economics and Business, Czech Republic

Abstract: *Honesty is deemed a central principle of the procedure leading to discharge of debts. A debtor seeking debt relief is obliged to maximise satisfaction for creditors while refraining from any actions that could harm or favour any of them. In accordance with Becker's classical theory of crime, the paper assumes that the debtor's decision to act (dis)honestly is a matter of rational choice. The debtor chooses between the certainty of honest performance of duties and the risky alternative of dishonesty. The aim of the paper is to provide an analytical framework for understanding this decision-making process and to identify how legal and institutional factors can influence it. To illustrate this, the paper applies a basic state-preference model. The model demonstrates that the debtor's ultimate decision is shaped by three key variables: (1) the potential gain from dishonesty, (2) the severity of sanctions, and (3) the likelihood of detection and punishment of dishonest conduct. Each of these variables is subsequently analysed in the context of Czech insolvency regulation, highlighting how the legal framework can influence the debtor's incentives.*

Keywords: *Discharge of Debts, Dishonest Intent, Economic Analysis of Law, Insolvency Proceedings, Personal Bankruptcy, State-Preference Model.*

JEL Classification: K22

DOI: <https://doi.org/10.62768/ADJURIS/2025/5/12>

Please cite this article as:

Vrba, Milan, „Dishonesty in Discharge of Debts: A Law and Economics Perspective on Czech Insolvency Law”, in Grmelová, Nicole & Anna Kretková (eds.), *Prospects of Law in Business*, ADJURIS – International Academic Publisher, Bucharest, Paris, Calgary, 2025, p. 147-161, <https://doi.org/10.62768/ADJURIS/2025/5/12>.

1. INTRODUCTION

Honesty is deemed a central principle of the procedure leading to dis-

¹ This paper was prepared within the framework of the IGA project of the Prague University of Economics and Business no. IGA 43/2024 “Dishonest intent in rehabilitation methods of prevention and resolution of insolvency.”

charge of debts. Under Czech law, a debtor seeking discharge is obliged to maximise satisfaction for creditors and to refrain from any conduct that could harm or favour any of them.² Other legal systems take a similar approach.³ The EU has reinforced this principle in Directive (EU) 2019/1023, which obliges Member States to make discharge of debts available to entrepreneurs, while at the same time stressing that it should be accessible only to honest debtors.⁴

This paper builds on the economic theory of crime, attributed primarily to Gary S. Becker,⁵ which views criminal behaviour as the product of rational choice.⁶ The same reasoning can be applied to any form of unlawful conduct, including dishonest behaviour in proceedings leading to discharge of debts. Accordingly, the paper treats (dis)honesty as the outcome of a rational decision: the debtor chooses between the certainty of fulfilling obligations honestly and the

² Decision of the Supreme Court of the Czech Republic of 13 August 2024, No. 29 NSČR 77/2024. ECLI:CZ:NS:2024:29.NSCR.77.2024.1. Similarly decision of the Supreme Court of the Czech Republic of 30 May 2022, No. 29 NSČR 44/2020. ECLI:CZ:NS:2022:29.NSCR.44.2020.1. See also MORAVEC, Tomáš and David MACHAČ. Poctivý záměr v oddlužení ve světle novely č. 252/2024. *Studia Iuridica Cassoviensia* [online]. 2025, 13(2), pp. 148–160 [viewed 12 October 2025]. Available from: doi.org/10.33542/SIC2025-2-08

³ See European Commission. Study on a New Approach to Business Failure and Insolvency. Comparative Legal Analysis of the Member States' Relevant Provisions and Practices [online]. 2016, pp. 294–297, 303, 320–323. [viewed 12 October 2025]. Available from: https://commission.europa.eu/document/download/ec2350c9-b7e2-4599-b9a6-ecceae7c2374_en?filename=insolvency_study_2016_final_en.pdf. For Slovak law refer to VETERNÍKOVÁ, Mária and Andrea SLEZÁKOVÁ. Annulment of Debt Relief Due to Dishonest Intention of the Debtor in the Decision-making Practice of Slovak Courts. In GRMELOVÁ, Nicole (ed.) Conference proceedings. 15th International Scientific Conference “Law in Business of Selected Member States of the European Union”. October 25–27, 2023, Prague, Czech Republic. Prague: Oeconomica Publishing House, 2023, pp. 95–106 [viewed 12 October 2025]. Available from: https://lawinbusiness.vse.cz/wp-content/uploads/Law-in-Business_2023.pdf.

⁴ Recitals 78–79, art. 23(1) of Directive (EU) 2019/1023. See RAMMESKOW, Ulrik In BRAEGELMANN, Tom, Christoph G. PAULUS, and Reinhard DAMMANN. European Preventive Restructuring: An Article-By-Article Commentary. Bloomsbury Publishing Plc, 2021, pp. 261–262. See also JOKUBAUSKAS, Remgijus. Discharge of Debts of Insolvent Entrepreneurs Under the Restructuring and Insolvency Directive. *Utrecht Journal of International and European Law* [online]. 2023, 38(1), pp. 64–75 [viewed 12 October 2025]. Available from: doi: 10.5334/ujiel.606. MACHAČ, David. Debt Discharge for Insolvent Czech Entrepreneurs under the EU Directive 2019/1023. In GRMELOVÁ, Nicole, TOMČIAK, Petr (eds.) Horizons of Law in Business and Finance. Conference proceedings. 15th International Scientific Conference “Law in Business of Selected Member States of the European Union”. October 25–27, 2023, Prague, Czech Republic. Bucarest, Paris, Calgary: Adjuris – International Academic Publisher, 2023, p. 64 [viewed 12 October 2025]. Available from: <https://adjuris.ro/books/hlbf/Horizons%20of%20Law%20in%20Business%20and%20Finance.pdf>.

⁵ BECKER, Gary S. Crime and Punishment: An Economic Approach. *Journal of Political Economy* [online]. 1968, 76(2), pp. 169–217 [viewed 12 October 2025]. Available from: doi: 10.1086/259394.

⁶ WINTER, Harold. Economics of Crime. Taylor & Francis Group, 2019, pp. 2–5. WINTER, Harold. Issues in Law and Economics. University of Chicago Press, 2017, pp. 145–147. COOTER, Robert and ULEN, Thomas. Law & Economics. 6th ed. Boston: Prentice Hall, 2012, pp. 463–467.

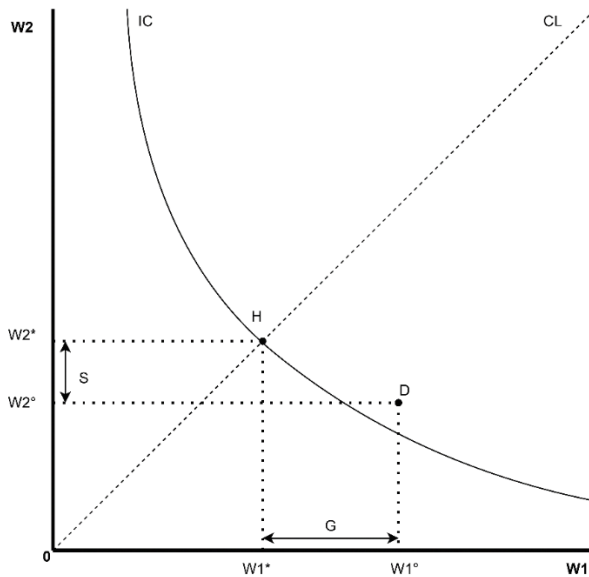
risky alternative of acting dishonestly.

The aim of the paper is to provide an analytical framework for understanding the debtor's (dis)honesty as a rational choice and to show how specific features of insolvency regulation influence their behaviour. To illustrate this decision-making process, the paper applies a state-preference model, which makes it possible to identify key variables that shape the debtor's conduct. It then analyses each of these variables in the context of Czech insolvency regulation, highlighting how legal rules and institutional practice can influence the debtor's incentives and promote honest behaviour.

2. (DIS)HONESTY IN THE STATE-PREFERENCE MODEL

The debtor's dilemma of whether to pursue dishonest intent in the process of discharge of debts can be illustrated using the state-preference model⁷ as follows:

Fig. 1. Debtor's dilemma



W1 represents the debtor's wealth if dishonest conduct remains undetected and unpunished. W2, on the other hand, represents the debtor's wealth if dishonesty is revealed and sanctioned. The diagonal axis of the quadrant is the certainty line (CL): for any point on it, $W1 = W2$, meaning that the debtor's

⁷ For detailed explanation of the state-preference model refer to e.g. GRAVELLE, Hugh, and Ray REES *Microeconomics*. 3rd ed. New York: Pearson Education, 2004, pp. 466 et seq.

wealth is the same regardless of whether dishonesty is revealed.

Each point in the graph corresponds to a unique combination of W_1 and W_2 , to which the debtor assigns a certain level of utility. Points providing the same utility form an indifference curve (IC). ICs can be thought of as contour lines on a map: points on the same curve bring the same “altitude” of utility, points below it (closer to the origin) bring lower utility and points above it bring higher utility. A rational debtor seeks to maximize utility. Therefore, combinations of W_1 and W_2 lying above a given IC are preferred, those on the IC are equally acceptable, and those below the IC are inferior.⁸

Point H represents the debtor’s situation if they act honestly. Since wealth is then certain, H lies on the CL ($W_1^* = W_2^*$). Point D represents the risky alternative of dishonesty. For the purposes of further analysis, we will presume that dishonest conduct takes the form of concealing income⁹ or property¹⁰ since these are arguably the most frequent forms of dishonest conduct in insolvency proceedings.¹¹ If concealment succeeds, the debtor’s wealth rises from W_1^* to W_1° (the difference being the gain from dishonesty – G). If concealment is detected, however, wealth falls from W_2^* to W_2° (the difference being the sanction for dishonesty – S).

The IC passing through point H forms a boundary between the “area of dishonesty” (the area above the IC where all points yield higher utility than H) and the “area of honesty” (the area below the IC where all points yield lower utility than H). If point D lies above this IC, a rational debtor will prefer dishonesty over honesty, and vice versa. The regulatory task is therefore to shift point D below the IC passing through point H, thereby making honest conduct the debtor’s preferred option.

⁸ The indifference curve is always downward sloping because, to maintain the same level of utility, a decrease in W_1 must be offset by an increase in W_2 and vice versa. The IC depicted in the graph is convex, which corresponds to a risk-averse individual. For risk-neutral decision-makers, the IC is a straight line, while the IC of risk-seeking individuals is concave. An individual’s risk attitude affects how they respond to changes in key variables. For example, a risk-averse individual will be more affected by a percentage increase in the magnitude of the sanction than by an equal percentage increase in the probability of its imposition, even though the expected sanction is the same in both cases. See WINTER, 2017, *op. cit.*, p. 114; SHAVELL, Steven. Foundations of Economic Analysis of Law. Belknap Press, 2004, pp. 480–481; BECKER, Gary S. Crime and Punishment: An Economic Approach. *Journal of Political Economy* [online]. 1968, 76(2), p. 178 [viewed 12 October 2025]. Available from: doi:10.1086/259394.

⁹ Decision of the Supreme Court of the Czech Republic of 29 June 2023, No. 29 NSČR 161/2022. ECLI:CZ:NS:2023:29.NSCR.161.2022.1.

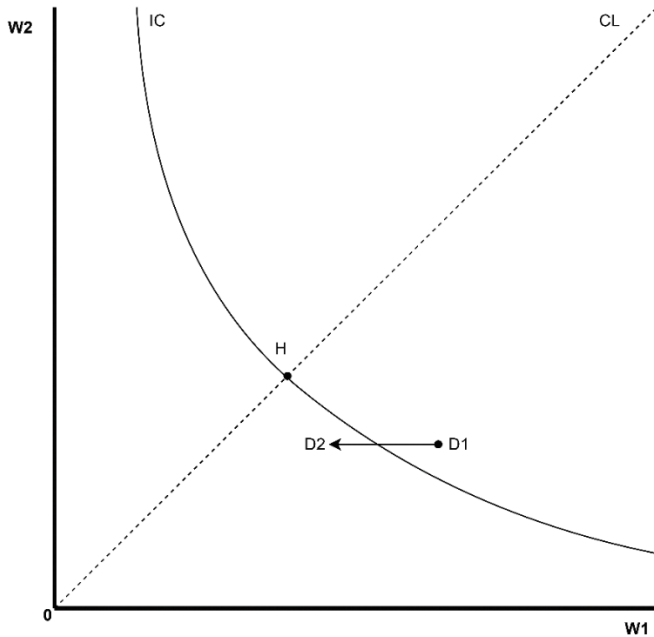
¹⁰ Decision of the Supreme Court of the Czech Republic of 17 June 2015, No. 29 NSČR 47/2013. ECLI:CZ:NS:2015:29.NSCR.47.2013.1.

¹¹ Beyond the mentioned situations, dishonesty typically includes actions aimed at prejudicing creditors even before the opening of insolvency proceedings, concealing liabilities, frustrating the satisfaction of creditors, giving preferential treatment to certain creditors, obstructing creditors or the insolvency practitioner from properly assessing the debtor’s financial situation, or deliberately diminishing the value of the debtor’s estate. See e.g. decision of the Supreme Court of the Czech Republic of 30 May 2022, No. 29 NSČR 44/2020. ECLI:CZ:NS:2022:29.NSCR.44.2020.1.

3. GAIN FROM DISHONEST CONDUCT

The debtor’s incentive to conceal property or income depends largely on the potential gain (G) that such conduct may yield. Legal rules and institutional measures can reduce or even eliminate this gain. This lowers the debtor’s wealth in the case where dishonesty goes undetected and shifts point D leftward in the graph, making dishonest conduct less attractive.

Fig. 2. Effect of reducing gains from dishonest conduct



A key way to reduce G is to make the debtor’s assets and income transparent. This can be achieved in two main ways. First, through public registers: land registers, securities registers, vehicle registers, the commercial register, and similar databases make it difficult for the debtor to conceal ownership. Where an asset is transparently recorded, the prospect of gaining from its concealment effectively disappears. Second, information can be obtained from third parties.¹² Banks, for example, are under a statutory duty to cooperate with the insolvency practitioner: they must disclose whether the debtor holds an account, provide balances, and deliver account statements. This enables the insolvency practitioner to reconstruct past transactions and neutralise attempts to divert or hide funds.

¹² Articles 43 and 44 of the CZECH REPUBLIC Act No. 182/2006 Coll., the Insolvency Act [zákon č. 182/2006 Sb., insolvenční zákon]. Hereinafter referred to as the Czech Insolvency Act or IA.

Obtaining information about debtor's assets can become more complicated if the debtor holds property abroad, most typically foreign bank accounts.¹³ Article 21(1) of Regulation (EU) 2015/848 addresses this by generally allowing the insolvency practitioner appointed by a court with jurisdiction under Article 3(1) to exercise all powers conferred by the law of the State of the opening of proceedings also in other Member States (subject to certain conditions).¹⁴ This enables the insolvency practitioner to formally request cooperation from foreign banks and other third parties just as they would domestically. In practice, however, such cross-border cooperation may be slower and less effective than domestic mechanisms, leaving still significant opportunity for gain from concealment. Moreover, Article 21 facilitates access to information but does not empower the insolvency practitioner to freeze or preserve assets located abroad. To address this limitation, proposals have been made to expressly extend the European Account Preservation Order (EAPO) procedure under Regulation (EU) 655/2014 to insolvency practitioners, who are currently not recognised as potential beneficiaries of this mechanism.¹⁵

A similar logic applies to income. Income paid by a third party (such as an employer, a pension authority, or another payer) is much harder to conceal. The payer reports the income to the insolvency practitioner and performs mandatory deductions directly,¹⁶ meaning that the debtor never gains access to the attachable portion of the income. In this sphere, G is virtually reduced to zero. By contrast, self-employed debtors must report their revenue and expenditure to the insolvency practitioner themselves so that the attachable portion of profit can be

¹³ SARRA, Janis, Stephan MADAUS, and Irit MEVORACH. Chasing Assets Abroad: Ideas for More Effective Asset Tracing and Recovery in Cross-Border Insolvency. *International Insolvency Review* [online]. 2023, 32(2), pp. 253–288 [viewed 12 October 2025]. Available from: doi:10.1002/iir.1499. In the Czech legal practice, see e.g. decision of the Supreme Court of the Czech Republic of 31 January 2024, No. 29 NSČR 58/2023. ECLI:CZ:NS:2024:29.NSCR.58.2023.1.

¹⁴ For more details see THOLE, Christoph. In BRINKMANN, Moritz (ed.). *European Insolvency Regulation: Article-by-Article Commentary*. München: Verlag C.H. Beck, 2019, pp. 211 et seq. For instance, referring to Article 18 of Regulation 1346/2000 (similar to the current Article 21 of the Regulation 2015/848), the English court held that in insolvency proceedings opened in the UK (pre-Brexit) the insolvency practitioner could require a former bookkeeper residing in Ireland to deliver up the company's accounting records. The court confirmed that an insolvency practitioner may exercise powers conferred by the law of the State of the opening of proceedings also in other Member States, provided there is a sufficient connection to the jurisdiction. Decision of the High Court of Justice (Chancery Division), England and Wales of 22 February 2010, No. [2010] EWHC 317 (Ch) [online]. In BAILII Database. British and Irish Legal Information Institute. [accessed on 2025-10-12]. Available from: <https://www.bailii.org/ew/cases/EWHC/Ch/2019/2503.html>.

¹⁵ European Commission. Study on Tracing and Recovery of Debtor's Assets by Insolvency Practitioners [online]. 2022, pp. 69-72. [viewed 12 October 2025]. Available from: https://commission.europa.eu/document/download/abd928b8-4719-4e1e-8495-77d8e9a9140b_en?filename=Final%20Report%20-%20Study%20on%20tracing%20and%20recovery%20of%20debtor%E2%80%99s%20assets%20by%20insolvency%20practitioners%20-%20March%202022.pdf.

¹⁶ Article 406(3) IA.

calculated.¹⁷ Needless to say, the insolvency practitioner's ability to verify the accuracy of such reports is very limited.

Another way of curbing gains from dishonesty is by restricting the debtor's ability to deprive creditors of value through certain legal acts. In debt-discharge proceedings, for example, refusing an inheritance or a gift requires the consent of the insolvency practitioner,¹⁸ preventing the debtor from unilaterally reducing the estate. Fraudulent transfers of property can be challenged through *actio Pauliana*,¹⁹ allowing assets wrongfully diverted from creditors' reach to be restored.

Despite these measures, G can never be completely eliminated. Besides the difficulty of verifying the income of self-employed debtors, assets not recorded in public registers (cash, movables etc.) remain inherently harder to control. The legal framework addresses this at least partially by imposing several duties: the debtor must disclose all assets in the statement of assets,²⁰ they must allow the insolvency practitioner access to all premises where such assets are located,²¹ and any person holding property belonging to the estate is obliged to notify the insolvency practitioner.²² Serious breaches of these duties may constitute a criminal offence,²³ yet in practice full compliance with these obligations cannot be entirely relied upon.

4. SANCTION FOR DISHONEST CONDUCT

The sanction for dishonest conduct in the debt-discharge process takes the form of either prolonging repayment plan,²⁴ terminating the proceedings without granting the debtor a discharge of residual debts,²⁵ or of revoking a discharge that has already been granted.²⁶ In all cases, the debtor remains liable for the outstanding debts and must continue to endure wage deductions or other forms of

¹⁷ Article 398b IA.

¹⁸ Article 412(6) IA.

¹⁹ Article 235 et seq. IA.

²⁰ Article 104(2), Article 211(1) and Article 392(1) IA.

²¹ Article 212(1) IA.

²² Article 213 IA. In this context, it is worth pointing out that the Dutch Supreme Court confirmed that an order issued by an English court (pre-Brexit) requiring a third party in the Netherlands to provide information about a bankrupt's assets falls within the scope of Article 18 of Regulation 1346/2000 (corresponding to the current Article 21 of Regulation 2015/848). Decision of the Supreme Court of the Netherlands of 18 March 2011, No. 10/00502, ECLI:NL:HR:2011:BP1404.

²³ Articles 222 and 225 of the CZECH REPUBLIC Act No. 40/2009 Coll., the Criminal Act [zákon č. 40/2009 Sb., trestní zákoník].

²⁴ Article 412b(6) IA. This sanction was introduced by one of the most recent amendments to the Czech Insolvency Act, effective from 1 October 2024. As of now, there is no relevant practical experience with its application.

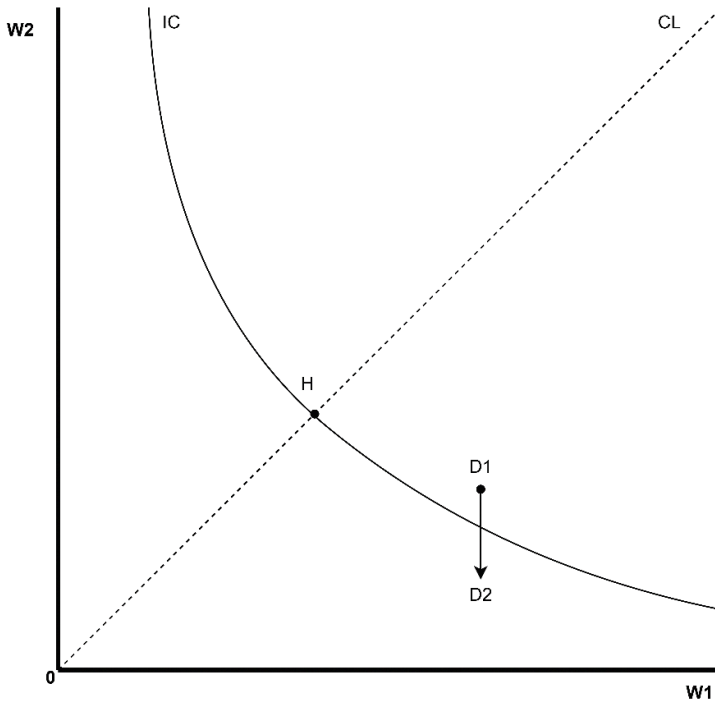
²⁵ Article 395(1), 405(1) and 418(4) IA.

²⁶ Article 417 IA.

enforcement against future income (whether in insolvency or enforcement proceedings).

From an economic perspective, the sanction (S) can be expressed as the present value of all additional deductions that the debtor must endure as a consequence of dishonest conduct. In the model, increasing S shifts point D downward, as it reduces the debtor’s wealth in the case where dishonesty is detected and punished, thereby lowering the overall utility of the dishonest option.

Fig. 3. Effect of stricter sanctions for dishonest conduct



Formally, sanction (S) can be written as:

$$S = \sum_{t=0}^T \frac{CF_t}{(1+i)^t} - \sum_{t=0}^R \frac{CF_t}{(1+i)^t}$$

where CF_t is the deduction in future period t , i is the discount rate, T is the total time until a new discharge can be granted, and R is the remaining time under the original repayment plan (of course, $R < T$). The sanction therefore equals the present value of all future deductions until a new debt relief can be granted, minus the present value of deductions the debtor would have been obliged to pay even without the extension or termination of the first process. In economic terms, S represents the present value of the net additional burden caused by the debtor’s

dishonesty.

As is evident from the above formula, the value of S is determined by four factors: the amount of the deduction in each period, the discount rate reflecting the debtor's time preference, the length of the future period during which deductions must be made, and remaining duration of the original repayment plan.

The amount of deductions (CF) is fixed by statutory rules on the attachable portion of income²⁷ and, absent legislative change, cannot be influenced in an individual case.

The discount rate (i) reflects the debtor's preference for present over future consumption. While its baseline level is influenced by prevailing market interest rates, it ultimately depends on individual time preferences. Empirical studies suggest that individuals with lower education, lower income, and lower socioeconomic status tend to apply a higher discount rate (thus strongly preferring present).²⁸ Since most debtors in debt-relief proceedings fall into these groups, they are likely to be relatively "short-sighted" when weighing immediate gains from dishonesty against the future costs of continued deductions. Even though this behavioural factor is important for understanding debtor decision-making,²⁹ it is essentially exogenous and cannot be directly influenced by legal regulation.

The key determinant of the sanction's severity is the length of the future period during which deductions continue (T). Czech insolvency law provides two alternative sanctions. In less serious cases, the court may extend the repayment plan by up to 18 months. In more serious cases, the debt-relief procedure is terminated entirely and the debtor is barred from initiating a new procedure for five years. Together with the initial phase of the new procedure (approximately half a year) and the subsequent three-year repayment plan, this means that at least 8.5 years must pass between the termination of the first procedure and the granting of a new discharge. The longer this period, the more severe the sanction.

Lastly, the perceived severity of the sanction is determined by the remaining duration of the original repayment plan (R). The net burden on the debtor depends on how much time was left in the plan at the moment of its extension or termination. The debtor would have been required to undergo deductions during this remaining period anyway, so these "baseline" deductions cannot be regarded as part of the sanction. To determine the true sanction, the present value of these baseline deductions must be subtracted from the total present value of all future

²⁷ Article 276 et seq. of the CZECH REPUBLIC Act No. 99/1963 Coll., the Civil Procedure Act [zákon č. 99/1963 Sb., občanský soudní řád].

²⁸ See e.g. HARRISON, Glenn W., Morten I. LAU, and Melonie B. WILLIAMS. Estimating Individual Discount Rates in Denmark: A Field Experiment. *American Economic Review* [online]. 2002, 92(5), pp. 1606–1617 [viewed 12 October 2025]. Available from: doi: 10.1257/000282802762024674.

²⁹ COOTER, Robert and ULEN, Thomas. Law & Economics. 6th ed. Boston: Prentice Hall, 2012, pp. 470–474. See also POSNER, Richard A. An Economic Theory of the Criminal Law. *Columbia Law Review* [online]. 1985, 85(6), pp. 1213–1214 [viewed 12 October 2025]. Available from: doi: 10.2307/1122392.

deductions. It follows that shortening the standard repayment period autonomously increases the effective severity of the sanction.³⁰

In other words, the shorter the remaining repayment period (R), the more severe the sanction becomes. In all cases of termination, the debtor cannot obtain a discharge for at least 8.5 years. If termination occurs at the very start, however, the debtor would still have been subject to deductions for the full three years of the original plan, so the effective additional burden is roughly 5.5 years of extra deductions. By contrast, if termination occurs near the end of the plan, the debtor loses almost all of the benefit of the payments already made and must wait the entire 8.5 years again. Termination late in the process is thus substantially more painful, because nearly the whole waiting period counts as a “pure” penalty.

In summary, apart from exogenous factors such as the amount of future deductions and the debtor’s discount rate, there are two key determinants of the sanction’s severity: (1) the total time that must elapse before the debtor can again obtain a discharge (T), and (2) the remaining duration of the original repayment plan at the moment of its extension or termination (R). The severity of the sanction increases not only with T, but also (perhaps less intuitively) as R becomes shorter. Together, these two factors determine how far point D is pushed downward in the model and thus how strongly dishonest conduct is disincentivised.

5. PROBABILITY OF IMPOSITION OF SANCTION FOR DISHONEST CONDUCT

Another key variable in the model is the probability of detection and punishment of dishonest conduct (P).³¹ In the state-preference diagram, P is reflected in the slope of the indifference curve: the higher the P, the flatter the IC, and vice versa.³² Put differently, as P increases, the “area of dishonesty” (the area above the IC) becomes smaller, making it more likely that point D will fall below the curve and that the debtor will choose honesty.

The first factor influencing P is the debtor’s own conduct. The debtor may actively attempt to reduce the probability of detection by engaging in concealment efforts such as hiding assets, falsifying records, or transferring property to third parties. These activities, however, are not costless: they require time, resources, and often the assistance of others. In terms of the state-preference model,

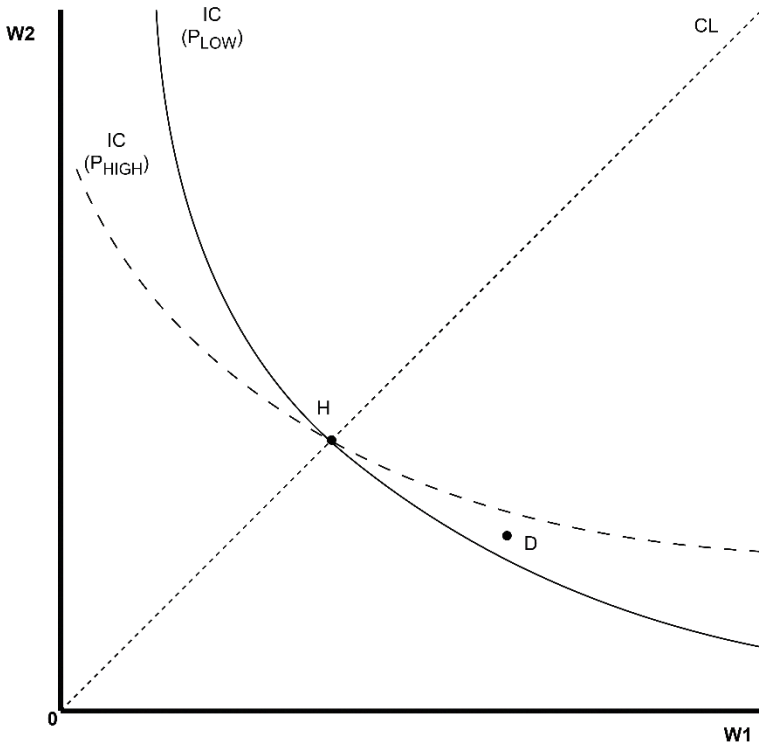
³⁰ The amendment to the Czech Insolvency Act effective as of 1 October 2024 shortened the general duration of the repayment plan from five to three years, reflecting the transposition of Directive (EU) 2019/1023. As a result, the sanction for dishonest conduct has become more stringent.

³¹ More specifically, we consider probability as it is perceived by the debtor (i.e. their subjective probability). SHAVELL, Steven. *Foundations of Economic Analysis of Law*. Belknap Press, 2004, pp. 481, 515–518.

³² The slope of IC is given by $\frac{MU(W1).(1-P)}{MU(W2).P}$ where MU stands for marginal utility of W1 or W2 and P is the probability of imposition of sanction (ranging from 0 to 1). As P approaches 1 (i.e. nears certainty), the slope of the IC approaches zero, causing the IC to become nearly horizontal.

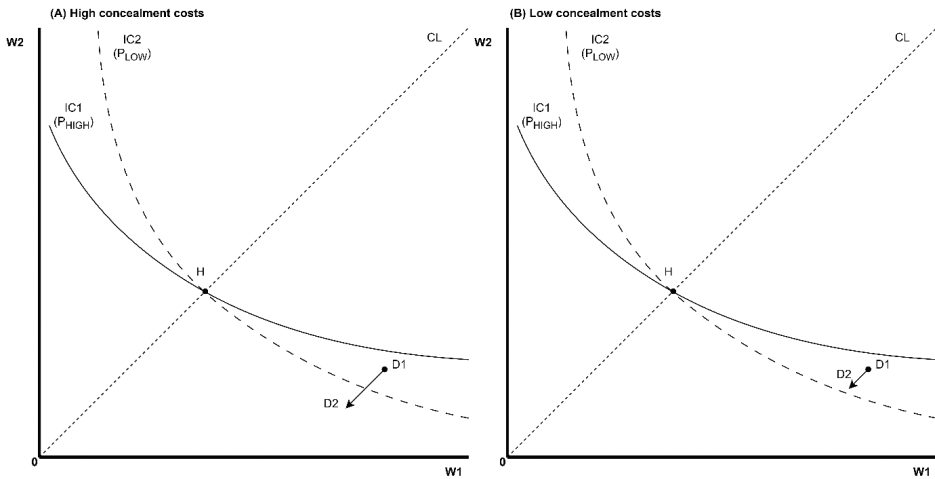
such costs shift point D downward and leftward, parallel to the certainty line, because they reduce the debtor's wealth in both states of the world. The overall effect on the debtor's choice is therefore ambiguous: while a lower P makes the indifference curve steeper and increases the relative attractiveness of dishonesty, the simultaneous reduction in wealth caused by concealment costs makes dishonesty less attractive. Which effect ultimately prevails depends on their relative magnitude.

Fig. 4. Effect of higher probability of imposition of sanction for dishonest conduct



In the following graph, point D1 lies below IC1, meaning the debtor is better off remaining honest. The debtor can, however, exert effort to conceal property or income, thereby lowering the probability of detection. This makes the indifference curve steeper, resulting in a new curve IC2. At the same time, the concealment costs shift the original point D1 to a new position D2. If these costs are sufficiently high, D2 falls below IC2 and honesty remains the preferred choice (A). If the costs are relatively low, D2 lies above IC2 and the debtor will choose dishonesty (B). Regulation should therefore aim to raise concealment costs enough to ensure that the negative wealth effect outweighs any benefit gained from reducing P.

Fig. 5. Effect of debtor’s effort to lower the probability of detection of dishonest conduct



The probability P also depends on the insolvency practitioner’s investigative effort. Effort raises P but is costly (requiring time, enquiries, analysis, coordination with third parties etc.). A key disincentive is the loss of future fees if dishonesty is established and the case is terminated. Since the insolvency practitioner is paid a flat monthly fee, this opportunity cost is the highest at the beginning of the process and declines as it nears its end. From a purely cost–benefit perspective, the insolvency practitioner’s effort (and thus P) can be expected to rise as the remaining duration of the repayment plan becomes shorter.

Regulation can adjust these incentives to raise P throughout the case. One option is to neutralise the fee disincentive by preserving part of the insolvency practitioner’s remuneration upon termination or by granting a detection bonus. Even though the Czech Insolvency Act generally empowers courts to increase the insolvency practitioner’s remuneration where they find it justified,³³ the Czech Supreme Court has held that examining the debtor’s honesty, investigating voidable transactions, and monitoring the debtor’s handling of assets fall within the insolvency practitioner’s ordinary supervisory duties and therefore do not justify any exceptional increase in remuneration.³⁴ Further measures include credible penalties for negligent performance of insolvency practitioner’s duties and lowering the cost of investigation through easier data access, cross-border cooperation, clearer procedural powers (including enforcement of third-party cooperation) etc.

The final factor influencing P is the courts’ approach. If courts adopt an

³³ Article 38(3) IA.

³⁴ Decision of the Supreme Court of the Czech Republic of 28 November 2018, No. 29 NSČR 27/2017. ECLI:CZ:NS:2018:29.NSCR.27.2017.1.

overly lenient stance, dishonesty may go unsanctioned even when detected, rendering the statutory sanction ineffective. Moreover, terminating a case for dishonest actions requires the court to state this ground explicitly and provide detailed reasoning,³⁵ which is procedurally more demanding. In practice, courts are often inclined to terminate proceedings for procedurally simpler reasons (e.g. insufficient payments) that do not require the same detailed justification. Additionally, if the debtor voluntarily moves to have the proceedings discontinued, the court does not examine any other grounds for termination (including dishonesty).³⁶ In such cases, although the process is terminated, the five-year bar on filing a new petition does not apply, allowing the debtor to initiate a new process almost immediately.

To counter this, the law lowers the “administrative cost”³⁷ of using dishonesty as a ground for termination by easing the evidentiary burden on courts: dishonesty need not be fully proven but only established to the level of a “reasonable presumption.”³⁸ This standard is less demanding than the usual civil standard of proof,³⁹ which makes it procedurally easier for courts to apply the dishonesty ground and thus enhances its preventive function.

6. CONCLUSION

A rational debtor chooses between honest fulfilment of duties and dishonest conduct by comparing the utility derived from each option. The state-preference model identifies three key variables influencing this decision: potential gain (G), the severity of the sanction (S), and the probability of its imposition (P).

Higher gains make dishonesty more attractive. Gains can be reduced by measures that prevent concealment or limit its benefits, such as automatic income deductions, public registers, and cooperation duties of banks and other institutions. To further curb gains from dishonesty, the EU legislator could consider expressly extending the European Account Preservation Order (EAPO) mechanism to insolvency practitioners.

Stronger sanction discourages dishonesty. Its severity grows with the time before a new discharge can be granted. The newly introduced sanction allowing courts to extend the repayment plan by up to 18 months should not lead to a generally more lenient approach, whereby courts replace termination of the

³⁵ Decision of the Supreme Court of the Czech Republic of 29 April 2024, No. 29 NSČR 92/2023. ECLI:CZ:NS:2024:29.NSCR.92.2023.1.

³⁶ Decision of the Supreme Court of the Czech Republic of 26 January 2023, No. 29 NSČR 43/2022. ECLI:CZ:NS:2023:29.NSCR.43.2022.1.

³⁷ Administrative costs of civil proceedings are the sum of the costs to everyone involved therein, including costs of taking evidence. COOTER, Robert and ULEN, Thomas. *Law & Economics*. 6th ed. Boston: Prentice Hall, 2012, pp. 384–386.

³⁸ Articles 395(1), 405(1) and 418(4) IA.

³⁹ Decision of the Supreme Court of the Czech Republic of 30 January 2020, No. 29 NSČR 101/2019. ECLI:CZ:NS:2020:29.NSCR.101.2019.1.

case with a mere extension of the repayment plan. Instead, it should be applied to cases of moderate misconduct that previously went unsanctioned because full termination would have been disproportionate. The sanction also becomes progressively more severe as the original plan nears its end. Notably, the recent reduction of the standard repayment period from five to three years has indirectly made sanctions for dishonest conduct stricter.

Finally, a higher probability of sanction encourages honest behaviour. Debtors may resort to various strategies to impede detection of their dishonesty, but regulation should ensure that the costs of such efforts outweigh any benefit from lowering P . The insolvency practitioner's investigative effort also increases P , yet it is constrained by resources and incentives. Besides facilitating access to relevant information (including in cross-border contexts) a key improvement could involve preserving part of the practitioner's remuneration upon termination of the case or introducing performance-based bonuses. Courts likewise influence P through their approach to dishonest debtors. Excessive leniency or reluctance to apply dishonest intent as a ground for termination of the debt-relief procedure considerably weakens deterrence and undermines the preventive function of the law.

Considered jointly, these variables show how legal rules can be designed to shift the debtor's choice in favour of honesty and thus enhance the integrity of the debt-relief process.

REFERENCES

1. BECKER, Gary S. Crime and Punishment: An Economic Approach. *Journal of Political Economy* [online]. 1968, 76(2), pp. 169–217 [viewed 12 October 2025]. Available from: doi: 10.1086/25 9394.
2. COOTER, Robert and ULEN, Thomas. Law & Economics. 6th ed. Boston: Prentice Hall, 2012.
3. GRAVELLE, Hugh, and Ray REES Microeconomics. 3rd ed. New York: Pearson Education, 2004.
4. HARRISON, Glenn W., Morten I. LAU, and Melonie B. WILLIAMS. Estimating Individual Discount Rates in Denmark: A Field Experiment. *American Economic Review* [online]. 2002, 92(5), pp. 1606–1617 [viewed 12 October 2025]. Available from: doi: 10.1257/000282802762024674.
5. JOKUBAUSKAS, Remgijus. Discharge of Debts of Insolvent Entrepreneurs Under the Restructuring and Insolvency Directive. *Utrecht Journal of International and European Law* [online]. 2023, 38(1), pp. 64–75 [viewed 12 October 2025]. Available from: doi: 10.5334/ ujiel.606.
6. MACHAČ, David. Debt Discharge for Insolvent Czech Entrepreneurs under the EU Directive 2019/1023. In GRMELOVÁ, Nicole, TOMČIAK, Petr (eds.) Horizons of Law in Business and Finance. Conference proceedings. 15th International Scientific Conference “Law in Business of Selected Member States of the European Union”. October 25–27, 2023, Prague, Czech Republic. Bucarest, Paris, Calgary: Adjuris – International Academic Publisher, 2023, p. 56–67.

- [viewed 12 October 2025]. Available from: <https://adjuris.ro/books/hlbf/Horizons%20of%20Law%20in%20Business%20and%20Finance.pdf>.
7. MORAVEC, Tomáš and David MACHAČ. Poctivý záměr v oddlužení ve světle novely č. 252/2024. *Studia Iuridica Cassoviensia* [online]. 2025, 13(2), pp. 148–160 [viewed 12 October 2025]. Available from: doi.org/10.33542/SIC2025-2-08
 8. POSNER, Richard A. An Economic Theory of the Criminal Law. *Columbia Law Review* [online]. 1985, 85(6), pp. 1213–1214 [viewed 12 October 2025]. Available from: [doi: 10.2307/1122392](https://doi.org/10.2307/1122392).
 9. RAMMESKOW, Ulrik In BRAEGELMANN, Tom, Christoph G. PAULUS, and Reinhard DAMMANN. European Preventive Restructuring: An Article-By-Article Commentary. Bloomsbury Publishing Plc, 2021, pp. 261–262.
 10. SARRA, Janis, Stephan MADAUS, and Irit MEVORACH. Chasing Assets Abroad: Ideas for More Effective Asset Tracing and Recovery in Cross-Border Insolvency. *International Insolvency Review* [online]. 2023, 32(2), pp. 253–288 [viewed 12 October 2025]. Available from: [doi:10.1002/iir.1499](https://doi.org/10.1002/iir.1499).
 11. SHAVELL, Steven. Foundations of Economic Analysis of Law. Belknap Press, 2004.
 12. THOLE, Christoph. In BRINKMANN, Moritz (ed.). European Insolvency Regulation: Article-by-Article Commentary. München: Verlag C.H. Beck, 2019.
 13. VETERNÍKOVÁ, Mária and Andrea SLEZÁKOVÁ. Annulment of Debt Relief Due to Dishonest Intention of the Debtor in the Decision-making Practice of Slovak Courts. In GRMELOVÁ, Nicole (ed.) Conference proceedings. 15th International Scientific Conference “Law in Business of Selected Member States of the European Union”. October 25–27, 2023, Prague, Czech Republic. Prague: Oeconomica Publishing House, 2023, pp. 95–106 [viewed 12 October 2025]. Available from: https://lawinbusiness.vse.cz/wp-content/uploads/Law-in-Business_2023.pdf.
 14. WINTER, Harold. Economics of Crime. Taylor & Francis Group, 2019, pp. 2–5.
 15. WINTER, Harold. Issues in Law and Economics. University of Chicago Press, 2017.