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Liberalizing Current Rules on Financial Assistance across the EU

New EU Directive changing the rules on financial assistance

- A legislative process has finished at the EU level and now it is up to the Member States to decide whether or not they will permit financial assistance under the conditions of the Directive.
- According to information provided by the Ministry of Justice, it is impossible to predict which road the Czech Parliament will take, nor the reaction of the professionals in the field. In the spring of 2007, the EU should release its study analyzing the impact of the Directive – and the Czech Republic will probably decide its course thereafter.
- Liberalizing of the current rules would simplify the steps taken in acquisition financing, as well as reduce its costs.

What is financial assistance?

- A company (target) may not provide financial resources and thereby reduce its net assets in relation to acquisition of its own shares by a third party (NewCo), *i.e.* providing loans, trusts or deposits, including security for the financial obligations arising from the acquisition of its shares by a third party.
- For example, in a buyout, the lenders will look to the target's assets for security to support NewCo's borrowings since NewCo, as the buyout vehicle, is a shell company with no assets of its own (other than the shares in the target), or guarantees by the target of NewCo's borrowings. As a result, the prohibition on financial assistance will apply in all buyout situations where shares are being acquired.

Permissible procedure subject to approval by respective Member State

- According to a proposed EU Directive, it should be open to Member States to permit financial assistance up to the amount of a company's distributable reserves, so as to cover the aggregate of the transactions made under financial assistance.
- Where the laws of a Member State permit financial assistance, they will safeguard the transactions through various means, such as:
 - Fair-market conditions;
 - Avoiding financial risk;
 - Preventing conflicts of interests.
- Corporate requirements according to the proposed EU Directive:
 - A written report from the company's Board of Directors submitted at the General Meeting, containing the reasons, risks and conditions;
 - Prior approval from the general meeting;
 - Every shareholder has a right to contest the general meeting's approval of the transaction.

Financial assistance not allowed under law

- **Second Company Law EU Directive.** Under the current regime of Article 23 of this Directive, a company may not provide financial assistance except in certain limited circumstances (financial institutions, the acquisition of shares by or for company employees).
- **Czech Commercial Code.** Although the Second Directive applies only to joint-stock companies, the Czech Commercial Code has expanded prohibition to cover limited liability companies as well (Section 1, §161e).