Central & Eastern European legal update.

Czech Republic.

Securities issuers face EU regulations shake-up

The rules regulating issuers of securities in the European Union are set to undergo a radical overhaul over the next 18 months or so.

The new Prospectus Directive, which comes into force in the middle of 2005, will set a template for the form and content of prospectuses for securities that are listed within the EU or are offered to the public within the EU. The new Transparency Directive, meanwhile, is scheduled to come into force in the second half of 2006 and will impose onerous ongoing disclosure obligations on issuers of securities that are listed (both currently and in the future) within the EU.

Unfortunately, although the basic framework of the new regulatory regime is already complete, several of the finer points are still under discussion. Even so, now that the Czech Republic is an EU member, issuers of securities in the Czech Republic should also start thinking now about the kinds of measures they will need to implement in order to comply with the new rules.

Problems for some issuers

Many issuers in the wholesale debt markets will undoubtedly feel the weight of these changes. At present, EU issuers of so-called "specialist securities" – such as Eurobonds, convertible bonds and Global Depository Receipts (GDRs) – are able to take advantage of wide-ranging exemptions for which the current EU wholesale regime allows. Prospectuses for these types of securities are currently subject to disclosure requirements that are less strict than those that apply to "retail" offers (a reflection of the "professionals only" nature of the target market), and they must comply with only very moderate ongoing disclosure requirements.
Under the new EU regime, "wholesale" exemptions will only be available for debt securities and GDRs with minimum denominations of EUR 50,000; while such exemptions will not extend to convertible bonds at all, no matter how high the denomination. Accordingly, it is likely that a significant number of investors will no longer wish to invest in debt securities and GDRs in such large denominations, once the new regulations come into effect.

Issuers of securities that do not fall within the new exemption parameters will, under the new regime, be required to:

(a) produce a lengthy, retail-style disclosure document that includes past financial statements and conforms to International Financial Reporting Standards (IFRS) or "equivalent" standards (it is not yet known which accounting standards will be treated as equivalent for these purposes);

(b) include in the offering document a summary in "non-technical" language, which may have to be translated into the official languages of the member states in which the securities are to be offered; and

(c) comply with new, stricter ongoing disclosure requirements, which will include the filing of:

(i) annual and semi-annual financial statements that have been produced in accordance with IFRS or "equivalent" standards;

(ii) (in the case of issuers of shares) quarterly financial information; and

(iii) an annual list of any information that has been made available to investors elsewhere in the world.

Other issues

In point of fact, many issuers that are incorporated in the EU would shortly have been required to produce IFRS financial statements in any case, under new EU regulations that take effect in 2005. However, it could be that non EU-based issuers with securities listed in the EU who do not produce their financial statements in accordance with IFRS will have to restate their accounts in the approved form, solely for the purposes of complying with these EU disclosure requirements.

Liability for a prospectus could also be something of a grey area. For example, the Prospectus Directive preserves each member state’s ability to maintain national rules on liability for information contained in prospectuses, yet it also appears to require the Europe-wide publication of prospectuses. (The current regime, by contrast, only requires publication in the state where the offer or listing is being made.) This may well trigger liability regimes across the whole of the EU. Should this prove to be the case, then it will be
even more important for issuers to consider their potential liability in each separate EU member state.

**Be prepared**

Clearly, the new regime will have a substantial impact on the obligations and position of securities issuers in the EU. Even though the full extent of that impact so far remains unclear (since regulators are still hammering out several important details), it makes sense for issuers of securities within the EU – including issuers in the Czech Republic – to be aware, at least, of the challenges that lie on the horizon.

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**Hungary.**

Implementation of the Parent-Subsidiary Directive in Hungary

*The implementation of the Parent-Subsidiary Directive and the consequential exemption of dividends from withholding taxes is a landmark achievement in the Hungarian corporate tax system. Together with the other favourable features of the Hungarian tax system it makes Hungary a very attractive jurisdiction for international tax planning.*


Pursuant to the Directive, the economic double taxation of dividends (i.e. the phenomenon that distributed profits are taxed twice: once at subsidiary level as corporate income tax and once at shareholder level as dividend tax) is eliminated as follows:
(i) the country of the subsidiary is prohibited from levying withholding tax on the dividend it pays to the parent company; and

(ii) the country of the parent company must either exempt the dividend received by the parent company (exemption method) or must allow the parent company to credit the corporate tax paid by the subsidiary against the tax payable by it on the dividend received (indirect credit method).

The Directive sets certain further conditions on the application of the Directive, most notably that the parent company must have a minimum holding of 25% in the capital of the subsidiary for an uninterrupted period of two years. Member States may, however, set a lower threshold and a shorter holding period as a precondition for the application of the Directive.

Since Hungary became a member of the EU on 1 May 2004, it had to implement the Directive into its corporate tax system. Hungary has traditionally exempted dividends received by parent companies from corporate taxes (regardless of whether the dividend is paid by domestic or foreign subsidiaries) thus no change to the corporate tax law was necessary with regard to point (ii) above. On the other hand, the exemption of dividends from withholding taxes (point (i) above) became a new feature of the Hungarian tax system.

Hungary applies a 20% withholding tax on dividends paid by Hungarian subsidiaries to foreign parents. This dividend is lowered by any double tax convention in force between Hungary and the country of the parent company. None of the double tax conventions Hungary concluded with the EU Member States have, however, completely eliminated Hungarian withholding taxation on dividends. The implementation of the Directive in Hungary was, therefore, a big achievement indeed: dividends that were subject to Hungarian withholding tax before 1 May 2004 can now flow tax-free from Hungarian subsidiaries to their EU resident parents.

For the application of the exemption Hungary implemented the Directive in such a way that the minimum conditions set forth in the Directive apply: the parent must have a minimum holding of 25% in the capital of the subsidiary for an uninterrupted period of 2 years. In line with the decision of the European Court of Justice in the Denkavit case (C-283/94, C-291/94 and C-292/94) if the two-year condition has not been fulfilled at the time of the dividend distribution, the exemption still be applied. The condition for this is that a third person undertakes a guarantee for the payment of the eventual tax liability.

The Ministry of Finance and the tax authority have recently issued guidelines on the interpretation of the conditions of the exemption. The key elements of the guidance may be summarised as follows:

– it has been confirmed that the exemption applies to all dividends paid by Hungarian subsidiaries after 1 May 2004, regardless of whether the dividend is paid from profits accumulated before or after 1 May 2004.
Consequently, Hungarian subsidiaries may now distribute to their EU resident parents all earnings accumulated in the previous years without withholding tax obligations;

- the guarantee (necessary for the tax-fee payment of dividend before the passing of the two-year period) must be provided by a party which is financially reliable and will be capable of paying the eventual tax liability. The guarantee must be provided in the form of an agreement with the tax authority. The tax authority has the right, therefore, to refuse the guarantee if it does not find the guarantor sufficiently reliable;

- the need to provide the guarantee does not apply if the dividend is paid in kind (rather than in cash). If a Hungarian subsidiary pays dividends in-kind to its EU resident parent within the two-year holding period then the subsidiary will be obliged to pay the withholding tax. This tax will be reclaimable by the parent after the two-year requirement has been fulfilled.

These guidances set a clear framework for the application of the Directive in Hungary. We are convinced that the exemption on dividend withholding taxes and the clarity of the underlying rules will have a significant influence on the structuring of investments in Hungary. While it will primarily attract investments from other EU Member States, it can be of use in respect of investments originating from non-EU Member States, provided that the investment is structured through an appropriate EU holding location. The abolition of the dividend withholding taxes must be viewed in conjunction with other favourable features of the Hungarian tax system, e.g. the abolition of withholding taxes on interest and royalties paid to foreign entities (effective from 1 January 2004) and the well established practice of the Ministry of Finance to make clear binding rulings which give tax planners the comfort of certainty. These features have, undoubtedly, made Hungary a very attractive jurisdiction for international tax planning.

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Limitations of the Act on Polish language

As a consequence of Poland joining the EU the Act on the Polish language has been amended. Business entities now have more freedom in choosing the language for their transactions. Use of the Polish language is generally no longer required, subject to certain exceptions (where one of the parties is a public entity or a consumer or in transactions relating to labour law).

Introduction (how was it before Poland joined the EU?)

Before 1 of May 2004 the Act on the Polish Language\(^1\) (the “Act”), required that all agreements had a Polish version if the transaction was to be performed in Poland. This applied even if only one of the parties to the transaction was a Polish entity.

Now Poland has joined the EU there are fewer ‘Polish language’ obligations

came into force on 1st May 2004.

As from this date, the obligation to use Polish language in legal documents has been limited to:

– contacts with public entities;
– relations with consumers;
– transactions relating to labour law.

Contracts with Public Entities

According to the Act, in any agreements with public entities (the Act: “entities performing public tasks”) Polish is the official language. This means that any documentation submitted to public entities and any transactions with these entities, has to be prepared in Polish. Consequently, one cannot expect public entities to issue any documentation in a foreign language.

The definition of a public entity is very wide and includes every constitutional and local authority of public administration. It does not however include territorial self-government units unless they are performing public tasks.

Transactions concluded with consumers

The use of Polish language in agreements with consumers is required when:

\(^1\) dated 7 October 1999 (Dz. U. 1999 No 90, item 999).
– the consumer is domiciled in Poland, and
– the agreement will be exercised in Poland.

Transactions relating to labour law
In the same way as in cases relating to consumers, the Act requires the use of Polish language in transactions relating to labour law (the Act: “in execution of provisions of labour law”), if:
– the employee is domiciled in Poland, and
– the agreement will be exercised in Poland.

Obligation to use the Polish language - what does it mean in practice?
The obligation to use Polish language, in practice, means that any agreement or documentation which can be classified into one of the categories described above has to have a Polish version.
If there are two language versions of the agreement, the Polish language version will be the prevailing one, unless the parties have expressly decided to the contrary.
It should be noted that the obligation to use Polish language does not apply to transactions solely between entrepreneurs. Therefore, an agreement between two professional business entities does not need to have a Polish version.
The obligation to use Polish language also includes, among others: naming of goods and services, offers, guarantees, invoices, bills, manuals, product information, advertisements, etc. This obligation does apply, e.g. to: proper names, commonly understandable graphic forms, trade marks, foreign-language computer programs (except for their descriptions and instruction manuals), customarily used technical terminology, rules incorporated in their original language pursuant to the standardisation provisions.

Other Exceptions to the Act
Employment contracts or any other documents required under the Labour Code as well as agreements concluded with consumers, can be prepared in a foreign language only:
– at the request of an employee or consumer, who is a citizen of one of the European Union member states (other than Poland), and who has been notified of the right to an agreement in Polish, and
– at the request of an employee who is a foreigner if the employer has their seat in one of the European Union member states.
What if the obligation has not been observed?

In cases where the obligation to use Polish language has not been observed, the authorities may impose a fine. Moreover, in the case of any dispute before the court, a foreign language version cannot constitute evidence of the execution of an agreement. The evidence of witnesses and evidence in the form of statements of the parties to the agreement, is also not admissible, unless all parties to the agreement consent to it, a customer requests it in a dispute with an entrepreneur, or if the fact of executing that agreement is made probable in writing in a document other than the agreement itself. Also, contracts for the provision of services by electronic means\(^2\) concluded with a service provider, with its seat located outside Poland, may constitute evidence of execution of the agreement, even when they are only in a foreign language version.

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Romania.

New capital markets legal framework in Romania

As part of the EU accession effort, Romania recently enacted a new Law to regulate its capital markets – law no. 297 of 2004, in force since 28 July 2004 (the “New Law”). The New Law unifies the existing capital markets legislation which had previously been scattered in four separate acts and introduces significant changes meant to ensure the consistency of the Romanian legislation with EU Directives regarding capital markets. Due to the broad scope of the changes introduced by the New Law, in this article we are only presenting a summary of the more important provisions.

\(^2\) within the meaning of the “Act on provision of services in electronic form” dated 18.07.2002 (Dz.U. Nr 144, poz. 1204).
Public offers

1.1 General

As a rule, public offers for sale or purchase of securities of any kind require the publication of a prospectus which has to be approved in advance by the National Securities Commission (the “NSC”). A public offer must be effected through an authorised intermediary. The provisions regarding the prospectus are in line with the “Prospectus Directive” and the New Law contemplates the possibility of cross-border offers. However, secondary legislation is yet to be issued by the NSC.

Publicity for any offering (including the form and contents of any advertising materials) is subject to approval by the NSC.

In connection with public offerings, book-building activities are allowed, subject to the provisions of future NSC regulations.

1.2 Private placements

By exception from the above-mentioned obligation, the New Law allows for certain sale offers to be performed without the need to publish a prospectus or obtain any other NSC approval:

(i) when the offer is addressed to qualified investors (defined in a similar manner as in Directive 2003/71/EC) only; or

(ii) when the offer is addressed to less than 100 individuals or legal entities, other than qualified investors; or

(iii) when the total value of the offer, the issue price for the securities and the minimum value of the subscriptions per investor are at least equal to the ones established through (as yet unissued) NSC regulations.

Any resale of securities acquired through such operations shall be considered a separate transaction and may or may not constitute a public offer, according to the general rules.

For the first time Romanian legislation now provides for certain “safe-harbours” designed to allow the placement of securities with professional and/or high net worth investors.

1.3 Take-overs

Take-over bids are offers addressed to all (other) shareholders for the entirety of their participations, where the bidder intends to acquire the shares corresponding to more than 33% of the voting rights in the target Company. The 33% threshold for mandatory takeover bids was reduced from 50% plus one share in order to comply with the EU position. However, investors that already owned more than 33% at the time of the entry into force of the New Law do not have an obligation to promote a take-over bid unless they intend to acquire more than 50% of the voting rights of the relevant issuer.
Before a takeover offer can be sent to the target company and made public it must be approved by the NSC. For the duration of the offer, the target company is subject to a special, restrictive regime.

A competing takeover offer may be launched as long as it offers a price which is at least 5% over the price of the initial offer. The NSC will fix a common closing date for all competing offers.

The New Law does not expressly envisage the possibility of effecting a public exchange offer (i.e. a tender offer in which the consideration mainly consists of the shares of the bidder). Arguably one could be promoted using the rules for the public takeover offer although difficulties will be encountered due to the formalities required for the issuance of new shares by the bidder, which are not suitable for a tender offer. The same considerations apply for a mixed offer. In any event, such offers would have to be approved by the NSC.

1.4 Squeeze-out and sell-out

An offeror which owns more than 95% of the share capital of a company or has acquired as a result of a public offer to purchase all the shares of all the shareholders more than 90% of the shares it was seeking to acquire, has the right to request the minority shareholders to sell their shares to the offeror at a fair price. The price stipulated in a takeover bid in which the offeror acquired more than 90% of the targeted shares is deemed as a fair price; if this criterion is not applicable, the fair price is determined by an independent expert. The precise mechanism of the squeeze-out will be determined through future NSC regulations.

Minority shareholders can request the majority shareholder (i.e. a person meeting the above criteria) to buy their shares at a fair price.

The ability of the majority shareholder to “squeeze out” the minority is a new concept in Romanian legislation. A legal debate still continues as to whether a provision that appears to oblige someone to surrender their property is constitutional.

2 Changes to the legal regime of listed companies

2.1 Change of concept - "listing" versus "public trading"

Previously all publicly-traded companies were required to list on a regulated market and were subject to a special legal regime. The New Law eliminates the concept of publicly-traded companies and makes listing conditional upon fulfilling minimal criteria in line with the requirements of the EU Directives, including an the anticipated capitalisation of at least € 1,000,000. Only listed companies are now subject to the special obligations set out below. Pending further NSC regulations being issued, it is as yet unclear what legal regime will
be applicable to the many companies that have become publicly traded as a result of the mass privatisation process but that do not satisfy the criteria required for an official listing.

2.2 Transfer of shares

All registry operations are to be made by the Central Depository and transfer of ownership of non-derivative financial instruments occurs upon clearing (also made by the Central Depository) on the basis of delivery versus payment. The Central Depository is an entity yet to be created – it is expected to be created by some kind of merger of the existing clearing systems and independent registry companies. Until the Central Depository is created, the NSC has decreed that all share transfers will continue to happen in the manner provided under the old law.

2.3 Security interest on securities

Establishment of a security interest over securities is made by registration in the securities owner’s account of the securities amount, guaranteed obligation and creditor identity. Publicity and priority are ensured by registration with the Central Depository starting with the date of registration.

2.4 Mergers of listed and unlisted companies

Under the New Law a merger between a publicly-traded company and a privately-held company will no longer always result in a publicly-held company. The resulting company will be listed or unlisted depending on the listed or unlisted nature of the absorbing entity or the decision of the general meetings of the shareholders of the relevant companies approving the merger in case of a merger creating a new entity.

2.5 Share capital increases

One major change in the legal regime of listed companies is the disappearance of the rule requiring the mandatory update of the value of immobilized capital before any new contributions. The regime of contributions in kind has also been liberalised, although the New Law sets out that such contributions must consist of “high performance assets”. Time will show how broadly interpreted this phrase will be.

A shareholders’ preference right for share capital increases with contributions in cash can be removed by an Extraordinary General Assembly (with a quorum of at least three quarters of the shareholders and 75% majority vote). The provisions relating to the quorum make it virtually impossible to disapply pre-emption rights, as it is hard to get more than three quarters of the total number of shareholders of a listed company to attend a shareholders’ meeting.

2.6 Exceptional powers of the Board of Directors
The Board of Directors can be authorised through the Constitutive Act or by the General Assembly of Shareholders to increase share capital up to an approved maximum ceiling. However, the Board of Directors will be the body deciding whether or not to perform such share capital increase.

The decisions of the Board of Directors in the exercise of the powers delegated by the General Assembly of Shareholders are subject to the same requirements, and may be contested in court on the same basis, as the decisions of the General Assembly of Shareholders.

2.7 Audit

Auditors can be required to draw up a financial audit report, as well as additional reports (on the basis of information given by the directors) at the request of shareholders representing at least 5% of the voting rights.

The auditors must report to the NSC any activity contrary to the provisions of the law or other activities with material impact, such report not being considered a breach of confidentiality. The NSC shall not disclose such information to third parties, except for aspects concerning criminal law which may be disclosed to the proper authorities.

3 Expected restructuring of the Romanian capital market

3.1 Merger of the stock-markets

Romania currently has two important securities markets: the Bucharest Stock Exchange ("BSE") and the Electronic Securities Exchange ("Rasdaq"). It is expected that Rasdaq will be merged into the BSE in the near future and most companies traded on Rasdaq shall be listed on the lower tiers of BSE. However, certain companies are expected to fail to meet the listing criteria – clarification of their legal regime is pending.

3.2 Regulated markets regime

The setting-up and operation of the regulated markets follow the principles set forth in the EU Directives. The regulated market concept as set out in the New Law is more loosely defined and more flexible than the previous regulations. Regulated markets include both stock-exchanges and commodities exchanges, but the NSC has to issue a series of regulations detailing the legal regimes of such markets. Similarly, further NSC regulations must implement rules relating to the operation of alternative trading systems, which are in principle allowed under the New Law.

3.3 Establishment of the Central Depository

The New Law provides for the establishment of a Central Depository, a joint stock company with the following key functions:
– depositing of securities;
– clearing and settlement of securities transactions; and
– maintenance of the Register of shareholders of listed companies

One important consequence of immediate practical impact will be the replacement of the existing registry companies by the Central Depository for the registry operations of listed companies. Similarly, the Bucharest Stock Exchange shall have to give up its in-house clearing and registry function. Moreover, securities traded through an alternate trading system will also be registered with the Central Depository. Only shares or bonds which are not traded will not be registered with the Central Depository.

T-bills will have a special depository operating pursuant to different rules.

4 Passsporting issues

Under the New Law, certain financial investment services are regulated activities which can be undertaken only by entities authorised by the NSC or the National Bank of Romania. These regulated activities coincide broadly with those set out in EU Directives, which raises the issue of whether EU based intermediaries may provide financial services based on the “passport” regime.

While the New Law is in line with the European directives and includes provisions which allow financial intermediaries from member countries to undertake regulated investment activities in Romania, the moment of entry into force of these particular provisions of the New Law has been postponed until Romania’s entry into the European Union – which is not expected to be earlier than 1 January 2007. Furthermore, the provisions of the law are quite general and are due to be detailed by regulations which are yet to be issued by the NSC.

Under these circumstances, we can only conclude that an effective “passporting” regime is not yet available in order to allow foreign financial services intermediaries to provide services directly in Romania.

5 Conclusion

The New Law goes a long way towards integrating the Romanian legal framework regarding listed companies with European directives and includes numerous interesting changes which bring it closer to modern capital markets regimes. At the same time, several important and sensitive issues are still poorly regulated and, unfortunately, a large part of the required rules
are left for the NSC to decide in secondary legislation. This makes many provisions of New Law hard to interpret or apply. Based on past experience the secondary legislation could be a long time coming.

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Russia.

Russian Tax Authorities start to actively combat aggressive tax schemes

Recent tax reforms in Russia left taxpayers with a Tax Code which provides them with clear tax regulation and instruments to protect their rights. At the same time, the Tax Code does not contain effective mechanisms enabling the tax authorities to combat sophisticated tax schemes. As a result, many aggressive tax schemes were developed and the tax authorities failed to combat them due to numerous formalities limiting the rights of the officials. The courts, which historically reviewed only the form rather than the substance in tax disputes, normally supported taxpayers and not the tax authorities. Attempts by the authorities to tighten tax rules (e.g. by amending transfer pricing regulations and VAT payment mechanics) were not successful. Although tax schemes were not accepted by all taxpayers, in certain sectors tax schemes have been typical for some time. But growing tax losses for the state resulting from the application of tax schemes has forced the Government to change the situation. This article examines a number of recent amendments to the tax legislation.

Changes in the tax regulation

With effect from 1 January 2004 the system of Investment Agreements between Russian regional and local authorities and taxpayers have come to an end. These agreements provided substantial reductions in tax payments if a taxpayer made investments (which could have been nominal) in a particular region. The system was the basis for so-called Russian off-shore
or low-tax companies. Unfortunately, some companies which used Investment Agreements to make real investments, became victims of the new regulation.

In 2004 the State Duma also approved changes in the tax law that increased export duties and mineral extraction tax for oil companies. A number of technical changes were made to combat tax schemes.

**A bone fide taxpayer: court concepts**

The Russian Constitutional Court (the highest court in Russia) has developed a concept of a bona fide taxpayer (when reviewing a tax dispute relating to the transfer of taxes from taxpayers bank accounts to tax authorities). The concept enables the tax authorities to collect tax from non-bona fide taxpayers which try to pay taxes through economically (but not legally) bankrupt banks. Such a structure used to work because under the Tax Code a tax is treated as paid at the moment of receiving a tax payment instruction by the bank. Although no clear concept of a bona fide tax payer has been developed, the tax authorities have started to use the concept to combat tax schemes, sometimes successfully.

**Yukos case**

Russian oil giant Yukos and its numerous subsidiaries became a target for police and tax authorities, which accused the group of illegal tax planning, mostly based on concentrating income in trading companies registered in low-tax regions. The tax office’s $3 billion tax claim against the group was dramatically supported by the court and there is information in the press that new similar claims are pending by the authorities at the moment.

This shocked many tax professionals, who had not believed that the form of the transactions could be ignored for tax purposes by the court. Although it is likely that the case will be reviewed by the higher courts, both taxpayers and tax advisers are considering where the state is drawing the line between legal and illegal tax optimisation in light of the Yukos case. The answer will affect thousands of domestic and foreign taxpayers with respect to their past and current business.

This is an indication that Russian law is at the moment in a period of intensive development of anti-abuse provisions and concepts, which should be considered carefully in any current project related to Russia.

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New EU Directive on cross-border mergers of companies expected soon

The European Union shall soon adopt a new company law directive, which will facilitate cross-border mergers of commercial companies between different Member States. The Directive on cross-border mergers of companies with share capital (the “Directive”) is intended to cover all companies with share capital which are viewed as having legal personality and separate assets that serve to cover the companies’ debts. The Directive will open a new array of corporate and tax structuring options, many of which will only become apparent over time as more and more companies elect to undertake cross-border mergers. This article highlights some of these issue opportunities.

Reducing the cost of cross-border mergers

Three cross-border merger transfers are covered by the Directive: transfer of all assets and liabilities to an acquiring company, to a new company, or to the company holding all the securities or shares representing the capital of the merging entity. The following simplified procedures should allow companies to carry out a cross-border merger with reduced legal and other costs compared to current rules:

- the merging companies will have to draw up draft terms of the merger and will have to have them approved by the general meeting of each company;
- draft terms and completion of the merger will have to be publicized in the appropriate public register;
- legality of the procedure will have to be certified by the competent authorities;
- a single expert report will be permitted.

In case of a merger between companies where the acquiring company already holds all or most of the shares or other securities of the company being acquired that confer the right to vote at the latter company’s general meetings, the number of steps have been reduced in order to simplify the procedure.

The Directive specifies the law of the Member State which governs the formalities, taking effect and publication of completion of the merger. Under applicable national law, protection will be offered to the interests of creditors, debenture holders, holders of securities other than shares, minority...
shareholders and employees, as regards rights other than those related to participation in the company, vis-à-vis each of the merging companies. Companies created by cross-border merger operations will remain subject to the compulsory employees’ participation rules applicable in the relevant Member State.

After the date on which a cross-border merger takes effect it will no longer be possible for the merging entities to unwind the merger, however, the Directive will be without prejudice to the application of competition law rules on control of concentrations between undertakings.

Tax – will mergers open new planning opportunities?

From a tax perspective, the Directive opens up a wide variety of potentially advantageous corporate and tax planning possibilities which will need to be carefully examined in each particular case. Cross-border mergers (although defined more widely than in the Directive) and certain tax implications of such mergers within the EU are already regulated by the Merger Directive (No. 90/434/EEC). In principle, the Merger Directive introduced common taxation of mergers in situations, where national legislation allowed for such mergers before the Directive described in this article was prepared.

Whilst the Merger Directive, deals with some issues such as the value at which assets are transferred in a cross-border merger, it does not deal with a number of other tax issues that may arise in connection with cross-border mergers, which have the potential to create either opportunities or pitfalls for businesses. Some of the questions which may arise include:

- What happens with tax losses accumulated in one Member State by the wound-up company?
- How will the shareholders of the wound-up company be affected, once they receive shares in a company located in a different Member State (will other withholding tax rules on dividends apply)?
- Will the merger enable the merged company to use another (more beneficial) tax regime – e.g. tax rates, depreciation rules, thin capitalisation rules?

For example, with respect to tax losses, Slovak legislation allows tax losses accumulated by the merged company to be carried forward by its legal successor. Although it is not yet clear how the legislation would treat cross-border mergers specifically, if the current rules remain in force, the possibility to merge profitable and loss-making businesses in various countries could turn out to be a powerful tax planning tool.

Similar attention should be paid to all issues raised in this article and other questions that companies may face in practice when deciding on cross-border mergers. There will certainly be many questions but also potentially
advantageous opportunities in the process, which companies should examine with their legal and other advisors.

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Feedback

Is there anything you would change in this legal update in relation to its format or its content? Are there any issues you would like to see discussed in future editions of Central & Eastern European Legal Update, or have any questions of general interest that could be answered in future editions? Please let us know at CEELegalUpdate@linklaters.com e-mail address.

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