

Corporate law Legal Alert

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CROSS-BORDER LEGAL MERGERS

Late 2005, the European Commission adopted the European Directive on Cross-Border Mergers of Limited Liability Companies (Directive 2005/56/EC, the "Directive"). The Directive deals with cross-border legal mergers between limited liability companies from different member states of the European Union. The Directive lays down a framework of rules facilitating cross-border mergers between companies in the European Union and requires the removal of obstacles in national laws to such mergers. The Directive does not apply to mergers between companies from only one member state, but only to mergers involving at least two companies from different member states. The Directive allowed the member states until 15 December, 2007 to incorporate the Directive to national legislation. Although the Dutch government did not meet this deadline, it did prepare a legislative proposal for the implementation of the Directive into Dutch law.

The Legal Merger

Merger is the juridical (*legal*) act of two or more legal persons, whereby one acquires the property, rights and interests and the liabilities of the other by universal succession of title or whereby a new legal person, formed or incorporated by them jointly by such juridical act, acquires their property, rights and interests and the liabilities by universal title. As a result of the merger the merging legal persons shall, save for the transferee legal person, cease to exist. The members or the shareholders of the legal persons ceasing to exist shall, as a result of the merger, generally become members or shareholders of the transferee legal person.

The Directive sets down several requirements which must be met before a cross-border merger can be completed. In particular, there are safeguards for shareholders of the merging companies; they must approve the merger and must have the right to inspect a number of documents, including the draft terms of the merger and a report

prepared by an independent expert about the merger and its consequences. In certain circumstances, the companies involved must also ensure that there are adequate employee participation arrangements. The merger must be approved by national authorities of the jurisdictions involved designated for this purpose, and must be published in the relevant national registers of companies of those jurisdictions.

Dutch Legislative Proposal

The Dutch legislative proposal applies to Dutch private limited liability companies (*besloten vennootschap*), public companies with limited liability (*naamloze vennootschap*) and European Cooperative Societies (*Europese Coöperatieve Vennootschap*) established in the Netherlands. While there is no certainty as to when and in what form the legislation will come into force, it is anticipated that this will be in the course of 2008. It should be noted that the Directive has no direct application into national laws of the member states, although the deadline for implementation has passed.

The main advantage of the introduction of cross-border mergers is that it allows for the transfer of assets and liabilities by universal title from a disappearing entity from one European jurisdiction to a surviving entity located in another European, while in the event of liquidation or a sale of assets and liabilities, all assets and liabilities must be transferred individually. In addition, the disappearing entity ceases to exist by operation of law and the shareholders of the disappearing entity will – generally – automatically become shareholders in the surviving entity. Moreover, we understand that the cross-border merger may also be beneficial from a tax perspective, as it may provide for a cross-border transfer of assets free from both corporate income tax and dividend withholding tax.

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www.donahuelaw.us

Principal Contact:

Rutger Lambriex
Tel.: (212) 773-2392
E-mail: Rutger.Lambriex@dp.ey.com

Ernst & Young Tower
5 Times Square
New York, NY 10036-6530
Tel: (212) 773-6250
Fax: (212) 773-8814

According to the proposal – and in line with Dutch corporate law – a cross-border triangular merger is also facilitated. This merger differs from the legal merger, since the shareholders from the disappearing entity will not become shareholders of the surviving entity, but instead will acquire shares in a group company of the surviving entity. This type of merger has the advantage for the shareholders that they can usually acquire more “in demand” shares (*courante aandelen*) in the parent company, instead of shares in the surviving entity. The parent company benefits from this construction since there will be no additional minority shareholders in the surviving entity. The triangular cross-border merger is limited to mergers whereby a Dutch company acts as surviving entity.

In line with the requirements as set forth in the Directive, the Dutch proposed legislation also deals extensively with the rights of minority shareholders and creditors. This includes the possibility of compensation of a minority shareholder which voted against the merger proposal, in the event the surviving entity is not a Dutch company.

In the Meantime

As mentioned here above, the Dutch legislative proposal is yet to come into force. In addition, the Directive has no direct application into national laws of the member states. While regulations (*verordeningen*) of the European Commission and the provisions of the EC Treaty itself work directly, provisions of directives that have not been implemented within the deadline can only have direct effect if the directive’s provisions are “sufficiently precise” and “unconditional”. This follows from case law of the

European Court of Justice. The Directive leaves the member states certain choices as regards implementation.

However, in December 2005, the European Court of Justice ruled that legal barriers preventing cross-border mergers can be contrary to the freedom of establishment as provided for by articles 43 and 48 of the EC Treaty (also known as the “Sevic ruling”). The general view after the Sevic ruling was that cross-border mergers were – under certain circumstances – possible under Dutch law.

Based hereon, the Amsterdam sub district court (*Kantongerecht*) recently upheld a cross-border merger between a Dutch limited liability company as the disappearing entity and a German GmbH as the ‘surviving entity’, including the transfer of liabilities from the Dutch entity to the German entity. The court (the lowest ranking court in the hierarchy of the Dutch court system) effectively overruled existing Dutch merger rules by relying on the mentioned European court judgment. However, it must be noted that the court’s judgment contradicts comments made previously by both the Dutch Ministry of Justice as well as advice from a committee that advises the government on Dutch company law legislation. These comments and advice (which remain in place) had clearly indicated that cross-border legal mergers were not possible under current Dutch law, pending implementation of the Directive in Dutch law.

Based on the foregoing, cross-border legal mergers should – under circumstances – be possible under the current rules, even though the current Dutch legal merger rules did not at their inception envisage cross-border legal mergers.