New rules on financial assistance: the end of the prohibition

The Royal Decree of 8 October 2008 amending the Belgian Companies Code (“BCC”) has substantially amended the rules on financial assistance. These new rules will enter into force on 1 January 2009.

These amendments are part of a broader set of measures taken in order to contribute to the promotion of business efficiency and competitiveness of companies without reducing the protection offered to shareholders and creditors. The main innovation is that a company will now be able, under certain conditions, to provide financial assistance to a third party willing to acquire its shares.

The Royal Decree implements European Directive 2006/68/EC amending the Second Company Law “Capital Directive”. This Directive provides the Member States with the opportunity to ease some of the capital protective measures that were taken in the light of the aforementioned Capital Directive, amongst others the rules pertaining to financial assistance. Although the scope of the Directive is limited to rules regarding public limited liability companies (NV/SA), the Belgian legislator decided to extend the application of the new capital rules to private limited liability companies (BVBA/SPRL) and cooperative companies with limited liability (CVBA/SCRL).

The current prohibition

Under the current version of article 629 BCC, a public limited liability company (NV/SA) is prohibited from advancing funds, granting loans or giving guarantees with a view to the acquisition or the subscription of its shares or profit sharing certificates by a third party. The current Belgian financial assistance prohibition is a matter of public policy. Any advance, security or guarantee granted in breach of this prohibition is void or voidable. Moreover, the directors of the company are (i) jointly and severally liable towards the company and third parties for any damage resulting from such a breach and are (ii) liable to criminal sanctions for infringement of
article 629 BCC[5].

The majority of legal authors are of the opinion that such prohibition must be interpreted restrictively due to the criminal nature of the sanctions attached. It is therefore generally admitted that financial support given by the company in view of acquiring the shares of its affiliates, or financial support given by the affiliate company for the acquisition of shares issued by its parent company, is excluded from the scope of the current prohibition.

An overview of the new rules on financial assistance

Under the new version of article 629 BCC[6], a company will be entitled to provide financial assistance with a view to the acquisition of its shares by a third party provided the following stringent conditions are met:

1. the transaction must take place under the responsibility of the company’s board of directors at fair market conditions (i.e. taking into account the usual market interest rate and the usual collaterals for similar types of financing as well as the credit standing of the third party);
2. the transaction is subject to prior approval by the general meeting of shareholders (with the same quorum and majority requirements as for an amendment to the Articles of Association);
3. the board of directors must draft a special report[7] explaining (i) the reasons for such transaction, (ii) the interest of the company to enter into such transaction, (iii) the conditions of the transaction, (iv) the liquidity and solvency risks involved for the company and (v) the price at which the shares are sold. In addition, if a director of the parent company or the parent company itself benefits from the transaction, the report of the board must explicitly justify such a decision taking into account the capacity of the beneficiary and the consequences for the assets of the company[8];
4. the assistance must be paid out of and cannot exceed the amount of distributable profits (within the meaning of article 617 BCC)[9]: The company must set up a non-distributable reserve on the liabilities’ side of its balance sheet equal to the total amount of the financial assistance.

Article 629 BCC (new version) further provides that where the shares are acquired directly from the assisting company (i.e. not from a selling shareholder), either through the sale of its own shares (in accordance with article 622§2 BCC) or through a subscription by the beneficiary to a capital increase, the acquisition of the company’s shares must occur at a fair price.

Except for the requirement of sufficient distributable profits, the above conditions do not apply where financial assistance is granted to members of the personnel or to affiliate companies controlled by the personnel[10].
Open questions

The new rules described above will undoubtedly facilitate the granting of financial assistance by a company in view of the acquisition of its shares by a third party. These rules also give rise to a number of open questions.

One of them relates to the interpretation of article 629 BCC. Article 23 of the Capital Directive as amended by Directive 2006/68/EC provides indeed that where Member States permit a company to, either directly or indirectly (i.e., through a parent or an affiliate), grant financial assistance, they shall make such transactions subject to the conditions set out in that article (i.e. the conditions of new article 629 BCC). Therefore, the question remains as to whether a strict interpretation of article 629 BCC will prevail as is the case with the current prohibition of financial assistance[11] or, on the contrary, if an interpretation of article 629 BCC in conformity with the Capital Directive would not command that such a provision be interpreted extensively so as to prohibit the use of indirect financial assistance through a parent or a subsidiary of the company without complying with the stringent conditions.

Another –more practical - question relates to the liability of directors and selling shareholders. It is unlikely that they will be willing, before closing the transaction, to assume the liabilities (corporate benefit justification, possible criminal sanctions, etc.) relating to the approval of financial assistance granted to the acquirer of the company. Therefore, it may be so that the main benefit of the new rules will be the simplification of debt push down structures after the closing of the sale and under the responsibility of the acquirer of the company’s shares.