The Cross Border Merger Regulations and The European Public Limited Liability Company Regulations – An Analysis

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Contents

INTRODUCTION

There follows an analysis of the two Irish regulations which allow organisations with an international dimension to re-organise their businesses on a European, as opposed to on a purely national, level.

(1) The Cross Border Merger Regulations; and
(2) The European Public Limited Liability Company (the "SE") Regulations

The European Communities (Cross Border Mergers) Regulations 2008 (the "**CBM Regulations**") were enacted in Ireland on 27 May, 2008, in order to implement Directive 2005/56/EC (the "**CBM Directive**"). The CBM Regulations allow that any Irish limited-liability company, other than an Irish company that is limited by guarantee, may be party to a cross-border merger with an entity in another member of the EEA.

The European Communities (European Public Limited-Liability Company) Regulations 2007 (the "**SE Regulations**") were signed into law on 22 January, 2007, in order to give full effect to Council Regulation (EC) Number 2157/2001 of 8 October, 2001 (the "EC Regulation"). The SE Regulations allow for the creation and management of a single, transnational, intra-EEA, legal and corporate entity called a Societas Europaea ("**SE**"): in short, a "European Company".

The common theme of these two Regulations is that they both provide novel solutions to those considering the merging and moving of international operations within the European Economic Area. In the case of the Cross Border Merger Regulations this is achieved by: (1) the absorption of one entity by another, (2) by the acquisition of an existing entity by another, or by (3) the formation of a new corporate entity into which two existing entities can move. In the case of the SE Regulations, this is achieved by, (1) the merger of two entities, resulting in an SE, (2) the formation of a new holding or subsidiary company which takes the form of an SE, or (3) the transformation of existing corporate entity into a new entity called the SE.

THE CROSS BORDER MERGER REGULATIONS

The European Communities (Cross Border Mergers) Regulations 2008 (the "**CBM Regulations**") allow that any Irish limited-liability company that is not a company limited by guarantee (NB. Contrast a company limited by guarantee with the more common company limited *by shares*) may be party to a cross border merger. According to the CBM Directive, a merger is an operation whereby one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company (or to a company that they form), in exchange for the issue to their members of shares representing the capital of that company (or of the newly formed company) and, if applicable, a cash payment. Alternatively, it is an operation whereby a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the shares representing its capital.

The principal benefits of the Regulations are as follows:

- firstly, that they provide a harmonized platform for mergers within the EEA;
- secondly, that liquidation is avoided as the Transferor Company will be dissolved automatically once the merger is effected;
- thirdly, that there is legal certainty as once the merger is approved by the competent authority (which in Ireland is the High Court) in a member state the merger cannot subsequently be deemed null and void; and
- finally, that the assets and liabilities of the Transferor Companies transfer automatically by operation of law, eliminating the need for any additional documentation.

It is important to note, however, that unlike the provisions regarding the SE as laid out in the SE Regulations (described below), the registered office of the company post cross-border merger must be in the Member State in which the successor company is registered and does not have the potential to move from one Member State to another.

Effecting a Cross Border Merger

A cross border merger may be effected in one of the following three ways:

1. Merger by absorption

This is an operation in which, on being dissolved and without going into liquidation, a company transfers all of its assets and liabilities to a company which is the holder of all the shares or other securities representing the capital of the first-mentioned company.

This would occur where an existing company acquires all the assets and liabilities of its wholly owned subsidiary.

2. Merger by acquisition

This is an operation in which a company (*other than a company formed for the purpose of the operation*) acquires all the assets and liabilities of another company that is, or other companies that are, dissolved without going into liquidation in exchange for the issue to the members of that company, or the members of those companies, of securities or shares in the first mentioned company, with or without any cash payment.

The members of the Transferor Company are given securities or shares in the Successor Company when the Successor Company acquires the transferor company, either with or without a cash payment.

3. Merger by formation of a new company

This is an operation in which two or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a company that they form in exchange for the issue to their members of securities or shares representing the capital of that new company, with or without any cash payment.

Those holding securities or shares in the original companies will be given securities or shares in the newly formed company, with or without a cash payment.

Steps Involved in a Cross Border Merger

There are a number of steps which an Irish company must carry out pre merger in order to effect a cross border merger. These steps are roughly as follows:

1. In conjunction with the management of the other Companies involved in the cross-border merger, the Irish company must draw up and adopt draft common terms of merger.

2. The director's of the Irish company must prepare an explanatory report for the members of the Company. This report must explain the implications of the cross-border merger for the

members, creditors and employees of the Irish company and state the legal and economic grounds for the draft terms of merger.

3. The Irish company must appoint an independent person[1] to prepare a report on the cross-border merger proposals for the members of the Irish company.

4. The draft terms of merger must be delivered to the Registrar of Companies in Ireland (i.e. a statutory public official in Ireland) along with a notice specifying certain details regarding the Irish company and the proposed cross border merger. This notice must then be published in two national newspapers before the common draft terms of merger are approved by special resolution passed at a general meeting of the Irish Company.

5. The Irish company must apply to the High Court of Ireland for a certificate of compliance with the pre-merger requirements required of that company, such a certificate being conclusive evidence that the Irish company has properly completed the pre-merger requirements.

6. All of the merging companies must apply jointly to the competent authority in the country in which the company resulting from the merger will be registered for an order confirming the completion of the merger.

7. The Irish company must notify completion of the merger to the Registrar of Companies for either the registration of the merger or the de-registration of an Irish merging company where the company resulting from the cross-border merger is not Irish.

Employee Participation Rights in Cross Border Mergers

A company formed under the CBM Regulations differs from an SE in its treatment of employees. Generally, when a cross-border merger is effected, the rights and obligations arising from the contracts of employment of the Transferor Companies are transferred to the Successor Company.

The CBM Regulations specifically protect what are known as “employee participation rights”. The CBM Regulations require that where the employees in a Transferor Company have employee participation rights, these must be protected where the Successor Company is Irish. Employee Participation is defined in the CBM Regulations as meaning “the influence of the representative body or the employees’ representatives (or both) in the affairs of a company by the way of (*a*) the right to

[1] Directive 2009/109/EC of 16 September 2009 amends this publication requirement by permitting publication on the merging companies’ websites instead. Members States are to implement the 2009 Directive by 30 June 2011 and, so, the CBM Directive will continue to apply until 30 June 2011.

elect or appoint some of the members of the company's supervisory or administrative organ, or (*b*) the right to recommend or oppose, or both to recommend and oppose, the appointment of some or all of the members of the company's supervisory or administrative organ.

Irish law already deals generally with the concepts of employee information and consultation procedures, however it does not provide for employee participation. The Regulations simply protect employee rights which already exist in any one of the merging companies as opposed to imposing new ones. The Regulations provide that the merging companies can either agree to negotiate a new agreement in relation to participation rights or alternatively they can adopt the default position of the standard rules.

Employee protection is dealt with under two headings:

1. Involvement:

The management or administrative organs of the merging companies must make arrangements for the establishment of a "special negotiating body". This is established to negotiate with the competent body of the merging companies regarding the establishment of arrangements for the involvement of employees within the Successor Company. The remit of the special negotiating body will be to ascertain what the position of the employees will be in the Successor Company.

The rules governing the involvement of employees in the Successor Company may be agreed between the special negotiating body and the management or administrative organs of the merging companies. Should no agreement be reached within 6 months, the Standard Rules (as set out in Schedule 1 of the Regulations) will apply.

2. Participation:

In Ireland there are no statutory provisions regarding employee participation. The CBM Regulations do not create new rights under this sphere, but merely protect existing rights in non-Irish merging companies.

If one or more of the companies involved in a cross-border merger had previously made provision for employee participation or are registered in a country in which employee participation is required, an Irish Successor Company must have regard for these participation rights.

Consequences of a Cross Border Merger

Some of the consequences of a successful cross-border merger include the following:

1. The transfer to the Successor Company of all of the assets and liabilities of the merging companies.

2. The issuing of shares in the Successor Company to the shareholders of the merging companies.

3. The dissolution of the companies being acquired in the cross-border merger.

4. Every contract, agreement or instrument to which a merging company is a party being construed and having effect as if the Successor Company had been a party thereto instead of the merging company.

5. The law of the state in which the Successor Company's registered office is located shall be the law applicable after the merger.

The CBM Regulations offer Irish companies a wide range of options with regards to the structure of their business, and this offers Irish companies significant commercial advantages. The Regulations provide Irish companies with an opportunity to plan and carry out the reorganisation of their business on a European level. They can now formulate international group structures more simply and cost effectively.

Other Considerations in Cross Border Mergers

As the Transferor Companies dissolve automatically in the case of a merger completed in accordance with the Regulations, a pre-merger reorganisation may be required in order to ensure that any assets and/or liabilities which are not intended to transfer are moved elsewhere.

Tax Consideration in Cross Border Mergers

A cross-border merger under the Regulations gives rise to certain tax concerns, including the issue of whether the cross-border merger gives rise to a charge to Irish capital gains tax, stamp duty or corporation tax.

Part 21 of the Taxes Consolidation Act 1997 implemented certain provisions of Council Directive No. 90/434/EEC of July, 1990, which provides for tax neutrality in relation to cross-border mergers. The Revenue Commissioners of Ireland have indicated that they are satisfied that the tax legislation as drafted is adequate to achieve tax neutrality in the case of cross-border mergers.

THE EUROPEAN PUBLIC LIMITED LIABILITY COMPANY REGULATIONS

The European Communities (European Public Limited-Liability Company) Regulations 2007 (the "**SE Regulations**") allow for the creation and management of a new legal and corporate entity called the Societas Europaea ("**SE**"). The SE is a European public limited company that is subject to Council Regulation (EC) Number 2157/2001 (the "**EC Regulation**") and subject to the laws applicable to a public limited company in the EU Member State in which the SE has its registered office.

The object of the SE Regulations is essentially to enable the creation of a single legal and corporate framework for companies who operate in more than one country within the EEA, eliminating the need for companies to comply with many different regulatory systems, and facilitating the often complex merger of companies from different Member States. The EC Regulation states that it is essential that companies should be able to plan and carry out the reorganisation of their business on a European level and that companies from different Member States should have the option of combining their potential by means of mergers. The introduction of the SE was intended to be the means through which the EC proposed to enable companies achieve this aim and to facilitate companies throughout Europe who wish to do business at an EU level.

A company which has its registered office in a Member State, but its head office outside the EEA, may also participate in the formation of an SE provided it can show "a real and continuous link" with the economy of the relevant Member State.

Forming an SE

An SE may be registered in any of the Member States of the European Economic Area ("**EEA**") and may be formed in any one of the five following ways:-

(1) An SE formed by Merger (through acquisition)
(2) An SE formed by Merger (through formation of a new company)
(3) Forming a Holding SE
(4) Forming a Subsidiary SE
(5) Transforming an existing entity into an SE

1. An SE formed by Merger (through acquisition)

Two or more public limited companies with registered offices and head offices within the EEA, or two or more existing SE's, may merge to form a new SE provided that at least two of them are governed

by the laws of different Member States. It is important to note that formation by merger is *only* available to public limited companies where at least two of them are governed by the law of different Member States.

In the case of a merger by acquisition, the acquiring company shall take the form of an SE when the merger takes place. The target company (or companies), which holds the target business(es) that is to be acquired, is wound up without going into liquidation and transfers to the acquirer all its assets and liabilities in exchange for the issue to its shareholders of shares in the acquiring company and a cash payment, if any, not exceeding 10 % of the nominal value of the shares so issued or, where they have no nominal value, of their accounting par value.

Draft terms for the merger must be drawn up by both companies and presented to general meetings of their shareholders for approval. It is important to note that the Director of Corporate Enforcement (i.e. a statutory public official in Ireland) may oppose the taking part in a merger by a public company on grounds of public interest. However, if and when all pre-merger acts and formalities have been completed, the High Court of Ireland will issue a certificate confirming that fact. It is possible for two or more public limited companies registered outside of Ireland to merge to form an SE registered in Ireland.

2. An SE formed by Merger (through formation of a new company)

In the case of a merger by the formation of a new company, the SE shall be the newly formed company. Two or more companies are wound up without going into liquidation and transfer all their assets and liabilities to a new company that they set up in exchange for the issue to their shareholders of shares in the new company and a cash payment, if any, not exceeding 10% of the nominal value of the shares so issued or, where they have no nominal value, of their accounting par value.

The draft terms of merger must be drawn up and presented to a general meeting of their shareholders for approval in the same manner as is required for an SE formed by merger (by acquisition). The Director of Corporate Enforcement may oppose the merger. Ultimately, when all pre-merger acts and formalities have been completed the High Court of Ireland will issue a certificate.

Consequences of an SE formed by Merger

Accordingly, the consequences of the formation of an SE formed by merger (whether by acquisition or by formation of a new company) are as follows:

- all assets and liabilities transfer to the SE;

- the shareholders of the merging companies or of the company being acquired (as the case may be) become shareholders of the SE; and

- both or all of the merging companies (as the case may be) cease to exist or the company being acquired ceases to exist, as appropriate.

3. Forming a Holding SE

Public and private limited-liability companies formed under the law of a Member State with registered offices and head offices within the Community may promote the formation of a holding SE provided that each of at least two of them:

(a) are governed by the law of a different Member State, or

(b) have for at least two years had a subsidiary company governed by the law of another Member State or a branch situated in another Member State.

Before forming a holding SE, draft terms for the formation and an explanatory report must be drawn up by the companies promoting the formation and presented to general meetings of their shareholders. The explanatory report must explain and justify the legal and economic aspects of the formation and indicate the implications for the shareholders and for the employees of adopting the form of a holding SE.

Regardless of where the holding SE will be registered, any Irish registered company involved in its formation must file the draft terms for its formation with the Registrar of Companies in Ireland at least one month before the company's general meeting.

Once the draft terms have been approved, shareholders have 3 months to notify the company whether they intend to contribute their shares to the formation of the holding SE. If the minimum proportions of shares (which, according to Article 32(2), shall be shares conferring more than 50% of the permanent voting rights) are not assigned within that time, the SE cannot be formed.

Where the conditions are fulfilled, a notice to that effect must be delivered to the CRO. Shareholders who have not previously indicated that they intend to make their shares available have a further month in which to indicate whether they intend to make their shares available for the purposes of forming the holding SE. The holding SE may not be registered until it is shown that the formalities have been completed and any conditions fulfilled.

The companies promoting the formation of a holding SE shall continue to exist and the shareholders who have contributed their securities to the formation of the SE shall receive shares in the holding SE.

4. Forming a Subsidiary SE

Companies or firms constituted under the civil or commercial law of a Member State including cooperative societies and other legal persons governed by public or private law, save for those which are non-profit-making, who have their registered offices and head offices within the Community may form a subsidiary SE.

An existing SE may set up one or more subsidiaries in the form of an SE.

5. Transforming an existing entity into an SE

A public limited-liability company formed under the law of a Member State which has its registered office and head office within the Community may be transformed into an SE if for at least two years it has had a subsidiary company governed by the law of another Member State. It is important to note that formation by transformation is *only* available to public limited-liability companies.

A company which has its head office outside the EU but its registered office in a Member State may participate in the formation of an SE provided it has a real and continuous link with the economy of the relevant Member State.

Moving an SE's Registered Office

One of the major advantages to the setting up of an SE is that the registered office of an SE may be transferred to another Member State and such transfer shall not result in the winding up of the SE or in the creation of a new legal person.

Before an SE can move its registered office to another Member State, the management or administrative organ of the SE must draw up:

- a transfer proposal in line with Article 8(2) of the EC Regulation; and
- a report explaining and justifying the legal and economic aspects of the transfer and its implications for shareholders, creditors and employees.

When the transfer proposal is drawn up, the SE must notify in writing its shareholders and every creditor (of whose claim and address it is aware of) of their right to examine the transfer proposal

and the report. They must be informed not later than one month before the general meeting is called to decide on the transfer.

A transfer proposal must contain certain information including the following:

- proposed registered office;
- proposed statutes;
- any implication on employees' involvement;
- the transfer timetable; and
- any rights provided for the protection of shareholders and/or creditors.

No decision to transfer can take place for at least two months after the publication of the proposal.

Every invoice, order for goods or business letter sent after the transfer proposal and report become available for inspection shall contain a statement that the SE is proposing to transfer its registered office to another Member State and this Member State must be identified in the notice.

Any transfer is subject to shareholder approval. Member States may implement minority protection provisions. Member States may provide that, as regards SE's registered in that Member State, the transfer of a registered office which would result in a change of the law applicable shall not take effect if any of that Member State's competent authorities opposes it within the relevant two month period. Such opposition may be based only on grounds of public policy.

Before the competent authority of a Member State can sanction the transfer of an SE's registered office, the SE shall satisfy the competent authority in that Member State that, in respect of liabilities arising prior to the publication of the transfer proposal, the interests of creditors and holders of other rights in respect of the SE have been adequately protected in accordance with the requirements set down by the Member State in which the SE has its registered office. The court, notary or other competent authority of the Member State shall, if satisfied that all formalities relating to the transfer have been complied with, issue a certificate affirming such compliance. One such formality is that the company being converted into an SE has net assets at least equivalent to its capital plus those reserves which must not be distributed under the law or the Statutes.

Where an SE is supervised by a national financial supervisory authority according to Community directives, the right to oppose the change of registered office applies to this authority as well.

An SE which has transferred its office to another Member State shall be considered, in respect of any cause of action arising prior to the transfer, as having its registered office in the Member State where the SE was registered prior to the transfer, even if the SE is sued after the transfer.

If an SE is insolvent, a transfer of registered office will not be allowed and certain safeguards exist to protect creditors.

Employee Participation when considering SE's

The rules on the involvement of employees in an SE are set out in Council Directive 2001/86/EC (the "**SE Directive**") and the provisions contained therein compliment the EC Regulation. The SE Directive is designed to ensure that employees have a right of involvement in the issues and decisions affecting the SE, and so an SE may not be registered and brought into existence unless an agreement on arrangements for employee involvement pursuant to Article 4 of the SE Directive has been concluded, or a decision pursuant to Article 3(6) of the Directive has been taken, or the period for negotiations pursuant to Article 5 of the Directive has expired without an agreement having been concluded.

Worker involvement provisions in the SE will be decided upon by negotiations between employees and management before the creation of the SE. If an agreement cannot be reached through the negotiations, provisions contained in the Directive will apply. The SE Directive provides for worker involvement in the SE if a minimum percentage of employees from the entities coming together to form the SE enjoyed worker involvement provisions. The SE Directive permits Member States to not implement these default worker involvement provisions in their national law, but then an SE cannot be created in that member state if the provisions in the Directive would apply and negotiations between workers and management are unsuccessful.

Creditor Protection when considering SE's

The amount of Creditor Protection afforded depends on the circumstances, as follows:-

1. When a company is seeking to become an SE or part thereof

All assets and liabilities of acquired companies pass to the SE and so creditors will continue to have a cause of action against the SE for debts owed to them before the companies merged or were acquired.

2. When an SE is seeking to move its registered office

See the commentary on moving an SE's registered office above.

Management of an SE

An SE can be managed and controlled in one of two ways, either a one-tier system, where management is undertaken by an 'administrative organ', or a two-tier system, where management is undertaken by a 'management organ' and a separate 'supervisory organ' supervises the work of the management organ.

1. One Tier system

Under this system, an administrative organ manages the SE.

2. Two Tiered system

Under this system, a management organ managers the SE and a separate supervisory organ supervises the management organ. The supervisory organ may not exercise management powers. However, both the management and supervisory organs must have at least two members. There is no upper limit on the number of members of either organ. Other Member States may set different lower and upper limits on the number of members of an SE's administrative, management and supervisory organs.

Deficiencies of the SE Regime

The SE framework has not proved popular in the Irish context and is little used. The major pitfall in the SE regime flows from the lack of harmonization of company and employment law through the EEA. There are obvious difficulties with trying to apply one set of rules and concepts to the operations of an entity whose origins might be in two diverse legal systems. The disconnect between the principles, ideologies and legislative history of common law and civil law systems is an added hurdle which may have to be overcome.

CONCLUSION

Since its fairly recent introduction the Cross Border Merger Regulations are being utilised in an increasingly diverse manner, from being used to achieve economies of scale within international businesses in these more leaner times to facilitating the extraction of the more successful parts of a business from a jurisdiction where its has been decided to cease operations altogether.

The SE Regulations, while older than the Cross Border Merger Regulations, are still little used and can only provide a solution to cross border businesses that would meet the requirements of a very limited few. The ability to move an SE's registered office around between EEA jurisdictions may seem like an attractive facility for those who want to submit their operations to a new regulatory regime that is more favourable to their existing needs. But a move of registered office is not straightforward: there are significant administrative and substantive hurdles to be overcome before the move of registered office will be permitted. Aside from this aspect, it is difficult to see where the growth in the use of SE might arise under the existing regime.

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