Buying a European Business -
the mysteries explained

Expert knowledge means success

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Introduction

This publication[1] looks at negotiated acquisitions in seven of the principal Member States of the European Community (EC): Belgium; France; Germany; Italy; The Netherlands; Spain; and the United Kingdom.

Descriptions of acquisition activity in Europe often concentrate on public takeover bids and the acquisition of stakes in listed companies. The statistics show, however, that negotiated acquisitions of privately-held companies predominate over takeovers, both in the number of transactions and the aggregate value involved.

Acquisition practices in Europe have tended to converge due to the internationalisation of domestic Mergers & Acquisitions (M&A) markets. The lowering of barriers to capital flows has also reduced the scope for governmental interference in privately-negotiated deals. However, this has enhanced the role of competition and merger control laws and governments do still retain control and influence in regulated and sensitive industries. In addition, harmonisation has had only limited effect in some important areas, such as taxation, and cultural differences continue in many ways to be more important than legal differences.

Each country is not reviewed separately. Instead, common themes and issues are taken we describe how those are treated differently, if at all, in each jurisdiction. By adopting a thematic approach we emphasise the similarities as well as the differences in law and practice. In this publication, we concentrate on agreed cash acquisitions by a foreign buyer of 100% of the shares of a limited liability company. The special issues that arise in relation to partial acquisitions or joint ventures are not covered here.

Cross-border acquisitions tend to be more difficult and complex than purely domestic transactions. Cultural and language differences, as well as lack of familiarity with local issues, are likely to present obstacles to both parties and will need care, time and sensitivity to overcome.

The first steps

Having identified a possible target, the purchaser will try to obtain basic information on the target's ownership, capital structure and management and further information on its business. To the extent it does not have this information already, it should build a data base of information on the target's market, using sources such as yearbooks, Chamber of Commerce files, libraries, trade sources and market research reports.
The quality of publicly available information greatly depends on the country, the target's area of business and the type of entity.

Corporate entities

There is a multiplicity of different types of corporate entity in Europe, in particular under the civil law systems of continental Europe.

The limited liability business corporation is the predominant form, although in all European countries a distinction is drawn between the joint stock company (e.g. the German AG, the French SA or the Italian SpA), which is often misleadingly called a "public" company even though it is often used for businesses without a stock exchange quotation, and the limited liability "private" company (e.g. the German GmbH, the French SARL or the Italian SrL).

The principal differences between the two types of company are the level of prescribed minimum share capital (joint stock companies generally have a higher level of minimum capital), the types of share capital (eg usually only joint stock companies can issue bearer shares) and the types of management structures available. Many EC company law harmonisation rules currently only apply to "public" companies.

Nevertheless, the limited liability corporation is by no means the exclusive form of business entity. Many businesses operate through various types of unlimited company, general partnership or limited partnership (such as the French societé en commandite type of company). For example, in Germany there are some 120,000 registered limited partnerships (KGs) and a popular business form is the GmbH & Co KG, a limited partnership where the general partner is a limited liability company.

Use of this publication

IMPORTANT NOTE

This publication should only be used as a general guide since it was originally produced about 10 years ago and some of the data, particularly on requirements in certain European countries, may have changed.

As with most things, it is advisable to take professional advice before taking action on matters referred to. Nevertheless, we hope the publication is helpful.

Basic information on the entity can usually be obtained from either the national or local court register or company registration office. For limited liability companies this will include the minimum information specified in the EC Directives, including copies of constitutional documents, details of share capital and particulars of the directors or managers. In some cases (eg UK companies, a French SARL or a German GmbH), a search will also reveal the identity of the shareholders but this is the exception rather than the rule (in The Netherlands a search will only reveal the identity of a single shareholder). In some countries (e.g. France and the UK), the public registry can also provide information on mortgages, pledges and other security granted by the company to banks and other financiers.

Financial information

In addition, unlike the US or Japan, the public file can prove a useful source of basic financial information on unlisted companies. The Fourth EC Company Law Directive, adopted in 1978, imposed:

- uniform formats for annual accounts;
- common principles of valuation for items in the accounts (historical cost, accruals principle, prudence concept, etc);
- the overriding requirement that the accounts show a "true and fair view";
- a requirement that annual accounts be audited; and
- a requirement to file copies of the annual accounts for public inspection.

The Seventh EC Company Law Directive, adopted in 1983, imposed requirements to prepare consolidated accounts and harmonises the rules as to which entities must be included in the consolidation.

Management structures of companies in Western Europe

	"Public" Company	"Private" Company
Belgium	SA/NV1,2: board of directors (minimum 3)[3]	SPRL/BVBA1: one or more managers
France	SA[2]: board of directors (minimum 3; maximum 24)[4] - two tier board optional	SARL1: one or more managers (supervisory board optional)
Germany	AG: two tier board mandatory	GmbH[1,2]: one or more managers - supervisory board mandatory in some cases under the co-determination system
Italy	SpA[2]: board of directors (sole director possible)[5]	SrL[1]: board of directors (sole director possible)[5]
Netherlands	NV: board of directors (sole director possible) - two tier board optional and mandatory in some cases	BV[1,2]: board of directors (sole director possible) - two tier board optional and mandatory in some cases
Spain	SA[1,2]: board of directors (sole director possible)	SRL[1]: board of directors (sole director possible)
United Kingdom	plc: board of directors	Ltd[1,2]: board of directors (sole director possible)

Notes

1. Type of limited company typically used for a medium-sized family-owned trading company.
2. Type of limited company typically used as a medium-sized wholly-owned subsidiary of a listed company.
3. As from 1 July 1996 a SA/NV can have 2 directors provided it only has 2 shareholders.
4. In France, directors of an SA must hold qualification shares.
5. An Italian SpA and certain larger SrLs must also have a board of statutory auditors (*collegio sindacale*) consisting of 3 or 5 members plus alternates. Smaller SrLs may also adopt this structure in their statutes. All of the members of the board of auditors need to be professional accountants or hold another relevant qualification. In addition to the audit of the annual accounts, members of the board of auditors attend meetings of the board of directors, perform a quarterly check on cash and investments and may investigate any aspect of management. To this extent, it has some resemblance to a supervisory board.

The ability to exercise control over management will usually be of importance to a buyer but the management structures of business organisations vary widely. There are usually constraints on the ability to manage a business solely in accordance with shareholder wishes. In many European countries even a 100% shareholder only has limited powers to remove or replace a company's management, in particular where directors or managers are appointed for a fixed term of office or where there is a two tier board structure. Two tier board structures may be encountered in Germany, The Netherlands and, less frequently, in France.

Germany

An AG must adopt a two-tier board structure consisting of a supervisory board (Aufsichtsrat), appointed by shareholders and a separate management board (Vorstand) whose members are appointed by the supervisory board for fixed terms of office. Members of the supervisory board cannot also be members of the management board. The supervisory board's approval is required for certain decisions of the management board and the supervisory board also exercises general supervision over the management board and approves the accounts prepared by management.

Under the co-determination system and works' councils legislation, employees of an AG with more than 2,000 employees have the right to elect half the members of the supervisory board, although the chairman (who has a casting vote) continues to be appointed by the shareholders. At least one member of the management board (Arbeitsdirektor) must be elected by employees. Employees of an AG with fewer than 2,000 employees have the right to elect one-third of the members of the supervisory board. A GmbH with up to 500 employees is not subject to co-determination. Where a GmbH has more than 500 employees it must have a supervisory board, one third of whose members are elected by employees. Where a GmbH has more than 2,000 employees, employees have the right to elect half the members of the supervisory board, although (as is the case for an AG) the chairman (who has a casting vote) is appointed by shareholders. Special rules apply in the mining and steel industries. The supervisory board supplements the normal system of management of a GmbH by managers (Geschäftsführer), but even where co-determination does not apply the shareholders of a GmbH can establish a form of advisory board (Beirat). The works' councils of German companies also have extensive rights to information and consultation as well as rights of veto over certain decisions by management.

The Netherlands

Banks, insurance companies and certain large companies (Structuurvennootschap) are subject to special rules, which require them to adopt a two-tier board structure. A company will be subject to these rules if its net assets exceed NLG 25m (approximately US$14.4m), it (or any of its subsidiaries) has a works' council and its group employs more than 100 employees in The Netherlands.

When a company becomes subject to these special rules, the first members of the supervisory board (raad van commissarissen) are appointed by shareholders but subsequently the supervisory board appoints its own members and is thus, in effect, a self perpetuating body. Recommendations for appointments to the supervisory board can be made by the management board (bestuur or directie), and by shareholders and works' councils. Shareholders and works' council have the right to appeal to the court against a proposed appointment. As with the German equivalent, the supervisory board appoints the members of the management board (who cannot also be members of the supervisory board). The supervisory board has powers of veto over certain important management decisions and approves the annual accounts prepared by management. Employees will also be represented by works' councils in these companies and the works' council has extensive rights to information and consultation, as well as powers which could, in fact, suspend or even block certain important transactions (including a change of control).

Where a foreign company acquires control over a Dutch company subject to these special rules, the rules will only partially apply after the acquisition if a majority of all employees of the enlarged group are employed outside The Netherlands. However, shareholders' powers to amend the constitutional documents (to take advantage of this) may have been restricted. In any event, such an amendment will need to be approved by the Ministry of Justice and thus may take time to implement.

France

An SA may adopt a two tier board structure but this is not mandatory and can be abandoned at any time by shareholders' resolution. Less than 2% of SAs have adopted this structure. Where an SA adopts the two tier structure, the supervisory board (conseil de surveillance) is appointed by shareholders although if there is a workers' committee two or more employee representatives (depending on the number of employees) will be entitled to attend its meetings (although they will not have a vote).

The constitutional documents can also allow employees to elect up to one quarter of the supervisory board. The members of the management board (directoire) are appointed by the supervisory board and can only be removed by shareholders on the recommendation of the supervisory board. As in Germany and The Netherlands, it is not possible to be a member of both boards and the supervisory board has certain powers of veto over some management board decisions and the right to examine the annual accounts.

EC Company Law Directive 90/605 adopted in November 1990 extended the scope of the Fourth and the Seventh Directives to cover partnerships and unlimited companies which in fact have limited liability.

However, concentration on the Directives may give a false impression of the degree of harmonisation and the degree of openness of financial information in Europe:

- significant divergences in accounting principles and practice continue to exist despite the Directives. There is a striking difference between The Netherlands and the UK on the one hand, where the commercial approach to accounting has traditionally been the dominant influence (exemplified by the overriding importance of showing a "true and fair view"), and the other countries of continental Europe, where financial accounting practice is linked to rigid rules, often dominated by fiscal accounting regulations (e.g. in Germany and Italy).
- the level of harmonisation imposed by the Directives is relatively modest. Member states remain free to go their own way on important areas such as revaluation of fixed assets, depreciation, treatment of goodwill and other intangibles, foreign currency translation, extraordinary items and pension costs.
- the Directives themselves allow significant exemptions for small and medium sized businesses. Small companies can be allowed to do without an audit. Small and medium sized companies can be allowed to file abridged or abbreviated accounts (even though they may be required to provide fuller financial statements to their shareholders). Small and medium sized groups of companies can be exempted from the requirement to prepare consolidated accounts.
- commercial attitudes to disclosure of financial information differ from country to country.

Potential purchasers need to be aware of these differences when evaluating financial information provided on a target company, and when considering the implications of contractual terms (such as accounts warranties and price adjustment formulae) which depend on the application of accounting principles and practices which may be unfamiliar. In some countries it is almost customary that the published accounts of a private company do not accurately reflect the profitability of the business claimed by the seller. This presents the buyer with a problem since it becomes difficult to evaluate the true worth of the business and may indicate significant hidden tax liabilities. A solution may be for the purchaser to commission a full audit but this can antagonise the seller and the results may cause difficulty with the local tax authorities.

In any event, a purchaser needs to consider at an early stage whether to arrange for an independent accountants' investigation of the target, even if it falls short of a full audit, and it must recognise that this may well be resisted by the seller for bona fide reasons.

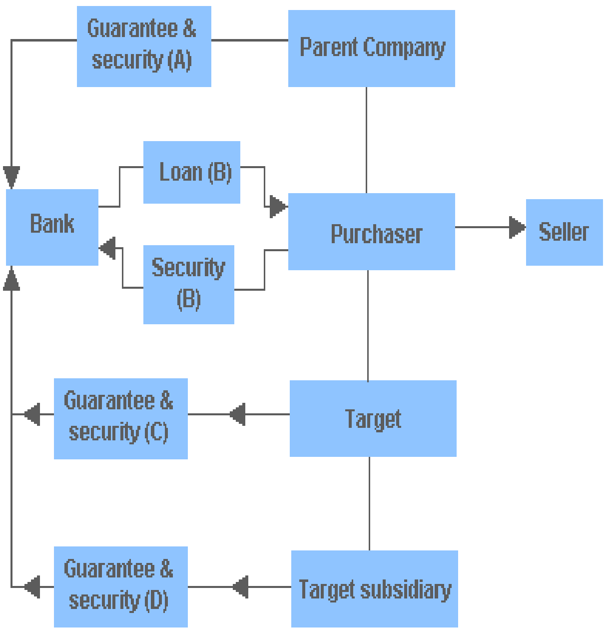
Availability of accounting information on unlisted companies

	Accounts available for inspection at	Main exemptions for individual company accounts	Tests for exemption for small or medium sized enterprises (individual company accounts)
Belgium	National Bank of Belgium	Small companies are exempt from audit (but must file abridged profit and loss account)	<u>Small:</u> BF 145m turnover (about US$4.6m) accounts including a BF 70m gross assets (about US$2.2m) 50 employees <u>Medium:</u> N/A
France	Local commercial court	(1) All SAs must be audited but small and medium sized SARLs are exempt from audit (2) Small companies can file abridged accounts, but must include a profit and loss account	<u>Small:</u> FF 3m turnover (about US$0.6m) FF 1.5m gross assets (about US$0.3m) 10 employees <u>Medium:</u> FF 20m turnover (about US$3.8m) FF 10m gross assets (about US$1.9m) 50 employees
Germany	Trade register at local commercial court	(1) Small companies exempt from audit (2) Small and medium sized companies may file abridged accounts (and small companies need not file a profit and loss account)	<u>Small (Exemptions apply if at least two ceilings are not exceeded):</u> DM 10,620,000 turnover (about US$6.9m) DM 5,310,000 balance sheet total - (about US$3.4m) 50 employees <u>Medium:</u> DM 42,480,000m turnover (about US$27.6m) DM 21,240,000 balance sheet total (about US$13.8m) 250 employees
Italy	Companies register at local Chambers of Commerce	(1) Small companies will be permitted to file abbreviated accounts (2) Small' SrLs will be exempt from audit if their capital is less than Lit 200m (about US$0.13m)	<u>Small:</u> Lit 4bn turnover (about US$2.6m) Lit 2bn gross assets (about US$1.3m) 50 employees <u>Medium:</u> N/A
Netherlands	Trade register of local Chamber of Commerce	(1) Small companies exempt from audit (2) Small and medium sized companies may file abridged accounts (and small companies need not file a profit and loss account or directors' report) (3) Exemption from audit and filing requirement for subsidiaries where an EC parent company has guaranteed debts	<u>Small:</u> NLG 10m turnover (about US$5.8m) NLG 5m gross assets (about US$2.9m) 50 employees <u>Medium:</u> NLG 40m turnover (about US$23.1m) NLG 20m gross assets (about US$11.6m) 250 employees
Spain	Local mercantile registry	(1) Small companies may file an abbreviated balance sheet and profit and loss account and are exempt from audit (2) Medium sized companies may file an abbreviated profit and loss account	<u>Small:</u> Ptas 600m turnover (about US$4.6m) Ptas 300m gross assets (about US$2.3m) 50 employees <u>Medium:</u> Ptas 2,400m turnover (about US$18.5m) Ptas 1,200m gross assets (about US$9.3m) 250 employees
United Kingdom **** See Note on Page 1**	National Companies Registry	(1) All companies required to prepare accounts (2) Certain small and medium-sized private companies may file abbreviated balance sheets (and certain small companies need not file a profit and loss account or directors' report)	<u>Small:</u> £2.8m turnover (about US$4.7m) £1.4m total assets (about US$2.4m) 50 employees <u>Medium:</u> £11.2m turnover (about US$18.9m) £5.6m total assets (about US$9.5m) 250 employees

Financial assistance

Using the target's assets to finance the acquisition involves a complex area of law but is a structure of particular interest to the leveraged buyer or a buyer that needs to "push down" acquisition debt to acquired subsidiaries. Unlike for example in the US, all EC Member States impose restrictions on a company advancing funds, making loans or providing security with a view to the acquisition of its shares by a third party. This is required by the Second EC Company Law Directive, at least for "public type" companies, but in most cases the rules apply to all types of limited liability companies.

Financial assistance illustrated



The guarantees and security given by Target (C) and Target's subsidiaries (D) may be prohibited financial assistance, but the parent company guarantee (A) and the Bank's primary security (B) are not prohibited.

What is financial assistance?

The most common forms of prohibited financial assistance involve the target and its subsidiaries giving security (in the form of mortgages, charges or guarantees) to support loans made to the purchaser for the purpose of the acquisition of the target (transactions (C) and (D) in the diagram).

The question of financial assistance must also be considered where the target lends money to the purchaser, waives debts owed by the seller of the shares, makes a gift to either the seller or the purchaser, buys assets from the purchaser to put it in funds or sells assets to either the seller or the purchaser (in particular in the last two examples where the terms of the transaction are not settled on an arm's-length basis).

There is some inconsistency between jurisdictions on whether the rules apply to a subsidiary of the target giving financial assistance in connection with the acquisition of shares in the target (but caution must be exercised before relying on the absence of specific rules relating to subsidiaries because their assistance might amount to prohibited indirect assistance by the target itself). The rules are usually mandatory and cannot be waived by shareholders or creditors (but see below).

What financial assistance can be given?

Normally the following financial assistance can be given by the target group:

- dividends paid out of distributable profits by the target, whether to the seller before the sale of the shares or, afterwards, to the purchaser;
- amounts paid out by the target on a lawful reduction of capital or as a result of the purchase or cancellation by it of some of its own shares (e.g. the redemption of redeemable shares). Most jurisdictions restrict these procedures in some way;
- a distribution made on the liquidation of the target.

Financial Assistance: An Update

On 1 October 2008 English law as it relates to the provision of financial assistance by an English company for the purpose of the acquisition of shares in itself or its English holding company, changed. The same change applies where, after the acquisition has taken place, assistance is given for the purpose of reducing or discharging a liability incurred for the acquisition.

The old statutory prohibition on an English private company providing this kind of assistance for the purpose of the acquisition of shares in itself or another private company was repealed. That repeal makes the "whitewash" procedure redundant.

However, the statutory prohibition still applies to any English public company and also to an English private company if the shares acquired are shares in an English public company. So, as is the case at present, if an English public company is acquired, that company must be taken private before any financial assistance can be given by its English private company subsidiaries.

Under section 678(1) of the Companies Act 2006, it is unlawful for a public company or its subsidiaries to give financial assistance to any person acquiring, or proposing to acquire, shares in that public company, where the financial assistance is for the purpose of the acquisition and where the assistance takes place before or at the time of the acquisition. Section 678(2) contains an exception to the prohibition, which applies where the primary purpose of the financial assistance is not for the purposes of an acquisition, or where the financial assistance is only incidental to that acquisition.

All of these routes may, however, have a number of adverse taxation or other consequences which mean that they are effectively unavailable.

Where the purchaser needs access to the assets of the target to fund its acquisition or the lenders to the purchaser want direct security in the form of guarantees from the target (or charges over the target's assets), there are alternative routes, including:

- purchasing the assets of the target instead of its shares: the financial assistance rules will then not apply and the purchaser can use the assets or grant security over them without restriction;
- in some jurisdictions (such as Germany) it may be possible for the purchaser first to buy the shares of the target and then to buy its assets (perhaps subsequently liquidating the target company);
- in many continental European jurisdictions, it is possible for the purchaser to create a new, locally incorporated subsidiary to buy the shares in the target and then to effect a legal merger between the new subsidiary and the target (a two step acquisition);
- in The Netherlands and the UK, there are certain exceptions which can be used to enable a private company to give financial assistance to a purchaser;
- the purchaser is able to offer any financier security over the shares in the target: although this is not the same as the financier getting direct rights against the assets of the target, it may be all that is available at least until a post-acquisition merger or other arrangement has been implemented (which may take some time).

In addition, a purchaser should look carefully at whether any existing debt owed to the seller can be refinanced from outside sources and whether it would be preferable for any working capital or other facilities needed by the target after the acquisition to be provided directly by the purchaser's financiers: normally it will be possible for the target to give security to financiers for its own direct borrowings without infringing the financial assistance rules.

The buyer must also take account of those rules inherent in most legal systems which require transactions to benefit the company. These rules usually come into the equation in relation to guarantees and security for debts and obligations of a parent company (upstream security).

Rules prohibiting financial assistance

	Rules apply to all limited liability companies	Rules expressly apply to financial assistance by subsidiaries	Principal statutory exemptions [1]
Belgium	Yes	No	Employee share purchases
France	Yes[2]	No	Employee share purchases
Germany	Yes[3]	Yes	None
Italy	Yes	No	None
Netherlands	Yes	Yes	A BV may grant loans to a purchaser of its shares up to the amount of the BV's freely distributable reserves
Spain	Yes	Yes	None
United Kingdom **See sidebar note on page 6**	Yes	Yes	A private company with a positive net worth or adequate distributable profits may provide financial assistance if directors can make a statutory declaration, supported by an auditor's report, as to the company's solvency

Notes
1. This table only addresses exemptions additional to those normally available for "public" type companies under the Second EC Company Law Directive, i.e. those for bank lending in the ordinary course of business and loans to assist the purchase of shares by employees.
2. A French SA is subject to rules modelled along the lines of those in the Second EC Company Law Directive. A French SARL is prohibited from lending to shareholders or managers or granting guarantees for the benefit of shareholders or managers, whether or not connected with a purchase of shares.
3. German law contains detailed provisions and extensive case law prohibiting the erosion of share capital by the provision of financial assistance to a purchaser. As in all countries, each transaction should be examined on a case-by-case basis.

Structuring the acquisition

Shares versus assets? A critical question at the outset of any transaction is whether to buy the shares in the target company or its assets. The table below sets out, in outline, a comparison of asset purchases and share purchases to draw attention to the principal factors. Some of the tax issues are dealt with in this paper.

Outline comparison of asset and share purchase

Asset purchase		Share purchase	
1	Mostly clear of inherited liabilities (exceptions include employee and environmental liability)	1	All liabilities pass with company (need for warranties)
2	Able to pick and choose assets to be purchased	2	All assets pass with company (unless stripped out pre-sale)
3	Existing trading agreements may not be transferable	3	Continuity of trading arrangements (absent change of control clauses)
4	Higher transfer taxes	4	Lower transfer taxes
5	No carry forward of tax losses	5	Past tax losses may be carried forward (absent change of control rules)
6	Step-up of capital values for capital gains and depreciation purposes (and adjustment of trading stock to current value)	6	No step-up/adjustment of book values available
7	Risk of double tax charges for owners of company	7	Sellers of shares only pay capital gains tax (if at all)
8	Purchaser's interest expenses may be offset directly against taxable income derived from assets purchased	8	Purchaser may not be able to offset interest expense against the company's taxable income (absent tax consolidation rules)
9	Purchaser can grant security to lenders over assets acquired	9	Financial assistance issues for purchaser

Clear of inherited liabilities

In a share purchase, a purchaser primarily relies on representations and warranties for protection against inherited liabilities. The key commercial reason purchasers cite for preferring to buy assets is to avoid inheriting the liabilities of the target business. However:

- all the principal Member States have implemented the EC Acquired Rights Directive, under which the employment contracts of, and associated liabilities to, employees transfer automatically to the purchaser when business assets are sold as a going concern.
- a purchaser of business assets may end up being responsible for the tax liabilities of the seller. France, Germany, Italy and Spain (and Belgium as from 10 January 1997) all have rules which make a purchaser of assets responsible for some, if not all, of the tax liabilities relating to the business. In addition, the tax authorities may have tax liens over the assets transferred.
- some countries have rules to protect general creditors on an asset sale. In Germany, the purchaser of substantially all of the assets of a company or individual becomes liable for the seller's debts and use of the seller's business name can mean taking responsibility for the liabilities of the business (unless this is expressly excluded in the sale agreement). In Italy, the purchaser of a business also becomes liable for all debts of the business on the books at the time of the transfer whatever the arrangements agreed between the parties. In France, the purchaser of a business does not directly become liable for the debts, but the sale must be publicly announced in accordance with strict procedures and creditors have certain rights to oppose the payment of the price or to make counter-offers for the business. The onerous nature of these procedures and the high transaction taxes on a sale of assets make asset purchases complex to organise in France.
- a purchaser may inherit a liability with an asset (e.g. environmental liabilities) or may need to discharge liabilities to protect an asset (e.g. leased assets) or to protect the goodwill of the business. Most countries also have laws protecting creditors of an insolvent seller who has attempted to sell assets at less than fair value.
- Taking your pick
- The purchaser may prefer not to take all the assets of the target company, which is one result of a share purchase. However, although an asset purchase permits some selection of assets, it can be a cumbersome procedure. The individual assets will need to be carefully defined and the formalities for the transfer of certain assets may be burdensome, in particular in continental Europe where it may be necessary to involve a notary (although in Belgium and France a transfer of a fonds de commerce may short-circuit some of these formalities).

Comparison of transaction taxes on asset purchases and purchases of unquoted shares

	Asset purchase[1]	Share purchase
Belgium	12.5% (real estate)	Nil[2]
France	11.40% (fixed assets and goodwill) (but lower rates apply to the portion of the price less than FF700,000) VAT (recoverable) charged on inventory, but no VAT if the total business is taken over by means of an asset deal	SA:1% (maximum FF 20,000)[3] SARL: 4.8%
Germany	2% (real estate) VAT (recoverable) charged on certain other assets	Nil[4]
Italy	3% (basic and on goodwill) 8% (other fixed assets)[5] 15% (agricultural real estate)[5]	0.14%[6]
Netherlands	6% (real estate)	Nil[7]
Spain	16% or 6%[8]	Nil[9]
United Kingdom	1% (except moveables) – property stamp duty is higher	0.5%

Notes

1. It is assumed that the asset sale constitutes the sale of a business as a going concern so as to fall within the relevant exemption from VAT permitted by the EC VAT Directive (where the Member State has adopted this exemption).
2. If the company is a Belgian real estate company, the 12.5% real estate transfer tax may apply.
3. It is possible to avoid the charge by not using a bilateral contract for sale or by signing the bilateral contract abroad.
4. Real estate transfer tax of 2% may be payable on an assessed value if the company owns real estate and the purchaser acquires 100% of the shares. Where shares in a GmbH are transferred ad valorem notarial fees are payable, although they may be reduced by use of a foreign notary.
5. A cadastral tax of 2% is also levied on the purchase of fixed assets and real estate in Italy.
6. Sales of shares in an SpA between non-residents transacted outside Italy are not subject to stamp duty. All legal documents executed in Italy must be drawn up on stamped paper (Lit 10,000 every four sheets).
7. The real estate transfer tax of 6% may be triggered by the sale of shares in a Dutch real estate company.
8. The transfer of assets is in principle subject to VAT at a rate of 16%. VAT may also be payable in certain cases instead of Transfer Tax (6% rate) on the transfer of real estate.
9. The transfer of shares in a Spanish real estate company will be subject to Transfer Tax at a rate of 6% (i) when the purchaser acquires control of it or (ii) when shares were issued in exchange for real estate and the transfer takes place within a year. In addition, there may be ad valorem notarial or other fees payable in connection with the transfer of shares in a Spanish company.

On an asset purchase, significant trading agreements (such as distribution and licence agreements) may not be transferable to a purchaser without the consent of the other parties. On a share purchase, existing trading arrangements continue unless they are subject to a break or change of control clause.

Transfer taxes

The transfer taxes applicable to asset and share purchases are summarised in the table on page 24. In most cases, the transaction costs of an asset purchase will be higher than those in a share purchase. In France and Italy, it may be possible to mitigate the high transfer taxes applicable to asset sales by "hiving down" the required assets by way of a capital contribution into a new company which is then sold to the purchaser.

The 'ideal' structure

There are likely to be many factors to be taken into account for any acquisition. However, in every transaction the ideal structure will seek to maximise the returns for all the parties. This means meeting the following, sometimes conflicting, objectives:

- minimising the tax paid by the seller on the deal;
- minimising capital duty payable on capitalisation;
- maximising relief for acquisition costs e.g.:
- by offsetting financing costs against taxable profits;
- by claiming full tax depreciation of the purchase price through stepping up asset values;
- maximising the efficiency of the extraction of profits e.g.:
- by preserving any tax benefits (such as carried forward losses or investment incentives) attached to the business;
- by minimising withholding taxes and corporate taxes on future cross-border interest, dividend and royalty flows;
- by creating a flexible structure so that any future restructuring (including internal reorganisations or sale of assets or shares) can be implemented at no or low tax cost
- minimising currency risks for the buyer.

Whatever the financial and tax objectives, the structure must also be squared with other commercial concerns. These may include the need for the target to be fitted into the buyer's existing group structure, which may be particularly difficult where the target's business crosses divisional boundaries. The buyer also has to assess whether the structure of the deal will have an impact on the post-acquisition management of the business, e.g. where employment terms have to be harmonised, where differences in the methods of distribution and supply have to be reconciled or where the inter-relationship between the target business and the seller (or the seller's group) needs to be unwound over a period of time.

Minimising the seller's taxes

An ideal structure will suit the seller as well as the buyer. The seller will want to maximise its net return from the sale. In some countries, there are very favourable tax regimes for individual sellers of shares. For example, in Belgium an individual seller of shares will be free of all tax so long as the purchaser sets up a Belgian company to effect the purchase and that company does not resell to a non-resident within 12 months. In The Netherlands, individuals will normally hold their shareholdings through a personal holding company that benefits from the participation exemption (so that tax can be deferred until the proceeds are distributed). In the UK, sellers may wish to defer taxation by accepting loan notes (or shares in the purchaser) in exchange for their shares.

The seller's tax concerns may often militate against an asset purchase even though other concerns might indicate that route. Generally, for individual sellers, an asset sale gives rise to two layers of tax: first, tax on the company when it sells the assets and secondly, tax on the shareholder when the proceeds are distributed to it. The combined level of tax will often significantly exceed the tax that would have been paid had the buyer bought shares instead.

Summary of capital gains taxation on the sale for cash of unquoted shares

	Resident corporate seller [1]	Resident individual seller [2]
Belgium	Nil if the shares are of a company subject to a normal tax regime	Nil if sale is to a Belgian company which retains the shares for at least 12 months: otherwise 16.5% but only if the seller and his family have held more than 25% of the company within the last five years
France	(1) 20.9% (including the exceptional contribution of 10%) on long term (2+ years) gains (2) 36.66% (including the exceptional contribution of 10%) on short term gains	Effective rate of 20.4% if the purchaser and his family have held more than 25% of the company within the last five years (otherwise only taxable if gains exceed specified threshold – in 1997 FF100,000 (about US$19,200)[3]
Germany	45% (retained profits) 30% (distributed profits)	Nil unless (a) seller holds (or has held within last five years) 25% of the share capital; or (b) shares acquired within last 6 months. Where gains are taxable, gains of less than DM 30m (about US$19.5m) on sales of shares representing more than 25% of the capital are taxed at half the average income tax rate (i.e. 26%). Taxable gains of more than DM 30m are taxed at the full income tax rate (53%)
Italy	53.2%	Nil if shares have been held for more than 15 years. Otherwise 25% of the gain (but in some circumstances seller may elect for reduced rate of 1.05% of the sale price where the transaction is executed before an authorised intermediary or notary and tax is paid at the time of the transaction)[4]
Netherlands	Nil if corporate seller benefits from "participation exemption" (has held more than 5% of the company since the start of the financial year)	25% if shares are part of a substantial interest (more than 5%) in the company held by the seller or his family during the last five years. Otherwise nil
Spain	35%	Shares acquired before 9 June 1996 are subject to a flat rate of 20% [5]. Shares acquired on or after 9 June 1996 are subject to a flat rate of 20% (where the shares have been held for more than 2 years)[6] and in any other case a progressive rate up to 56%.
United Kingdom	33%[7]	Progressive up to 40%[7] (annual exemption £6,000 (about US$0.01m))

Notes

1. The figures given for corporate sellers do not take account of lower rates that may be applicable to small companies (e.g. UK)
2. Assumes that the individual seller does not hold shares as a business asset, in which case, normally speaking, the special rules may not apply.
3. Special rules apply to sales of shares in French real estate companies.
4. The seller cannot elect for the reduced rate where the shares (a) have been held for more than 5 years or (b) the shareholding represents more than 5% of an unlisted SpA or 15% of an SrL. Where shares were acquired before 28 January 1991, the base cost for calculating the capital gain will be readjusted to the value on that date if the shares have been held for more than five years, the shares were acquired by inheritance or the shareholding falls below the percentage levels mentioned in (b) above. Special rules apply to gains in the year from 28 January 1991.
5. The base cost is adjusted by the relevant factor depending on the year of acquisition. The capital gain is also reduced by a specific percentage (depending on the nature of the asset) for each year for which the asset has been held up to 31 December 1996 (disregarding the first two years).
6. The first 200,000 ptas are exempt from tax.
7. UK capital gains tax may be deferred if the seller accepts loan notes or shares in place of cash.

Maximising relief for acquisition costs

Offsetting finance costs

A common route is for the buyer to set up a local holding company which borrows money to effect the acquisition. In a multi-jurisdictional transaction, this may mean the creation of multiple "mirror companies" to act as the acquisition vehicles for each of the companies in the target group. This will enable the purchaser to take advantage of any local rules on tax consolidation (or equivalent "fiscal unity" rules) to offset the interest expense on the borrowings against the profits of the target company. Tax consolidation rules (or a functional equivalent) exist in France, Germany, The Netherlands, Spain and the UK but are not available in Belgium or Italy. In those countries a "two step" acquisition may be the answer (see 3.4); however as from 1 January 1997, anti-abuse provisions restricting interest deductions for such intermediate holding companies apply in The Netherlands.

The leveraging up of a local acquisition vehicle can cause problems:

- it may infringe "thin capitalisation" rules or minimum debt:equity ratio requirements. For example, in Germany, Spain and the UK, the taxation authorities will look at the level of related party debt funding of a local subsidiary. Subject to any available tax treaty, this may lead to a denial of tax deductions for interest expenses and the re-characterisation of interest expenses as dividends for withholding and other tax purposes.
- interest paid to non-residents may be subject to local withholding taxes which may reduce the benefits of obtaining the local tax deduction.

Where acquisition debt has to be incurred in a foreign parent, there may be ways to "push down" the debt to local subsidiaries after the acquisition so as to offset the interest expense against local operating profits (subject to any rules against giving financial assistance). For example:

- the local subsidiary might borrow money and on-lend the proceeds to the parent to refinance the acquisition debt – but even if the loan is interest free the subsidiary may be deemed to be generating interest income which is subject to local tax.
- the local subsidiary might borrow money to fund a dividend to the parent company (which it can then use to pay off the acquisition finance) – but there may be withholding taxes to pay on the dividend flow and the parent may suffer tax in its own jurisdiction on the dividend income in the absence of exemptions or reliefs (e.g. the Dutch participation exemption).
- the parent company could sell an asset or business to the acquired subsidiary which funds the payment of the purchase price with local debt – but the parent may suffer tax on capital gains on the disposal unless there are exemptions or reliefs which can be used to shelter the gain (e.g. the Dutch participation exemption).
- the subsidiary could borrow money to invest in the equity of an offshore affiliate which lends the proceeds to the parent – this more complex route has been used in a number of highly leveraged transactions.

Stepping-up asset values

Where there is an acquisition of assets of the business rather than shares, the purchase price can be allocated to the various assets (although there can be considerable disagreement with the tax authorities as to the method of allocation). Generally, the allocated portion of the purchase price can be treated as the basis for depreciation or amortisation for tax purposes and as the base cost for capital gains tax purposes on a subsequent disposal. Where the allocated value exceeds the seller's historical cost, this can enhance the tax savings from depreciation or amortisation and reduce the capital gains tax payable on a subsequent disposal. There may also be an incentive to make a greater allocation to trading stock as this may reduce future taxable trading profits.

Only a few countries (such as Italy, The Netherlands and Spain) allow a tax deduction for the amortisation costs of goodwill, intellectual property and other intangibles. This may be an incentive to allocate as much as possible of the purchase price to the tangible assets acquired. Techniques have also been developed involving the sale and lease-back of intangibles to and from entities located in jurisdictions which allow amortisation of intangibles or have low tax rates.

In some countries the gain on a sale of intangibles may be exempt from tax and this technique can realise a tax-free step-up of the assets acquired.

In an acquisition of shares, the purchase price for the shares may exceed the book value of the underlying assets. Generally, it will not be possible to step-up the book value of the underlying assets to reflect the purchase price. However, some countries, such as Italy, allow a step-up to be achieved through a tax-free merger (by absorption) of the target with a local intermediary holding company or a liquidation of the target.

Maximising the efficiency of the extraction of profit

Preserving tax loss carry-forwards

A number of countries limit the utilisation of tax loss carry-forwards to reduce corporate taxes after a change of control. This prevents companies being bought for the benefit of their tax losses. For example, tax losses may be forfeited in The Netherlands if there is a change of control linked to a cessation of the trade and in the UK if there is a major change in the business before or after the change of control. In France and Belgium, a material change in the company's activities may lead to the disallowance of tax losses. In Spain, tax losses are reduced if a related entity acquires control linked to a cessation of business prior to the change of control.

Minimising withholding taxes

Every cross-border structure should be set up to minimise taxes which are levied on items of income that flow through the structure up to the shareholders. It should allow excess funds available in one company to be transmitted to another company (by way of a loan or otherwise) in a tax-effective manner.

Most countries impose withholding taxes on dividends, interest and royalties. These taxes are expressed as a percentage of gross amounts paid and ignore the fact that the recipient may have incurred substantial costs in earning such gross income and that its net profit may be much lower than the gross amounts. Even if the withholding tax can be credited against the recipient's corporate income tax liability (which is not always the case), this leads to double taxation. As with interest, the flow of dividends and royalties can be routed through entities which can claim protection under tax treaties against the imposition of withholding taxes. The most common example is the use of Dutch holding and finance companies.

Following the implementation of the so-called "Parent-Subsidiary Directive", intra-EC flows of dividends are generally free of withholding tax provided the parent-subsidiary relationship persists for two years. This makes The Netherlands an attractive base for a regional holding company, as a Dutch company will be able to receive dividends from other EC companies free of withholding tax, and then remit those dividends to an offshore parent through the Dutch treaty network (which generally reduces the rate of withholding tax to 5%).

Where remitting dividends or interest could lead to inefficiency, there may be scope for using cross-border royalty or management charges. Transfer pricing restrictions usually mean that these have to be charged on an arm's-length basis, but structures can be found to ensure that charges can properly be made, e.g. by separately acquiring any intellectual property rights through a foreign acquisition vehicle.

Minimising corporate taxes

Most countries give double taxation relief for distributed profits which have already been taxed in another jurisdiction. This can either be done by exempting the dividend income from tax altogether (as in The Netherlands in cases where the participation exemption applies) or by giving a credit to be set off against the recipient's corporate income tax liability (as in Spain and the UK). The credit method of relief creates an incentive for the parent to defer distribution of profits earned by subsidiaries in low tax jurisdictions for as long as possible but both systems encourage companies to divert capital and income to low tax jurisdictions. To combat this, many countries (including France, Germany, Spain and the UK) have introduced "controlled foreign corporation" legislation under which income earned in "tax haven" countries and certain sources of passive income (e.g. dividends, interest and royalties) can be taxed in the parent's home country even if not actually distributed.

Sometimes, a structure cannot be reorganised to avoid these problems (e.g. because stripping out subsidiaries would crystallise capital gains taxes). It may be possible for an ultimate parent company directly to tap into the profits of an indirect subsidiary through the creation of a special class of "income access shares" which enable dividends to by-pass an existing corporate structure. Such a route may be particularly attractive to buyers who find that the foreign target company has a subsidiary in the buyer's home jurisdiction.

Flexibility

The new structure should provide maximum flexibility to allow future restructurings, spin-offs and so on. Often a holding company is formed which acquires the shares of the target companies either directly or through local intermediary holding companies. The holding company can be established in a country which exempts from corporate income tax any gain realised on the sale of the shares of the holding company's subsidiaries. This gives flexibility for a tax-free resale of all or some of the target companies or a tax-free transfer of a target company to another member of the group.

The Netherlands is often selected as the location for the holding company. The Dutch "participation exemption" means that capital gains (and dividends) on shareholdings in qualifying subsidiaries are exempted from Dutch corporate income tax. In addition, locating in The Netherlands gives access to The Netherlands tax treaty network which may help not only with withholding tax problems but also with countries (such as Spain) which tax the capital gain made by a non-resident on a sale of shares in a domestic company. Spain may tax such capital gains when the main asset of the domestic company is real property located in Spain.

Minimising currency risks

A purchaser will want to minimise currency exposures by matching local currency finance to local currency income. The gradual elimination of exchange control restrictions throughout Europe has made this matching process easier.

Weighing the options

Sellers (in particular individual as opposed to corporate sellers) usually want to sell shares (to avoid double tax charges as well as the uncertainty and inconvenience of liquidating the target). Purchasers may prefer to buy assets to benefit from the ability to take clear of inherited corporate liabilities, the step up of book values or the ability to grant security over assets. In practice, however, throughout Europe, share sales tend to predominate over asset sales, in part because many of the purchaser's objectives can often be met in other ways.

Employee consultation

Many continental European countries require companies with a specific number of employees to establish a workers' council or committee to represent the employees in their dealings with management. The powers of such councils vary from country to country but, generally speaking, they will have to be consulted on major changes affecting the workforce, such as dismissal programmes or major reorganisations of working practices. In addition, where the target has recognised a union for collective bargaining purposes, the union may have to be consulted on such matters. In The Netherlands, this will be the case whether or not the target has recognised a union.

Of more immediate concern to a purchaser, however, will be whether the workers' representatives have to be notified or consulted prior to completion of the acquisition (in particular where confidentiality is a concern) and whether the workers' council has any power of veto over the transaction. The table opposite indicates the legal requirements for establishing a workers' council in the principal EC countries and summarises the requirements to notify or consult with such a council where there is a change in control of the company.

Employee consultation requirements in an acquisition of shares

	Workers' council or committee required	Acquisition required to be notified to workers' council
Belgium	If more than 100 employees	Workers' council must be consulted prior to signing or public announcement of acquisition and its views made available to shareholders
France	Normally if 50 employees or more	Workers' committee must be consulted prior to signing
Germany	If 5 employees or more Economic committee is also required if 100 employees or more	Works council (and economic committee, if any) must be informed of the transaction at the latest immediately after binding contracts are signed.
Italy	No	Employee notification/consultation generally not mandatory, but may be required under collective agreement with unions
Netherlands	If more than 35 employees	Where there are more than 100 employees and a works' council, unions must be consulted at an early stage and the works' council must be notified of a proposed change of control (and has powers to suspend or even block the transaction)
Spain	If more than 50 employees	No legal requirement to notify or consult
United Kingdom	No	No legal requirement to notify or consult

Notes

1. In The Netherlands, the workers' council in larger enterprises must be consulted prior to final agreement being reached on a proposed change of control. In addition (unlike in other countries), the workers' council has a limited power to suspend or even block the transaction through an application to the court.
2. Under Chapter II of the Dutch Merger Code (which is not legally binding but is expected to be observed) trade unions must also be notified of a change of control at the stage where agreement is likely to be reached between the parties involved. This may be at a relatively early stage in the negotiations, even before the main terms (such as the price) have been agreed.
3. Similarly, in France, the timing and scope of consultation with the workers' committee can be an area of concern for both the buyer and the seller. It is generally considered that consultation is to take place before signing.
4. In Italy, there is no consultation requirement but it may still be advisable to consult with employees, particularly senior employees. The collective bargaining agreement applicable to executives of industrial enterprises gives them the right to resign within six months of a change in control and the right to compensation equal to one-third of the amount that would have applied if they had been dismissed.
5. Spanish labour law also gives senior executives the right to resign and claim compensation within three months of a change in control where there is also a significant change in the governing body of the company or a substantial change in the nature of the executive's activities.
6. In Belgium, the acquisition of one-third or more of the capital of a Belgian company whose net assets exceed BF 100m (approximately US$2.8m) must be notified to the regional Ministries of Finance, Economic Affairs and Regional Development. There is no power of veto and the notification is merely to allow the Ministries to assess the possible employment repercussions of the transaction. Notification should also be made to the local social security office.

The EC Works Council Directive was required to be implemented in all Member States by 22 September 1996 (other than the UK where it does not apply because of the UK "opt out" from the EC social chapter). This Directive requires companies to establish procedures for the consultation of employees or the establishment of European works councils where a company (or group) employs more than 1000 employees in Europe and at least 150 employees in at least two Member States (excluding the UK). Implementing legislation is still being finalised in a number of Member States although it is likely that it will be necessary to consult with any European works council on a proposed acquisition.

If the transaction is structured as an acquisition of business assets, the EU Acquired Rights Directive will require prior consultations with union representatives, in addition to any required consultation with workers' councils.

Completion

The agreement will address the manner of completion (closing) of the sale of shares in some detail but the detailed mechanics of completion will depend on the legal nature of the shares in the target being transferred:

- In the UK, shares will usually be in registered form and the transfer of title takes place by way of the delivery of a properly executed instrument of transfer, and the share certificate, which is prima facie evidence of title, followed by registration of the transfer in the company books of the target (which normally will require the passing of a board resolution of the target, at least if the target is a private limited company). A similar procedure applies to shares in a French SA or an Italian SpA where the certificates (or receipts) are delivered to the purchaser with a signed ordre de mouvement (France) or girata (Italy) and the transfer is then registered in the books of the company. Similar procedures apply where shares in a Belgian SA/NV, a Dutch NV or a German AG are in registered form.
- Where the shares take the form of bearer shares (as would be common for a Belgian SA/NV, a Dutch NV or a German AG) it will normally be sufficient for the seller to deliver the physical share certificate at completion, although in Germany for example constructive delivery may take place instead where the shares are held in safe custody with a bank.
- In a Belgian SPRL/BVBA, a French SARL, a German GmbH, an Italian SrL, a Dutch BV and a Spanish SRL there are no share certificates as such and the shares are transferred by a deed of transfer, which in Germany, The Netherlands and Spain must be notarised. A transfer of the shares in the capital of such a company may also have to be registered in the books of the company (eg in the case of an Italian SRL).
- Notarial or similar requirements may apply to other types of company. For example, in Italy registered shares in an SpA are transferred by endorsement of the certificates before a notary or an authorised Italian bank followed by registration with the company. In Spain, the transfer of bearer shares in a SA must be formalised before a notary or a sociedad de valores or an agencia de valores (stockbroker). Where there are notarial or other similar requirements this can mean that completion must take place locally. The requirement for a local completion may be reinforced by rules (such as those in Italy and Spain) requiring the remittance of funds to local vendors through an authorised bank, or practical concerns such as those resulting from the security risks of moving bearer share certificates. This may cause practical problems in a multi-jurisdictional transaction.
- The manner of settlement of the purchase price will also depend on local practice. Although telegraphic transfer is the usual preferred method of settlement, in Spain certified bank cheques are commonly used and in the UK settlement may be by means of physical delivery of a banker's draft at completion.

In some cases it will be necessary to hold a board meeting of the target at completion for the purpose of registration of the transfer of shares. In the case of transfers of shares in a Belgian SPRL/BVBA, French SARL, German GmbH, Italian SrL or Spanish SRL, it will also usually be necessary to hold a shareholders' meeting to waive pre-emption rights or other restrictions on transfer. In some countries, these meetings cannot be held abroad, which can cause difficulties in an international transaction.

In addition, where the local law requires a company to have more than one shareholder (or, as in France, requires directors to hold qualification shares), the purchaser will have to nominate companies or individuals as additional shareholders to meet these requirements. In continental Europe this will often be done by nominating a director to take one of the shares and taking an option to acquire that share (and deposit of the share certificates and a blank instrument of transfer).

As well as the mechanics for passing title to the shares to the purchaser, the sale and purchase agreement will also usually contain provisions to ensure that the purchaser obtains practical control of the target at completion. In most cases, this will involve obtaining resignations from outgoing directors and other company officers (coupled with waivers of claims for loss of office). In the absence of such resignations the purchaser may not be able to remove unwanted officers before the expiration of their term of office. The purchaser will also want to ensure that the outgoing shareholders hold a shareholders' meeting to appoint the purchaser's nominees to the board (in the UK this can generally be done by the outgoing directors instead). Where there is a two-tier board the question of the removal and replacement of company officers is more complex. For example, in Germany, worker representatives on the board cannot be replaced by shareholders and in The Netherlands the supervisory board of a *structuurvennootschap* is self-perpetuating and employees may have certain rights to object to proposed appointees.

In addition, the purchaser may want key directors or staff to sign revised employment contracts at completion. To the extent these are aimed at tying up key personnel by fixed term contracts, long periods of notice or post-termination restrictions on competition, their effect may be limited by local rules which entitle an employee to resign on relatively short notice periods or which require a separate payment for a non-compete obligation (as in France and Spain). In France, the maximum number of directors who are also employees of the company is limited to one-third of the board.

The completion mechanics should also address any steps necessary to unwind existing links between the target company and the seller (e.g. the repayment of debts owing between the target and the seller and the release of guarantees given by the seller for the target). However, where there are assets or facilities shared by the seller and the target (e.g. premises, accounting systems or distribution arrangements), it may not be practical to deal with these at completion. There may need to be transitional arrangements to allow a period of gradual disengagement after completion of the sale.

Representations and warranties

In a typical Anglo-Saxon style transaction, the buyer will receive the benefit of extensive representations and warranties. It is commonly said that, in contrast, these are unnecessary in continental Europe because the codified systems of law provide a satisfactory alternative framework. However, in practice, while civil codes do provide some measure of implied protection to a purchaser as to the title to the shares being transferred, the degree of protection conferred on a purchaser regarding hidden liabilities of the target (or other similar matters) is limited and, more importantly, unclear. As a practical matter, purchasers are usually advised to assume that, in the absence of express representations and warranties, they will have few remedies against a seller of shares if the company turns out badly – ie caveat emptor (let the buyer beware).

Corporate law rules relevant to completion requirements on a share purchase

Types of share			Minimum no of shareholders	Notarial or other intervention required to effect transfer	Transaction taxes or stamp duties
Belgium	SA/NV	Registered or bearer	2	No	Nil
	SPRL/ BVBA	(Parts sociales) not represented by share certificates	2 (1 if an individual)	No	Nil
France	SA	Registered only (for privately held companies)	7 (and a director must hold one or several qualification shares, as provided in the company's by-laws)	No	1% (max FF20,000)
	SARL	(Parts sociales) not represented by share certificates	2 (1 shareholder permitted for EURL)	No	4.8%
Germany	AG	Registered or bearer shares	1[1]	No	Nil[2]
	GmbH	(Geschäftsanteil) not represented by share certificates	1	Yes (notary)	Notarial fees[2]
Italy	SpA	Registered only	2 (when incorporated)	Yes (notary or authorised Italian bank)	0.14%[3]
	SrL	(Quote) not represented by share certificates	2 (when incorporated)	No	0.14%[3]
Netherlands	NV	Registered or bearer	1	No for bearer shares Yes for registered shares (with limited exceptions)	Nil
	BV	Registered only (not represented by share certificates)	1	Yes	Nil
Spain	SA	Registered or bearer[4]	1	Yes in the case of bearer shares (notary, stockbroker or a sociedad de valores)	Notarial or broker fees[5]
	SRL	(Participaciones) not represented by share certificates	1	Yes (notary)	Notarial fees[5]
United Kingdom	plc	Registered only[6]	2	No	0.5%
	Ltd	Registered only	1	No	0.5%

Notes

1. At least five shareholders must form a German AG, but after formation the number of shareholders may be reduced to o.
2. Real estate transfer tax of 2% may be payable on an assessed value if the company owns real estate and the purchaser acquires 100% of the shares.
3. Sales of shares in an SpA between non-residents transacted outside Italy are not subject to stamp duty. All legal documents executed in Italy must be drawn up on stamped paper (Lit 10,000 every four sheets).
4. Spanish SAs in certain industries (banking, pharmaceutical, air transport and newspapers) may only issue registered shares.
5. Real estate transfer tax at the rate of 7% may be payable where shares in a Spanish real estate company are transferred or where the shares were issued in exchange for real estate.
6. A UK plc may issue share warrants to bearer which are similar to bearer shares, but this is rarely done in practice.

As a result, the giving of representations and warranties has become increasingly standard practice throughout Europe although the length of the warranties given (and thus the degree of protection conferred) tends to remain somewhat more limited than the typical Anglo-Saxon model. While every transaction is different, the table opposite sets out a brief checklist of key representations and warranties for inclusion in a typical sale and purchase agreement.

In addition, continental European warranties tend to be drafted in more general terms and may force fewer disclosures from the seller than the typical US or UK agreement. To the extent that detailed disclosures are required to qualify warranties given, this will tend to be done the US way, by annexing disclosures referred to in the warranties, rather than by the UK model of a separate disclosure letter. Purchasers may have to rely to a greater extent on their own due diligence investigations. They may also want to seek additional comfort by means of a completion audit as well as security for potential warranty claims either through retaining part of the purchase price for an agreed period (or placing it in escrow) or, in particular in continental Europe, through bank guarantees for the seller's warranty obligations. In The Netherlands, the courts have held that a purchaser may not in all circumstances rely on warranties where extensive due diligence has been carried out.

In the UK, the buyer usually gets protection against taxation liabilities by a separate deed of tax indemnity, in addition to detailed tax representations and warranties. Elsewhere in Europe the seller would normally only be asked to give representations and warranties regarding the company's tax liabilities, although this may be coupled with indemnity wording which achieves a similar result.

Where representations and warranties are given there will normally be a significant degree of negotiation as to the limits on the seller's liabilities. The seller will usually seek to negotiate a cap on the total amount of claims (and provisions restricting the bringing of small claims) as well as limits on the time within which any claims must be brought. It is conventional practice in most countries to distinguish between the time limits for claims under the commercial warranties and the time limits for claims under the tax warranties (which will often be tied to the statutory limitation periods on the tax authorities – usually between five and six years). In some countries, the statutory limitation period for bringing a claim under representations and warranties may be so short as to be unacceptable to the buyer. In that case, the only solution may be to agree an alternative governing law.

Checklist of key representations and warranties

- Title to shares purchased;
- Share capital structure of target company
  - what it is;
  - no options or conversion rights;
- Audited accounts accurate and provide for all liabilities;
- Since last audited accounts
  - business carried on in ordinary course;
  - no material adverse change;
- Liability items
  - borrowings;
  - tax position;
  - pensions;
  - environmental risks;
  - contingent liabilities;
  - litigation/disputes;
- Asset items
  - title to assets;
  - real property, intellectual property, etc.;
- Trading and business items
  - details of material contracts;
  - details of employees and terms of employment;
  - related party transactions/arrangements;
- All information supplied accurate/all material facts disclosed.

Further Information

Particular attention is drawn to the sidebar note on page 1 as to the use of information provided in this publication.

This guide is for general interest - it is always essential to take advice on specific issues. We believe that the facts are correct as at the date of publication, but there may be certain errors and omissions for which we cannot be responsible.

If you would like to receive further information about this subject or other publications, please call us – see our contact details on the next page.

References:

[1] This publication was inspired by Clifford Chance (who kindly allowed us to reproduce sections of their publication on this subject), a multi-jurisdictional law firm handling all aspects of business and finance. Their lawyers operate internationally and domestically under common law and civil law systems. They provide a full range of legal service from their offices in 24 major business and financial centres around the world. They may be contacted at 200 Aldersgate Street, London EC1A 4JJ, United Kingdom, Tel: +44 (0) 207 600 1000, Fax: +44 (0) 207 600 5555 or by e-mail to info@cliffordchance.com
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