Corporate Finance/M&A - France

New Law Implements Cross-Border Mergers Directive

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Introduction

Over six months late, and after receiving a reminder from the European Commission, France has finally transposed into law the EU Cross-Border Mergers Directive (2005/56/EC). This update considers the obstacles encountered in the transposition of the directive and the questions they raise.

The Law on the Adaptation of Corporate Law to EU Law (649/2008) was published in the *Official Gazette* on July 4 2008. The law is principally aimed at transposing EU Directives 2005/56/EC(1) and 2006/46/EC.(2) The law also includes measures regarding European cooperative entities.

The publication of Bill AN/41 on November 14 2007 ignited a debate which covered:

- the complex and unclear procedure for dealing with the employment aspects of cross-border mergers;
- the need for changes to the Commercial Code, which still includes clauses that contradict the aims of the Cross-Border Mergers Directive; and
- the need for a French notary to attest to the legality of a cross-border merger.

France failed to meet the December 15 2007 deadline for transposition and the delay was partly due to the debate on these points.

Participation Agreements

Articles 3 and 4 of the law pertain to the participation of employees in companies involved in cross-border mergers. The concept of 'participation' as used in the directive means the right of employees to elect representatives to the supervisory or administrative body of the company, much along the lines of the German model of co-determination.(3)

The requirement to establish an employee participation arrangement in the acquiring company can prolong and complicate the merger process. However, the relevant party need not negotiate a participation agreement with employees unless: (i) at least one of the companies participating in the merger applies rules on participation and had a workforce of at least 500 employees during the six months preceding the announcement of the merger; and (ii) the company created by the cross-border merger does not guarantee the same level of employee participation as the acquired company.

Given the complexity of the negotiation procedure, it is expected that French companies will not often acquire and absorb foreign companies which have an employee participation regime. However, mergers between two companies without participation regimes will remain fairly straightforward.

Amending the Commercial Code

One point seems to have been overlooked in the re-examination of the code, despite the fact that it was included among the revisions required for the adoption of the European company statute in 2005 (in the transposition of EU Directive 2001/86/EC). This outstanding issue is the need for the shareholders of a

French company unanimously to approve a merger operation in which the company is absorbed by a company from another EU member state. Such an operation could be seen as the equivalent of a change in the company's nationality; if this view is upheld, Article L223-30 of the code is relevant, as it requires a limited liability company's shareholders to approve such a change unanimously. Furthermore, the combination of Articles L236-5 (on the need for unanimous approval of an operation which may increase shareholders' obligations) and L225-97 (on changes of nationality) imposes the same requirement in the case of limited stock companies.

This omission in the new French law will effectively limit cross-border merger operations in which the French company is absorbed as part of an intra-group operation. Such operations may prove impossible for French companies with numerous shareholders, each of which could potentially veto the transaction. The omission is particularly unfortunate as provisions were added to the code (in connection with the transposition of the EU company directives) which allow for a supermajority vote on the creation of a European company and impose a share buy-back obligation. A similar provision could have been inserted for cross-border mergers in order to avoid the unanimity hurdle.

Role of French Notaries

During the parliamentary debates on the bill, numerous amendments were filed that questioned the role of French notaries in cross-border mergers; many experts felt that having a French notary verify the legality of the merger was inappropriate. The minister of justice maintained that a notary should be given this responsibility, but failed to explain her reasons. Article L236-60 of the code now provides that:

"*a notary, or the clerk of the court at which the surviving entity will be registered, must verify the legality of the merger and of the creation of the new company resulting from the merger within a fixed period set by a decree verified by the Council of State.*"

Consequently, two officials now have the authority to confirm the legality of a merger: a French notary and the clerk of the commercial court. The details of how this verification will be accomplished remain undecided. A notary or clerk who reviews the merger's legality in France will have to establish whether the foreign absorbed company has an employee participation regime and the procedures in France will vary accordingly. In seeking to establish this fact, the clerk or notary will likely have to rely on the opinion of a legal professional in the country in which the company is based. This system was in operation before the adoption of the new law: when a French company was absorbed, a foreign notary charged with verifying the legality of the merger would request an opinion under French law in order to ensure that the French company did not have an employee participation regime (as defined in the directive) and that the required steps for a merger under French law had been carried out.

Given the need to rely on foreign legal opinions, parties to a merger may prefer to choose a notary to verify the validity of the merger, as a French notary will likely be willing to rely on the opinion of a foreign colleague, whereas a commercial court clerk may be more reluctant.

The intervention of a French notary or court clerk for this purpose will not be required unless the company being absorbed is French; otherwise, a French court clerk need only deliver a certificate to confirm that the necessary documents (ie, the merger agreement and a report of the statutory merger appraisal) have been duly filed and that the correct notifications have been published. The completion of the merger will be carried out by an extraordinary shareholders' meeting of the foreign absorbing company, the legality of which will inevitably be a matter of foreign law. The verification of this key step will generally be accomplished by a foreign notary.

In practice, parties to a cross-border merger will attempt to draft a merger agreement that satisfies all the conditions for a merger under the laws of both countries involved. For example, where a French company is absorbed by a Dutch company, the merger agreement will usually follow the French model, as this is typically more extensive than a Dutch merger agreement and the Dutch notary will generally find in the French document all the elements required for a merger under Dutch law. Unlike French law, the laws of certain countries do not require the intervention of a statutory appraiser in the merger, allowing shareholders to determine the valuation of the assets and liabilities transferred to the absorbing company as a result of the merger. Nevertheless, before the adoption of the new law, in cross-border mergers the intervention of a French statutory appraiser was obligatory even when the laws of the absorbing company did not require it - in other words, both French and foreign requirements had to be applied. The new law on cross-border mergers appears not to have changed this cumulative approach.

Comment

Before the new law was adopted, cross-border mergers were possible under existing French corporate law

by virtue of the European Court of Justice's decision in *SEVIC*.(4) The new law provides for a new system for cross-border mergers, certain details of which will not be known until the French government has issued the required decrees.

Does this mean that mergers can no longer be carried out under the old method and that merging parties must wait for the decrees before implementing a new cross-border merger? Many months may elapse before the necessary implementing decrees are issued. However, the absorption of a foreign company by a French company may be difficult to implement until a decree defines the terms of the necessary verification by a French notary or court clerk. Moreover, a notary or clerk will hesitate to rule on the validity of a merger before knowing the rules that apply to such a verification. Will a similar reluctance hinder the absorption of a French company by a foreign company? Such mergers are less dependent on French law and seem simpler to implement. However, the new French law requires a court clerk to issue a special attestation to confirm that the necessary formalities of the merger have been completed in France,(5) and until the decree is published, clerks may hesitate to issue such a certificate.

However, insofar as EU law allows for the completion of cross-border mergers, the fact that French implementing decrees have not been issued cannot be seen as an obstacle to cross-border mergers in France, at least in theory. *SEVIC* established that it is illegal for a clerk to refuse to issue a certificate for a cross-border merger on the grounds that the relevant decree has not yet been adopted.(6) It is hoped that the required implementing decrees will be published soon, which would avoid a difficult situation for notaries and court clerks who are asked to verify the legality of a cross-border merger.

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Endnotes

(1) Dir Cons 2005/56, October 26 2005, *Official Journal of the European Union*, November 25 2005, L310; See Menjuck, *Les Fusions Transfrontalières des Sociétés de Capitaux*, RLDA 2006/5, 228.

(2) Dir Cons EC 2006/46, June 14 2006, *Official Journal of the European Union* August 16 2006, L224, August 16 2006, L224.

(3) Compare C trav, Article L2351-6 and Dir Cons EC 2001/86, October 8 2001, Article 2(k).

(4) C-411/03, December 13 2005.

(5) Article L236-29.

(6) See also the Court of Amsterdam's ruling in *Consuma Holding BV* on January 29 2007.

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