Austria
Financial Assistance
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INTRODUCTION

This guide sets out an overview of the rules on financial assistance in Austria in connection with:

- limited liability companies (GmbH);
- limited partnerships with limited liability companies or stock corporations as only unlimited partners (GmbH & Co KG or AG & Co KG); and
- stock corporations (AG).

GENERAL OVERVIEW

Which laws and regulations apply to financial assistance under Austrian law?

Under section 82 of the Austrian Act on Limited Companies (GmbHG), shareholders are not permitted to reclaim their contributions. For stock corporations, the equivalent law is section 52 of the Austrian Stock Corporation Act (AktG), which prohibits unlawful repayment of capital. Pursuant to section 66a of AktG, a target company is prohibited from financing, or providing assistance in the financing, of the acquisition of its own shares.

The rules relating to GmbHs are also applicable to limited partnerships where only limited liability companies or stock corporations act as unlimited partners, ie GmbH & Co KGs and AG & Co KGs.

Any financial assistance by a GmbH, AG or GmbH & Co KG/AG & Co KG for the acquisition of shares in such company generally results in a violation of the capital maintenance rules. In addition to the statutory provisions, Austrian courts have rendered precedents and scholarly articles provide guidance, setting the framework for financial assistance.

Financial assistance rules also play a role, particularly in the context of:

- acquisition financing transactions;
- leveraged transactions;
- group financings; and
- cash pooling arrangements within groups of companies.

What should be understood as unlawful financial assistance under Austrian law?

Austrian law does not allow repayment of capital to shareholders of GmbHs, GmbH & Co KGs/AG & Co KGs and AGs. Shareholders are only entitled to:

- dividends – ie, distribution of the net balance sheet profits of the company;
- funds and assets received in a formal capital reduction;
- liquidation surplus, subject to creditor protection provisions; and
- considerations received in arm's length transactions with the company.

Payments and benefits not within the scope of these rules will be qualified as a violation of Austrian capital maintenance rules and will result in the invalidity of the respective transaction.

FINANCIAL ASSISTANCE TO LIMITED COMPANIES AND STOCK CORPORATIONS

What qualifies as lawful financial assistance?

Shareholders can – and will, particularly in the context of acquisition financing – pledge their shares in the target company, and pledge or assign their claims to dividends and claims under the transaction documentation (eg claims for breach of representations and warranties). Upstream or cross-stream guarantees are possible when limited to the dividend amount.

The pledge over assets of a GmbH or AG (or partnerships where a GmbH or AG is the sole unlimited partner), to the benefit of banks and other lenders financing the direct or indirect acquisition of the pledging company or corporation, is subject to the limitations set by the capital maintenance rules. In practice, such pledges (or upstream and cross-stream guarantees not limited to the amount of dividends) are permissible only in narrow circumstances (see below).

Are there any exceptions to the capital maintenance rules for granting a security interest in the context of acquisition financing?

Austrian courts have developed certain requirements under which the pledging of the assets of the target and the granting of upstream and cross-stream guarantees may be deemed not to violate the capital maintenance requirements.

Pledges, guarantees, sureties, mortgages or other securities granted by the target to the financing banks or other lenders can be compliant with the capital maintenance rules if:

- the target receives adequate (ie, arm's length) consideration – case law and legal literature have developed criteria to determine adequacy depending on the financial situation of the lender and the expected (future) profitability of the Austrian target;
- the management of the target has undertaken a due assessment on borrowers' capability to repay funds; and
- the creation of the security interest is in the interest of the Austrian company (corporate benefit) (eg, the target receives certain funds originating from the acquisition financing to repay its own debts).

CONSEQUENCES OF PROVIDING FINANCIAL ASSISTANCE

Financial assistance provided outside the limits of the rules on capital maintenance, as interpreted by the courts, will be considered a violation of mandatory law. The transaction will be rendered (partially) null and void.

Legal consequences of violation of the capital maintenance rules

Since the transaction in violation of capital maintenance rules is considered (partially) null and void, the company can reclaim any payments made to direct or indirect shareholders and sister companies which are qualified as unlawful repayment of share capital. It can also claim related damages *inter alia* as a result of negative tax consequences.

The shareholders of a stock corporation will become directly liable to the creditors for the amount received and, in certain circumstances, the shareholders of a limited liability company can be held liable for the amounts received by other shareholders.

Finally, the transaction will be held void also towards third parties, particularly towards financing banks, if these third parties have or should have had knowledge (gross negligence required) of the violation of the capital maintenance rules.

Directors‘ liability

The managing directors or board members could be held liable for:

- having acted negligently in the context of having permitted payments later deemed in

violation of capital maintenance rules to shareholders;
- for having allowed the taking of security;
- for having made incorrect statements towards the companies; or
- having prepared incorrect financial statements.

OTHER RELATED MATTERS

Merging a leveraged acquisition vehicle with the target company

To be able to use the target company's assets as security for acquisition financing, it has been customary in the past to merge the target company into the acquisition vehicle (a special purpose vehicle or SPV). Thus, after a merger, the surviving company could pledge its own assets for its own (acquisition) debt without violating capital maintenance rules.

For years, market and court practice was that such a merger of the acquisition vehicle with the target company was not be permissible in the case of a downstream merger: the parent company's (acquisition vehicle's) shareholding in the target would be disregarded for purposes of calculation of the parent company's positive fair market value, An upstream merger was permissible, however.

In recent years, Supreme Court precedent has changed so that any merger (whether downstream or upstream) between an acquisition vehicle and the target is prohibited as long as any debt from the acquisition financing is outstanding. Therefore, the merger route is no longer available to use the target's assets for securing liabilities under acquisition financing.