Lithuania

Financial Assistance

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INTRODUCTION

This guide provides a concise overview of the rules applicable to financial assistance under Lithuanian laws in connection with closely held limited liability companies (*uždaroji akcinė bendrovė* or UAB) and widely held limited liability companies (*akcinė bendrovė* or AB).

FINANCIAL ASSISTANCE UNDER LITHUANIAN LAW

Overview

In Lithuania, it is generally prohibited for companies to provide financial assistance to acquire their own shares. The prohibition applies to both public and private companies. The statutory wording comes from the Second Company Law Directive 77/91, which prohibits companies from advancing funds, making loans or providing security with a view to the acquisition of their own shares by a third party. Most of the exemptions provided in the amendments of the Second Company Law Directive in 2006 have not been made available under Lithuanian law.

Relevant background in Lithuanian law

Lithuanian company law is mostly contained in the Law on Companies, which regulates incorporation, management and capital of both public and private companies. Public companies may be listed; private companies are 'closely held', with certain loose limitations on the number of shareholders and transferability of shares. The current Law on Companies was first adopted in 2000 and has gone through many amendments and recasts.

In addition to the Law on Companies, the Civil Code sets forth certain rules that are applicable to all legal entities in Lithuania. Financial assistance is only prohibited by the Law on Companies. Other legal entities (such as limited liability partnerships) are not subject to similar limitations.

The financial assistance prohibition was first introduced in Lithuania in 2003 and came into force in 2004. It was apparently a precursor for Lithuania's accession to the EU in 2004, and compliance with a respective condition to implement the Second Company Law Directive. Although the Directive only required the prohibition to apply to public companies, the Lithuanian legislator did not make an exception for private companies.

Wording of the prohibition

The initial wording of the financial assistance prohibition in 2003 was an attempted translation of the Second Company Law Directive, the correctness of which is sometimes disputed by both scholars and practitioners: 'a company may not pay in advance funds, make loans or provide security to third parties if such actions are directed at facilitating other persons to acquire shares of that company'.

In 2006, the Second Company Law Directive was amended to allow EU Member States to withdraw the financial assistance prohibition subject to certain conditions – in particular, with approval of the management and the shareholders meeting, and as long as the company's net assets remained above the authorised capital and statutory reserves. In essence, this meant that, if the Member State so allowed, financial assistance would be available from the reserves formed from the profits of the company.

An attempt was made in 2014 to lift the Lithuanian financial assistance ban according to the Second Company Law Directive (which is now incorporated into Codification Directive (EU) 2017/1132). However, instead of transposing the conditions under which financial assistance would be allowed, the Lithuanian legislator added the words 'directly or indirectly' – which were missing from the financial assistance restriction – and did not include any whitewashing procedure. Thus, not only was the financial assistance prohibition not removed – or at least made available subject to certain conditions – but it became more onerous (at least in theory).

Practically nothing has changed, notwithstanding the slightly improved wording which now reads as follows:

> 'A company may not, directly or indirectly, pay in advance funds, make loans or provide security to third parties if such actions are directed at facilitating other persons to acquire shares of that company.'

Most likely, the Lithuanian courts would interpret this wording in the context of the Directive, which speaks of prohibition to *'directly or indirectly, advance funds or make loans or provide security, with a view to the acquisition of its shares by a third party'.*

Reach of the ban

Lithuanian case law has developed a rather rigid approach towards financial assistance. In one case, the Lithuanian Supreme Court went as far as to quash security which was granted *after* the acquisition of shares. The Court relied on its finding that there had been a 'sufficient link' between the assistance (in the form of granting of a security) and the acquisition of shares.

An earlier case law from the lower courts acknowledged a post-acquisition merger between the bidding company and the target as an acquitting circumstance. However, it remains to be seen if such structures will be approved by precedents of the higher courts.

EXEMPTIONS

An exemption is available to help employees to acquire a company's shares under the relevant procedure prescribed by the Law on Companies. These specific provisions allow a company to motivate its employees by granting them its own shares. In this case, 'employees' may include those of a subsidiary or a parent company.

According to the Law on Financial Institutions, financial assistance is also available to:

- financial institutions when they provide financial services; and
- investment firms in certain cases.

CONSEQUENCES OF PROVIDING FINANCIAL ASSISTANCE

Invalidity of transactions

According to case law and most scholars, transactions made in breach of the financial assistance ban are null and void. The court should annul them *ex officio* even if no party disputes the relevant transactions. This does not make a huge difference in practice, as parties such as creditors or an insolvency administrator would normally challenge a loan or grant of security.

The fact that loans or security were granted in breach of financial assistance should not make the acquisition of shares unlawful, unless share transfer agreements have other fundamental flaws.

Management liability

According to the Lithuanian Law on Companies, the chief executive officer is responsible for compliance with financial assistance rules. Under Lithuanian law, the CEO is not just a managing director performing administrative function; although a CEO must be employed by the company, they also perform the role of a one-person management body. A Lithuanian company may opt to have no company board; however, even if a board is formed the CEO has certain specific functions, such as exclusive signature rights on behalf of the company. In this context, it is clear why the legislator puts the burden of compliance on the CEO.

However, it may be argued that the board (if formed) may also be held liable as it has fiduciary duties towards the company which may be breached by financial assistance. In other words, a burden of compliance put on the CEO may be interpreted as a responsibility to ensure compliance, but the general rules of delictual (tort) liability of the management bodies would remain intact.

There are no specific statutory provisions for the administrative or criminal liability of the management in case of illegal financial assistance. However, one cannot preclude that, in certain financial assistance events involving financial fraud, the applicability of Criminal Code would be invoked towards a CEO and other management bodies.

Fines

No administrative fines are explicitly set forth for the breach of financial assistance restrictions under Lithuanian law.