

# Q4

## D&I Quarterly 2007

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## MERGERS &amp; ACQUISITIONS

## > INTRODUCING CROSS-BORDER MERGERS AND DEMERGERS INTO FINNISH LEGISLATION

by Erkkä Pälä

### *EC requirements fulfilled – and more*

The legislation introducing cross-border mergers and demergers into the Finnish legal system is intended to enter into force in the near future. The legislation concerns both private and public limited liability companies as well as certain other types of entities. Principal amendments are included in the Companies Act and Co-operatives Act.

The new legislation implements the EC directive on cross-border mergers of limited liability companies (2005/56/EC, the "Directive"). The Directive does not cover cross-border demergers. However, in order to respond to companies', shareholders' and other stakeholders' recognised need for a cross-border demerger procedure, the new legislation contains also cross-border demerger provisions. The form and principles of the demerger provisions follow closely those of the cross-border merger provisions. The new legislation is applicable to mergers and demergers in which at least one of the participating companies is Finnish and the other company/ companies is/are situated in the European Economic Area.

### *Sevic judgment codified*

The new legislation codifies the so-called Sevic judgment (C-411/03) of the European Court of Justice. In *Sevic* it was confirmed that an EU member state cannot deny the registration of a cross-border merger merely due to the absence of national rules on cross-border mergers. Moreover, the *Sevic* judgment also predicted the need for a standardised and unambiguous cross-border demerger procedure.

As a main rule the new legislation is consistent with the existing legislation concerning corresponding domestic transactions. The legislative principles are analogous to those of the existing legislation concerning *Societas Europaea* ("SE") and it is likely that the general significance of SE decreases as a consequence of the new legislation. Hence, it is advisable to re-evaluate eventual intentions regarding establishment of a new SE.

The protection of public creditors is intended to be extended so that a public creditor is entitled to object to the merger or the demerger if the relevant public receivable (for example tax or other similar public payment) has been created before the due date of the public summons for the creditors. Until now the right to object has covered only receivables created prior to the registration of the merger or demerger plan. The described extension is applicable also to corresponding domestic transactions.

### *Effects on group structures and costs*

The new cross-border merger legislation offers possibilities for reducing administrative costs and simplifying the structure of international groups. The cost reduction possibilities will be especially beneficial for large finance and insurance companies (for example due to reduced supervision fees to different national financial supervisory authorities) practising cross-border business subject to license. On the other hand, the intended legislation does not as such affect the possible obligation to establish a Finnish branch office if business in Finland is continued after a cross-border merger dissolving a Finnish merging company. Thus, taxation, accounting and auditing costs related to a Finnish branch office must be taken into account also in the future.

### *Management's duty of care accentuated*

National cross-border demerger legislation is not harmonised by the EC legislation. The intended Finnish cross-border demerger legislation is not exhaustive, but merely provides for a general framework concerning the cross-border demerger procedure. As a consequence, even abrupt changes during the course of the demerger procedure cannot be excluded and the participant companies should at all times be prepared for sudden changes. Hence, the management of the participating Finnish company has an accentuated duty of care to safeguard shareholders' and creditors' rights in such situations.

## FINANCE &amp; CAPITAL MARKETS

## &gt; IMPLEMENTATION OF MIFID IN FINLAND

*by Tytti Laajanen*

## AMENDMENTS TO SECURITIES LEGISLATION

The directive on markets in financial instruments (2004/39/EC) ("MiFID"), which is an extensive rewrite of the financial services regulation within the EEA, was implemented in Finland as of 1 November 2007 by, *inter alia*, a revised Act on Investment Firms (922/2007), considerable amendments to the Securities Markets Act (495/1989) and several standards issued by the Finnish Financial Supervision Authority. Furthermore, OMX Nordic Exchange Helsinki Oy made amendments to its rules.

The significant changes include, *inter alia*, the following:

*Investment advisory services subject to license*

- the provision of investment advisory services became subject to license;
- renewed requirements relating to the organisation of the business of investment firms were introduced;
- procedures to be observed in client relationships when providing investment services are now regulated in more detail;
- authorised securities exchanges and securities intermediaries may establish multilateral trading facilities ("MTFs"), and securities intermediaries may deal on their own account with securities and other financial instruments by executing client orders outside stock exchanges or MTFs (so-called systematic internalisers); and
- new rules on transaction reporting were introduced.

*New regime for execution venues**New requirements for organisation*

The revised regulation brought detailed rules concerning internal organisation, systems and controls and requirements for independent functions for risk management, internal audit and compliance. However, the applicable requirements are to a certain extent dependent on the nature and scope of an investment firm's business. An investment firm must exercise due care when outsourcing any investment services or other important operational functions.

The Finnish legislator used the option granted by MiFID to allow investment firms to appoint so-called tied agents for the purposes of, for example, receiving and transmitting orders from clients, placing financial instruments and promoting the services of the investment firm. The investment firm remains fully responsible for any act or omission of the tied agent. It is not

### *New client classification rules*

possible for a tied agent to provide services on behalf of more than one investment firm.

Pursuant to the revised Securities Markets Act, securities intermediaries must classify each client as a non-professional or professional client or an eligible counterparty. The categorisation determines the procedures which must be observed in client relationships. For example, best execution rules, according to which intermediaries must take reasonable steps to achieve the best possible result for clients, do not apply when firms deal with eligible counterparties. The classification has also an effect on a firm's liability to obtain information from a client to determine the suitability of services or products for that client.

### *Trading of MTF securities exempt from asset transfer tax*

#### AMENDMENTS TO ASSET TRANSFER TAXATION

One of the key aims of MiFID was to increase competition between different execution venues. Consequently, in connection with the implementation of MiFID the exemption from the asset transfer tax applicable to publicly traded securities was extended to cover also securities traded in multilateral trading.

According to the new tax provisions, transfers of securities which are admitted to trading on an MTF are exempt from the asset transfer tax of 1.6 percent provided that such admission is based on an application by or the consent of the issuer and the securities are incorporated into the book-entry system. Contrary to the previous rules, in order to be free of asset transfer tax the transaction does not have to be executed at the trading place, but it must be carried out through a securities intermediary. Certain transfers, for example transfers relating to redemption proceedings or capital investment, are not exempt from the asset transfer tax.

## FINANCE &amp; CAPITAL MARKETS

## > NEW RULES ON CREDIT DATA

by Jukka Lång

### *Strict rules for processing credit data*

The Finnish Credit Data Act (the "Act") entered into force on 1 November 2007. The new Act sets forth rules applicable to processing of information regarding financial position of companies and personal economic circumstances of individuals.

The most significant changes to the previous legislation concern the scope of the term "credit data" as defined in the law. For the first time in Finland, the Act covers also credit data regarding companies and other corporate entities. Hence, the provisions protecting individuals from incorrect, unfounded and unnecessary processing of credit data are now extended to legal persons.

As part of their business, credit-rating agencies collect information regarding the financial position of companies and financial and personal circumstances of individuals. The purpose of the Act is to provide specific regulation of these activities and to enhance trust in financial activities as well as offering protection from indiscreet procedures.

In order to ensure the high quality of credit data, the Act strictly defines the categories of financial information that may be used for credit data and for the evaluation of creditworthiness.

### *New features to credit data*

The use of credit data on individuals is more extensively regulated than the use of credit data on companies. According to the new provisions laid down in the Act, also the credit data concerning a person in charge of a company (such as a managing director, a member of the board or a partner) may be used, with certain limitations, when evaluating the ability of the company or the person to answer for their commitments as a contracting party.

The Act makes it possible to extend credit data by a debtor's own request to include information on the background of a payment default entry. This means that, for example, the main reasons for a debtor's bankruptcy or an entry being due to liabilities of a debtor as a guarantor can be included in the credit data registers and reports.

The question of providing so-called "positive credit information", for example, information on well-administered loans repaid in due course, was considered during the preparation of the new Act. Due to practical difficulties relating to wider credit information system requirements, this reform was, however, buried.

### *Need to re-evaluate internal practices*

Since the Act requires special diligence from the users of credit data, it may be necessary to re-evaluate the credit data processing practices in the companies which regularly process credit information.

Generally, credit-rating services may be provided only to such parties which have a legitimate reason to process the information, for example, investigation of creditworthiness.

The credit data received from a credit-rating agency and possibly combined with other financial information received from other sources may only be processed in accordance with the provisions laid down in the Act.

### *Supervision*

Anyone conducting credit-rating operations must fulfil the qualifications laid down in the Act and submit a notification to the Finnish Data Protection Ombudsman. The Ombudsman supervises compliance with the Act and promotes the good credit information practices set out in the Act.

The credit-rating agencies are strictly liable for the correctness and accuracy of the information provided. A person who through wilful misconduct or gross negligence fails to comply with the provisions of the Act may be sentenced to a fine for a credit data violation.

### *No major changes to the credit data services*

Since the credit-rating agencies providing services in Finland have already been prepared for the new regulation, the Act is not expected to bring any major changes to their credit information services.

There is a one-year transition period before the Act comes into force in its entirety.

## DISPUTE RESOLUTION

## > DISTRICT COURT DISMISSES CHARGES IN LARGE SECURITIES CRIME CASE

by Juha-Pekka Mutanen and Mikko Koivula

### *Alleged misleading market information*

On 31 October 2007, the District Court of Helsinki handed down its judgment on a large white-collar crime case against 16 former executives of Jippii Group Oyj (today Saunalahti Group Oyj, a part of the Elisa Group). The former executives were accused, *inter alia*, of accounting offence, breach of disclosure duties, aggravated market manipulation and aggravated abuse of inside information.

According to the prosecution, the defendants had, *inter alia*, obtained unlawful economic advantage by providing incorrect and misleading information about Jippii Group's business prospects while at the same time selling to the market their shares in Jippii Group. The prosecution demanded that the defendants be sentenced to imprisonment of up to three years and to restitution of unlawfully obtained economic benefit from the sale of shares.

All charges were dismissed, mainly due to lack of proof and partly due to limitation of claims.

### *Stock exchange releases*

The charges concerning market manipulation and abuse of inside information were primarily based on three stock exchange releases published by Jippii Group in the spring of 2001. According to the prosecution, the company had in those releases provided misleading information about the results of its German subsidiary and misleading statements about the group's expected turnover and profit growth. The prosecution considered that the company did not have realistic possibilities to reach the turnover and profit forecasts for 2002 due to a liquidity crunch and problems in invoicing systems and network projects. According to the prosecution, all these problems were apparent already in the spring of 2001.

### *Effect on value of shares in growth companies*

In its judgment, the court appeared to place emphasis on oral testimony of witnesses as well as expert accounting opinions presented by the defence. According to the court, a manipulation of the German subsidiary's accounts or the delay of projects had not been proven. Moreover, the court considered that, in the spring of 2001, the value of telecommunications and internet companies was mainly based on the number of subscribers and the expected volume of future business. According to the court, liquidity problems were typical for growth companies and did not appreciably affect the value of their shares. Also, the court considered that any delays in the implementation of invoicing systems would be temporary and did not

therefore render the company's announcements of its business prospects misleading.

Accordingly, the court dismissed the charges holding that the existing problems in the company's business operations were not such as to appreciably affect the value of its shares and that the company's business forecasts could therefore not be considered as misleading.

### *High burden of proof*

The judgment appears to place a fairly high burden of proof on the party claiming violation of securities rules in connection with business forecasts which, in hindsight, turn out to have been overly optimistic. In the light of the court's judgment, overly optimistic forecasts, especially in growth companies, do not seem likely to easily attract criminal sanctions except where the grounds for such forecasts are manifestly erroneous.

The judgment has been appealed to the Court of Appeal.

## CORPORATE &amp; COMMERCIAL

## > NEW GENERAL TERMS AND CONDITIONS OF PUBLIC PROCUREMENT OF INFORMATION TECHNOLOGY

by Sakari Halonen

On 8 October 2007, the Advisory Committee on Information Management in Public Administration, JUHTA, which has been set up at the Ministry of the Interior to promote cooperation in information management between the State and municipalities, issued new terms and conditions of public procurement of information technology products and services ("JIT 2007").

The JIT 2007 replace the previous general terms and conditions of government procurement of information technology of 1998, known as the VYSE 1998 terms and conditions.

The JIT 2007 have been prepared in a project commissioned by the Ministry of Finance. Representatives of the government, municipalities and various governmental contracting entities as well as service providers of information and communication technology have participated in the project.

### *Structure of JIT 2007, general and special terms and conditions*

Like the VYSE 1998, the JIT 2007 include general terms and conditions (the JIT 2007 General Terms and Conditions) and various special terms and conditions applicable to different products and services. The special terms and conditions include:

- Special Terms and Conditions for Procurement of Customised Application Software;
- Special Terms and Conditions for Procurement of Services;
- Special Terms and Conditions for Procurement of Consultancy Services;
- Special Terms and Conditions for Procurement of Standard Software; and
- Special Terms and Conditions for Procurement of Equipment.

In addition, the JIT 2007 include the following model agreements:

- Model Agreement for the Procurement of Customised Application Software;
- Model Agreement for the Delivery of Services; and
- Model Agreement for Consultancy Services.

Moreover, JUHTA has prepared separate instructions for the use of the new JIT 2007, much like the instructions given for the use of the IT2000 terms and conditions. The instructions are intended for the use of the supplier and the public contracting entity. The JIT 2007 contain neither instructions nor terms or conditions concerning the underlying public procurement procedure resulting in the procurement.

### *Changes from VYSE 1998*

The general structure of the JIT 2007 remains mainly unaltered. However, the Special Terms and Conditions for Equipment and Software Maintenance Services (VHYE 1998) and the Special Terms and Conditions for Facilities Management Services (VKÄE 1998), which formed part of the VYSE 1998 terms and conditions, have been repealed. The terms and conditions contained therein are considered to be generally covered by the JIT 2007 Special Terms and Conditions for Procurement of Services.

The scope of application of the JIT 2007 has been expanded to cover also IT procurement by municipalities, whereas the VYSE 1998 terms and conditions were intended to be applied by the Finnish Government and its contracting entities only. Hence, the JIT 2007 are expected to harmonize IT procurement practices within the public sector.

Changes have been made to the provisions governing delivery, testing and acceptance of the products. The aim is to cover the entire life-span of the products. Furthermore, the provisions governing prices, pricing principles and terms of payment have been updated.

### *Division of intellectual property rights*

As in the VYSE 1998 terms and conditions, the intellectual property rights to both standard software and customised software applications vest in and remain the property of the supplier. The customer is, however, granted rather extensive rights to the software, similar to those granted under the VYSE 1998 terms and conditions. The only exception is for the intellectual property rights to the results of professional services rendered for an agreed task, which vest in and shall belong to the customer.

### *Other introduced new issues*

The JIT 2007 terms and conditions take into consideration possible use of open source material, as well as issues relating to data security. Moreover, the confidentiality provisions of the JIT 2007 General Terms and Conditions take into consideration the requirements of the Act on the Openness of Government Activities (621/1999).

CORPORATE &amp; COMMERCIAL

## > ARBITRATION CLAUSES IN EMPLOYMENT CONTRACTS

by Seppo Havia

On 23 August 2007, the Helsinki Court of Appeal gave its decision in a case concerning the enforceability of arbitration clauses in employment contracts.

### FACTS OF THE CASE

The defendant company was sued by its former employee whose employment had been terminated due to organisational changes within the company. The claimant demanded compensation on the grounds of unlawful dismissal. He also claimed for his bonus and holiday remuneration as well as arrears of his salary for the notice period.

#### *Three-person arbitration tribunal*

The employment contract contained an arbitration clause according to which all disputes arising from the contract in question were to be resolved by a three-person arbitration tribunal. The employee contested the validity of the clause and proceeded with his claim in the courts.

#### *Unreasonable arbitration clause*

The employee contended that the arbitration clause claiming it was unreasonable. In this regard, the employee argued that he did not have the financial means to submit to arbitration proceedings and that due to the nature of his employment the clause could not be deemed reasonable. The claims were contested by the company, which also challenged the substantive arguments made by the employee.

#### *Entirety of the contract*

### JUDGMENT OF DISTRICT COURT

In its judgment, the District Court focused on whether the arbitration clause in question was binding. Its reasoning was based on the Contracts Act (1929/228), under which unreasonable contractual terms can either be adjusted or disregarded. The Act provides that when considering whether a clause is unreasonable a court must take into account the entirety of the contract, the position of the parties, the conditions prevailing when the contract was entered into as well as at the present time, and any other relevant matters.

#### *Lack of equality*

According to a Supreme Court decision (1996:27), an arbitration clause may be deemed to be unreasonable especially in a situation where the relationship between the parties is characterised by a lack of equality, such as the relationship between an employer and an employee, or where the litigant would face significant legal costs. In another case (2003:66), the Supreme Court held that an arbitration clause may be adjusted or

disregarded if the dispute in question is straightforward and involves modest amounts of money.

#### *Nature of the contract*

The District Court considered that the claimant's employment contract was notably different from ordinary employment contracts, both in terms of his rights and his obligations. He was, *inter alia*, entitled to a share of the company's profits as well as subject to broad confidentiality and non-compete clauses. On these grounds, the contract was held to be a director's agreement, not suitable to be adjusted or disregarded.

#### *Financial significance of the dispute*

The court was also influenced by the fact that the dispute concerned compensation amounting to over EUR 200,000 and could as such be considered financially significant. Further, the District Court found that the claimant had not presented sufficient evidence to show his financial situation to be such that it prevented him from submitting to arbitration proceedings. The District Court therefore dismissed the claim.

#### JUDGMENT OF COURT OF APPEAL

The Helsinki Court of Appeal upheld the verdict of the District Court and found no reason to depart from the decision of the lower court. This decision has not been appealed, making the judgment of the Court of Appeal final.

#### CONCLUSIONS

#### *No hard and fast rule*

Under Finnish law, arbitration clauses in employment contracts are *prima facie* enforceable, and a court must be presented with specific grounds for adjusting or disregarding such a clause. Although in general terms arbitration clauses are likely to be held unreasonable in ordinary employment contracts but reasonable in directors' agreements, there is no hard and fast rule to be applied. The most significant factors influencing the courts in their analysis are the nature of the employment, the financial resources of the parties, the nature and value of the claim and overarching considerations regarding the parties' access to justice.

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