New Companies Act

in Finland

D&I Focus

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- The new Companies Act is due to enter into force on 1 September 2006.
- Express recognition is to be given to general principles of corporate law.
- A non par value system is to be introduced.
- The board's liability is to be enhanced.
- A solvency test is to be applied in connection with the distribution of funds.
- Decisions applying the new Act may be adopted already at the next annual shareholders' meeting.

Flexibility and Competitiveness

After several years of preparation, the Finnish government presented on 2 September 2005 to parliament its proposals for a new Companies Act (Government Bill HE 109/2005) ("the Act"). The Bill is expected to receive parliamentary approval in late 2005 or early 2006. In order to give businesses time to prepare for the new legislation, the Act is timetabled to enter into force on 1 September 2006.

The objective of the legislator is to introduce a company law that is both flexible and competitive within the European environment. Unfortunately, the Ministry of Finance has not been able to keep pace with the preparation of new taxation rules that are related to the Act. Consequently, many of the novelties provided for by the Act are likely to remain "dead letters" until the new tax rules are themselves introduced.

The Act applies to both private and public companies and has been completely rewritten with the aim of achieving readability and clarity.

Statutory Principles

The Act expressly recognises many general principles of corporate law that until now have been found only in jurisprudence and court practice. To reflect the interests of small private companies mandatory administrative procedures have been reduced and simplified.

Shareholder discretion has been increased as much as possible without compromising the protection of creditors. The Act seeks to emphasise the character of a limited liability company as a contractual vehicle governed by its articles of association. Shareholders' freedom of contract is limited only by express mandatory rules and good practice (business ethics).

The relationship between shareholders is based on the majority-rule and the principle of equality. Statutory minority protection may not be weakened by the articles of association. Decisions and actions that unjustly benefit a shareholder at the expense of the company or another shareholder are not permitted.

Share Capital - Non Par Value System

Shares in Finnish companies have traditionally had a nominal value which has been the minimum subscription price for each share. The Act abolishes such a link between a company's shares and its share capital. However, companies will have the possibility to maintain the nominal value if so specified in the articles of association.

A non par value system is to be introduced.

Furthermore, share capital may be raised without issuing new shares and, correspondingly, shares may be issued without raising the share capital. Consequently, the new rules will allow for share issues without consideration.

The new Act provides more flexibility when it comes to investing in companies and the return of funds to investors. Equity investments made in a company may be placed in separate unrestricted equity funds. Such equity may be distributed back to shareholders at the discretion of the shareholders' meeting subject to a procedure similar to the payment of dividends.

The possibility to issue shares at a low price or without compensation raises issues of equality. A directed share issue without consideration is permitted only if there are particularly weighty reasons for the issue. Under similar

circumstances the company may issue shares to itself without consideration.

Acceptable reasons for such an issue of shares are, inter alia, incentive schemes for company personnel or compensation paid to shareholders in connection with the combination of share classes, or the evening out of shareholdings for the purposes of a share split.

Financial Assistance

The rules on financial assistance remain to a large extent unaltered. It is not permitted under the Act to grant a loan to a third party for the acquisition of a company's shares.

It should, however, be noted that all detailed rules on inner circle transactions are abolished. Instead, all inner circle transactions will be judged on the basis of the corporate benefit principle.

Liability of the Board

The board's liability is one of the principles that has been enhanced. The obligations of the members of the board of directors are based on two cornerstones: the duty of loyalty and the duty of care. These translate into the business judgement rule, which is introduced in the preparatory works of the Act. The requirement of loyalty extends towards both the company and its shareholders.

Although the liability of directors requires proof of negligence, significant exemptions have been introduced. Negligence is assumed in connection with a breach of the articles of association, breach of an express statute and inner circle transactions. This shifts the burden of proof to the directors to provide proof that overrides the assumed liability.

The board's liability is to be enhanced

The Act includes an option to slightly reduce the board's liability. The articles of association may contain a specific provision pursuant to which the board is not liable towards the company for its actions or omissions unless they are based on gross negligence or wilful misconduct. Third party liability may not be reduced by any provision in the articles of association.

Solvency Test

As a counterbalance to the more flexible equity system, the Act introduces the solvency test concept. The solvency test is to be applied in connection with the distribution of funds. The distribution of funds is not permitted if the circumstances at hand are such that the board knows or should have known that the company is insolvent or would become insolvent as a result of the distribution.

The timing of the decision is relevant for the application of the solvency test. The board may not be held liable on the basis of hindsight. Nevertheless, the solvency test is an important element in the framework within which the actions of the board are evaluated. Due care should be exercised when documenting the information that the board relies on.

A solvency test is to be applied in connection with the distribution of funds

Selected Practical Observations

The Act introduces changes to a number of established corporate practices and provides extended possibilities concerning others. The following lists some of the relevant changes and other observations:

- the incorporation procedure is changed;
- the mandatory minimum share capital remains EUR 8,000 for private and EUR 80,000 for public companies;
- the minimum content of the articles of association is reduced to company name, domicile and objects of the company;
- the Act provides standard contents for the articles of association which are to apply unless otherwise stated in the adopted articles of association;
- the statutory minimum requirement for the composition of the board of directors is reduced to one ordinary member and one alternate;
- the statutory requirement to appoint a managing director is abolished;
- the rules regarding contributions in kind are extended;
- the possibility for distribution of profit based on interim accounts is introduced;
- the possibility for three-party mergers is introduced;
- the possibility for de-merger into an operating company is introduced; and
- an obligation to file a notice with the trade register in case more than 50% of share capital has been lost is introduced.

Amendment of Existing Articles of Association

The Act contains no immediate requirement for the amendment of the currently valid articles of association. Due to the largely non-mandatory nature of the Act, it may not be possible for companies to obtain the full benefit of the reform without amending their existing articles of association. Resolutions on such amendments may be passed immediately after the Act has been ratified, entering into force simultaneously with the Act.

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