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New Finnish Companies Act designed to increase Finland's competitiveness

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Background

On September 6, 2005, the Finnish Government submitted to the Parliament a bill for a new (limited liability) Companies Act.

The proposed new act is based solely on national legislative interests and one aim of the reform is to give Finnish companies a competitive edge in relation to foreign competitors by granting Finnish companies a wide range of flexibility. International trade and financing has been liberalized since the enactment of the present Companies Act and a majority of the old EU members have entered into a monetary union, adopting the euro as a single currency. These changes in the working environment of Finnish companies are, according to the government proposal, principal reasons for the reform. The new law also aims to promote competition among companies.

The proposed reform is extensive, and it covers the entire Companies Act. Foreign investors should be aware of certain important changes, which can be only referred to in a general manner in a short article of this nature. In particular, the new Act will bring important changes and benefits in relation to companies dealing in international trade, discussed below.

The new Companies Act has come into force on September 1, 2006.

More flexibility – more responsibility

The new Companies Act will enhance the sphere of possibilities and therefore improve the business conditions for Finnish companies in general. The sphere of possibilities is enhanced by reducing the amount of formal requirements and by enacting a whole new set of provisions and procedures e.g. in areas such as incorporation of the company, financing and corporate transactions. The new law will also give companies more options than its predecessor. By being more extensive, the new Act will clarify the present legal status and provide more certainty. The new Act will also include provisions about matters that so far have been dealt only in legal literature and case law.

One important change in the new law is the structure of its contents. The main legal principles have been set out in the first chapter. This approach gives the reader an idea of the principles on which the law is based and helps to understand the more specific provisions in the following chapters.

The new law will not affect the legal status of minority shareholders or creditors in general, although it includes some provisions that strengthen their position. Discrimination among shareholders will remain prohibited. Special attention has been given to small, privately held companies. The substantial clarification of the regulation, the broadening of the regulation and the way in which many provisions relating to smaller companies are written in areas such as shareholder meetings and articles of association, makes the law easier to approach.

The changes in the society toward a more competitive business environment, better access to capital and the changing corporate structure as well as the various business purposes for which a limited liability company is being used, require a more flexible corporate and business legislation. Therefore, the new Companies Act contains a number of optional provisions that give the companies and their shareholders a lot of discretion.

This flexibility highlights the importance of proper corporate planning. For instance, only a part of the subscription price of shares must be allocated towards the restricted equity of the company and the rest may be placed in the non-restricted equity portion and, thus, be used rather freely. This gives companies more financing opportunities especially in mergers and other transactions. Another major change is the division between shares and shareholders' equity. To illustrate this change, the new Act is based on the notion that a single share no longer represents a portion of the shareholders' equity. In other words, the shareholders' equity can be increased without giving out new shares, and new shares may be issued without increasing the shareholders' equity. As one repercussion of this changed approach, in the case of the acquisition by the company of own shares (a share buy-back) as well as share redemption, neither the acquisition by the company of its own shares nor a share redemption by the company has to result in a decrease of shareholders' equity.

The flipside of these reforms is the increasing responsibility of company management. According to the new Act, the management must act diligently in the best interests of the company. This may naturally vary in different situations. The increased flexibility puts more emphasis on the legal requirements and procedures that need to be followed when making corporate decisions and not e.g., whether an investment decision has in hindsight been reasonable. Corporate decisions are often made under uncertainty. Therefore, the management's duty of care should be judged objectively taking into account the circumstances prevailing when the decision was made.

Changes of interest to foreigners

One example of changes which may have an influence on foreigners is the increasing responsibility of shareholders for their decisions. All shareholders should keep some basic principles of the new Act in mind while making resolutions in shareholders meetings in order to avoid the possibility of a personal responsibility.

Another example of a situation in which foreigners are often affected is lending money to a Finnish company. The existing Act contains complicated provisions

regarding loans and guarantees granted to the "inner circle" of a company. Because of their vague and ambiguous nature, the provisions have caused practical problems also in group company situations each time inter-company loans and loan collateral have been made in a group of companies involving several jurisdictions, with one or more companies in Finland. The new Act would abolish the "inner-circle" lending and guarantee restrictions concerning monetary loans (and securities) granted to a party belonging to the "inner circle" of the company. Under the new Act, a loan to a party belonging to the related entities of the company, as well as any other loan, may be granted only if it is in the best interest of the company. Furthermore, there should be a business purpose for such transactions. This means that in group company situations a loan may be granted if a group company obtains benefits e.g., through accrued interest, future financing or in any similar way from the loan. Again, rather than attempting to provide "safe-heaven" situations, the governing organs of the company, principally the board of directors, are responsible for ensuring that the inter-company financial transaction is in the company's best interest and satisfies the above described criteria.

Conclusion

The reform brings various changes to the Companies Act. These changes are important to all constituencies of the company. The management has more discretion in its work, although it is bound by the duty of care. Similarly, the shareholders may want to monitor the managements' actions more closely. On the other hand, the responsibility of shareholders for their decisions is also wider.

The new Companies Act will bring a lot of new opportunities for companies in planning their corporate structure. It is therefore essential that this planning is done in a coordinated fashion with the required legal knowledge. From a legal point of view, the change is for the better and it is for the companies and their constituencies to take full advantage of the new, more flexible Companies Act.