INTERNATIONAL ASSOCIATION OF YOUNG LAWYERS

The pursuit of a company's interest over the life of a company

Commission(s) in charge of the Session/Workshop: Corporate Acquisition and Joint Ventures Commission

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National Report of Austria

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A. Interest of Equity Holders

1. Start-up phase

1.1 In your opinion, what is an entrepreneur's typical reasoning for setting up a specific business association? Attract investments by third parties? Avoidance of personal liability? Tax reasons? Protect IP rights and technology?

We believe that it is difficult to single out a "typical reason" that encourages entrepreneurs to set up a specific business association. Reasons vary very much depending on the envisaged scope of the business and the type of business. Generally speaking, entrepreneurs that aim to establish a "large" business will aim for establishing a corporation, while others will usually choose corporate forms that are easier to handle but do not offer some of the advantages of corporations (e.g. shielding from personal liability, facilitated transfer of shares).

Tax reasons might also play a big role in Austria, as there are significant differences in the taxation of corporations and other corporate forms like partnerships.

1.2 What kind of business association structures does your jurisdiction offer to equity holders (e.g., partnerships, corporation, LLC, etc.)?

- **What are the most crucial differences between these business association structures from an equity holder's perspective?**

The most common corporate structures are as follows:

- Stock Company (*Aktiengesellschaft, AG*): limited liability for shareholders, transfer of shares comparably easy, besides shares also other equity instruments like convertible bonds are available, independent board of directors (no instructions by shareholders possible), mandatory supervisory board, minimum capital EUR 70,000, strict capital maintenance rules.
- Limited Liability Company (*Gesellschaft mit beschränkter Haftung, GmbH*): limited liability for shareholders, share transfer requires notarial deeds, shareholders can issue instructions to managing directors and generally have more possibilities to directly control the company, no mandatory supervisory board, minimum capital EUR 10,000 (with certain further requirements), strict capital maintenance rules, more flexibility to adapt corporate governance of company to the needs of shareholders.
- Open Partnership (*Offene Gesellschaft, OG*): No limited liability, by default transfer of shares need consent by all shareholders (but articles can provide for more flexibility), shareholders are at the same time managing directors, no supervisory board, no minimum share capital, no capital maintenance rules, corporate governance can be adapted to needs of shareholders.

- Limited Partnership (*Kommanditgesellschaft, KG*): Similar to Open Partnership, but with non-managing shareholders with limited liability.

Other less common forms: Societas Europaea (European Stock Company, SE), Civil law partnerships (*Gesellschaft bürgerlichen Rechts*), Cooperatives (*Genossenschaften*).

- **If statistics on the use of business association structures are available in your jurisdiction: which are the most commonly used business association structures for start-ups? Do you see a particular reason for the dominance of one specific structure?**

We could not identify detailed statistics on specific corporate forms, but according to the most recent data published by Statistic Austria for 2012, by far the most new companies (15,830) were established as personal undertakings (*Einzelunternehmer*). 4,184 new companies were established as corporations and 4,063 were established as open or limited partnerships. This numbers seem to have been consistent over the past years (see http://www.statistik.at/web_de/statistiken/unternehmen_arbeitsstaetten/unternehmensdemografie_insgesamt/neugruendungen/index.html for details)

- **In case of a corporation or LLC (in the following we simply refer to the "*company*"): are there any equity instruments other than common shares that are typically used for equity investments? Non-voting shares? Other forms of participation rights?**

With respect to limited liability companies, statutory law does not provide for other equity instruments other than shares, but the law is relatively flexible so that instruments like non-voting shares or convertible bonds can be achieved to a certain extend by using alternative mechanisms.

- **Can equity investors remain anonymous (for example by the use of bearer shares)? Anonymous towards the company, other investors, the public? In the event equity investors cannot remain anonymous when holding shares, is there any alternative scheme that can be implemented to participate on an anonymous basis (for example, silent partnership schemes)?**

With respect to most corporate forms, shareholders need to be registered in the commercial register (that is publicly available).

Shareholders of stock companies are (with certain exceptions) not registered in the commercial register. However, since 2011 only listed companies may use

"anonymous" bearer shares, other stock companies have to use name shares (that are registered with the company, but not the commercial register).

It is also possible to use trust relationships or silent partnership agreements.

1.3 Once the entrepreneur has set up a company: what could be a typical focus of third party equity investors when they invest in a company in this phase?

- **What could typically be the friends', family's and fools' ("FFF") focus? Helping the entrepreneur to get his / her business going?**
- **What could typically be the professional investor's focus?**
- **If there is a difference in focus among the various equity investors, how is this typically reflected in the legal relationship (be it corporate or contract law)? Are there legal instruments that are only used by certain investors (e.g., only by professional investors)?**

We believe that in this context it is difficult to provide for generalized statements on the motives of investors, as in our experience the motives of investors vary to a great extent from company to company. Obviously, strategic investors will usually apply a more long-term perspective; while more yield orientated investors might look at a shorter term to "cash out".

With respect to the legal documentation, this most notably shows in the shareholder documentation, where yield orientated (e.g. private equity) investors usually already set out the conditions for their exit in the founding documents, e.g. the first shareholders agreement. There are, however, in our experience no legal instruments that are only used by a certain kind of investors. Rather, also professional investors would use typical legal instruments (e.g. drag along rights, right to demand an IPO, put options) that in each case need to be adapted to the specific needs of the company and its business plan.

2. Growth phase

2.1 In your opinion, does the focus of the equity holders (e.g., the FFF or professional investors) shift in the growth phase (as compared to the start-up phase)?

- **If so, what could be a particular focus for equity holders in the growth phase? Protection from dilution?**

- **In your experience, do the equity investors from the start-up phase participate in further capital rounds in the growth phase? Do they usually accept dilution? Do they usually cash out at this point in time?**

Again, we believe that it is difficult to provide for generalized statements, as the focus of equity investors differs from company to company and the motives of investors are usually very divers.

In our experience, quite often it is even difficult to distinguish between the start-up phase and the "growth phase", as in both phases the company is usually very dependent on the commitment of its founders and its initial circle of investors. Therefore, quite often the commitments by equity holders given in the start-up phase already extend to the growth phase and equity holders already commit in the course of the establishment to provide further funding in the growth phase (often subject to certain milestones and conditions being fulfilled). This is often accompanied by lockup periods. Only after the growth phase, these commitments are usually reduced or cease and equity holders gain more flexibility with respect to theirs potential exit.

On the other hand, during the growth phase the shareholders usually agree on quite strict dilution protection rules that go beyond the protection granted by statutory law.

2.2 In your jurisdiction, does the company law provide existing equity holders protection from being diluted in further financing rounds in the growth phase? If so, how are they protected? Is there a need for equity holders to seek protection on a contractual basis?

With respect to the two most common forms of corporations (stock company and limited liability company) shareholders holding 25% (voting rights (LLC) or capital (stock company)) have a veto right against capital increases and, therefore, against dilution.

In case an appropriate majority votes in favor of a capital increase, minority shareholders still have a subscription right. However, it is possible to exclude the subscription right of shareholders if there are objective reasons to justify such exclusion. Such reasons to justify an exclusion might for example be the issuance of stock options or the investment by a strategic investor for the purpose of a beneficial corporation.

As there is, therefore, a risk for minority shareholders to be diluted, it is sometimes advisable to protect minority investors. Such protection can either be achieved by implementing higher minority requirements for capital increases directly in the articles, or also for example by setting out protection mechanisms in the respective shareholders agreement (e.g. capital increase only by mutual approval of all shareholders).

2.3 When new potential investors offer to come on board during the growth phase, the existing equity holders may be reluctant to provide the information required to satisfy the potential new investor's need for valuation. The reason for the existing shareholders' reluctance may be, for example, that the required information contains (still) unprotected intellectual concepts, knowledge or ideas. In your experience, which legal instruments are used to find a balance between the potential new investor's need for information and the existing equity holders' wish to keep such information confidential? Do existing equity holders have legal means to prevent management from disclosing such information?

There are certainly a number of tools available to restrict the flow of information to new investors.

Regularly, information to potential new investors will be disclosed by the company in a due diligence process. The company and existing shareholders may for example consider the following measures:

- Non-disclosure agreements with adequate penalties in case of infringement
- Data rooms with only limited access (e.g. only to professional advisors)
- "Red files", that are only available to certain representatives
- Due diligence in several stages (e.g. "confirmatory" due diligence only after investor has issued a binding offer)
- Due diligence report issued by the company/existing shareholders

Existing equity holders have – to a certain extend – also the means to prevent the management of the company from disclosing confidential information. Details depend on the corporate form of the target company: While the management of stock companies is subject to very strict confidentiality obligations that even extend to the disclosure of confidential information to shareholders, the confidentiality obligations are less strict, and therefore more difficult to enforce, with respect to limited liability companies and partnerships.

3. Maturity

3.1 In your opinion, how does the equity holder base change between the start-up phase, the growth phase and the maturity phase? How does the focus of the equity holders change? Focus on fair distributions of earnings?

Naturally, companies in the maturity phase will often broaden their equity holder base. In our experience, this is also the phase in which investors not affiliated with

the founding shareholders will start investing in entities. (Austria does not have a significant number of high risk investors that would already provide significant equity in the startup or growth phase.) These new investors will usually focus more on their (immediate) return on investment and, therefore, also focus more on the achievement of short term profits.

3.2 In your jurisdiction, does the law provide for stricter corporate governance rules for large (privately-held) companies as compared to small companies? If so, what exactly triggers the application of the stricter corporate governance rules? In which sense are the corporate governance rules different / stricter?

The corporate governance rules for large and small (privately-held) companies are largely similar, with only a few exceptions, most notably:

- Accounting and auditing rules change depending on the size of the company, with Austrian law distinguishing between “small”, “medium” and “large” undertakings. (Classification of undertakings is subject to a rather complex set of criteria set out in Sec 221 of the Austrian Commercial Code.)
- Limited Liability Companies exceeding certain thresholds need to establish a mandatory supervisory board. (The rather complex criteria are set out in Sec 29 of the Act on Limited Liability Companies)

3.3 In your jurisdiction, do (certain) equity holders (e.g., majority shareholders) have obligations towards (certain) other shareholders or the company (e.g., duty of loyalty)? Please explain such obligations.

Yes, all shareholders and partners of Austrian entities are subject to duties of loyalty to the company and their co-shareholders. The extent of these duties varies between partnerships (were such duties are stricter, also e.g. including explicit non-compete obligations for the shareholders) and corporations (with less strict rules). Generally speaking, shareholders are prohibited from actively harming the company and might under certain circumstances also have to vote in certain ways to preserve the interest of the company.

3.4 Does the company have any means to control the circle of its equity holders (i.e., can the articles of incorporation prevent competitors from holding shares in the company?) or have such restrictions to be agreed among the other equity holders (e.g., shareholders' agreement)?

Corporations (Stock Companies, LLCs) only have means to control the circle of its shareholders, if such restrictions are set out in the articles of association of the respective company. In such case, transfer restrictions in favor of the company are directly applicable to third party acquirers. Obviously, it is also possible and common to agree on transfer restrictions in shareholders’ agreements but such restrictions are only of limited relevance to third party acquirers.

In contrast, with respect to partnerships (OG, KG) the situation is different as by default a change of a shareholder requires the consent of all other shareholders. (This can be altered in the articles of association).

4. IPO / Listed phase

4.1 How does the focus of the shareholders change through the going public as compared to the maturity phase? Does the fact that a shareholder may at any time sell the residual value in its share (ideally) at a fair price in your opinion soften the focus on distribution of earnings? Does the focus shift from long term to short term?

In Austria, also listed companies typically have strong core shareholders with very diverse motives, ranging from strategic participations to pure yield oriented investments. Besides, due to the fact that typically a listed company will also attract a large number of non-controlling minority shareholders and is also subject to stricter and more frequent financial reporting requirements, the focus will usually shift more to achieving short term results.

4.2 In your jurisdiction, are there publicly available records on the identity of (certain of) the shareholders in a listed company? If so, does this in your opinion influence the shareholders' focus?

Shareholders of (listed) stock companies are not registered in the commercial register.

However, shareholders are – with certain exceptions – obliged to notify the company if their voting rights exceed or decrease below certain thresholds (4%, 5 %, 10 %, 15 %, 20 %, 25 %, 30 %, 35 %, 40 %, 45 %, 50 %, 75 % and 90 %). The company is in turn obliged to disclose any such notifications received. Therefore, the identity of major shareholders can usually be traced on the basis of such disclosures.

We do, however, not think that this usually influences the shareholders' focus.

4.3 An efficient allocation of resources requires a most accurate pricing of the shares.

- **In this regard, are companies that are listed in your jurisdiction under an obligation to publish price-relevant information (ad hoc publicity)? If so, please provide a short overview of the respective rules including the exemptions from such obligation.**

- **It can be assumed that no jurisdiction requires listed companies to publish all price sensitive information. If this is correct in your**

jurisdiction, how does the law protect the market and its participants (including, the equity holders in the company) from market abuse? Are there insider trading and market manipulation prohibitions? If so, please provide a short overview and, if you can, provide certain peculiarities about them?

Listed companies are subject to ad hoc publicity requirements and have to immediately publish "insider information", i.e. information not known by the public, that concerns the company and that if it would be known by the public would have a significant impact on the share price. The rules are quite complex and detailed, and there are also several notable exceptions from the publication duties. Most notably, the company can postpone the publication if the publication would harm the legitimate interests of the company, as long as postponing the publication may not result in misleading the public and the company is able to maintain the confidentiality of the information (example: information on pending negotiations that are important for the company or decisions that are still subject to an approval by corporate bodies of the company). In such case, the company still has to inform the financial market authority on the postponement of the disclosure.

In addition, there is of course also an express prohibition of insider trading and market manipulation activities. Insider trading is subject to criminal liability of up to five years of prison sentence for "insiders" and three years for "non-insiders". Market manipulation is usually punished with monetary fines of up to EUR 150,000, if the market manipulation is not at the same time a criminal offence (e.g. fraud). Again, the rules regarding insider trading and market manipulation are rather detailed and complex.

5. Acquisition

5.1 In case a listed company (target) is approached by another company (bidder), the board of the target will have to decide whether it supports the offer (friendly offer) or not (unfriendly offer). What are the interests that the board of directors needs to take into consideration for this decision? Shareholders' interests only (e.g., offer price only)? The interests of other stakeholders (employees, community etc.)?

The Austrian Takeover Act sets out firm restrictions on the management of the target company: It must not take any measures that might impact the decision-making process of the shareholders and must not take any measures that might prevent the acceptance of the offer without having obtained the prior approval of the company's shareholders meeting (with the exception of a search for an alternative

bidder, that can also be performed by the management without prior approval by the shareholders meeting). The Takeover Act, therefore, requires the management to stay (mostly) neutral and shifts the decision-making process with respect to public offers (and measures to be taken in favor of or against an offer) to the shareholders.

The Austrian Takeover Act, however, requires the board of directors to make a reasoned statement on the offer including the potential effects of the offer on the shareholders, the company, its employees and the public interest.

5.2 In case of an acquisition of the listed company (target) by another company (bidder), the shareholders' are at a disadvantage as they cannot communicate efficiently or act in concert (for example, regarding the rejection of a low offer). A rational bidder should try to use this disadvantage of the shareholders to his benefit. In your jurisdiction, how does the law protect shareholders of the target in case of public tender offers? (for example, is there a specific process for public takeover offers which provides protection? Does the bidder need to treat target shareholders equally? Are there, for example, minimum price rules and/or best price rules?)

The Austrian Takeover Act sets out very detailed rules for voluntary and mandatory takeover offer bids. The rules are very complex and it is difficult to provide a meaningful summary in the context of this report[1].

The Austrian Takeover Act seeks to safeguard the equal treatment of all shareholders, the provision of sufficient information to all shareholders to make informed decisions, the avoidance of market manipulations and generally also a fast takeover procedure. To comply with these principles, the Takover Act sets out detailed rules for when offers need to be placed, the contents of these offers, how offers have to be published, examined and amended.

Shareholders need to be treated equally also with respect to the offer price and in case of mandatory takeover offers the price offered must not be below certain thresholds (most importantly, the price paid by the bidder to other shareholders during the last 12 months and the average stock exchange price of the last 6 months).

5.3 As mentioned above, a listing provides (ideally) liquidity for the company's shares and ensures a high level of information for a potential new investor. In fact, equity investors may invest in listed companies exactly for these reasons. In your jurisdiction, how is an equity investor protected from a delisting? Does the delisting require (qualified) shareholder consent? What are the

[1] The Austrian Takover Act has over 35 sections and even a short summary would likely exceed the suggested page limit of 15 pages..

deadlines for the delisting? Do issuers need to provide for an off-exchange trading for a certain period following delisting?

The following protection mechanisms are in our view the most relevant with respect to a voluntary delisting:

First, the company planning to perform a delisting needs to request approval by the Viennese Stock Exchange, which can deny such approval if the interests of the shareholders are not adequately protected.

Second, a delisting is only possible following a shareholder resolution with a qualified majority of 75%.

Third and most important to protect minority shareholders, before delisting the company or one of its core shareholders need to make a public bid to acquire shares of minority shareholders or initiate a formal compensation procedure to compensate shareholders for their shares, by which they are compensated at least in an amount equal to the enterprise value or, if higher, the average market value of the shares (being calculated over a certain period).

B. Interest of Debt Holders

1. Start-up phase

1.1 In your experience, what could be the typical focus of the FFF in this phase? Helping the entrepreneur to get his / her business going? How is this focus reflected in the legal relationship? For example, will such debt holders be likely to refrain from asking for security? Is the agreed interest rate likely to correctly reflect the risks for the debt investor?

The main intention of the so called "FFF" to invest in a start-up business is surely to make an entrepreneur's project possible and getting his business started. Although banks accept to give loans for startuppers under certain circumstances (e.g. to acquire assets or provide an overdraft facility) it is admittedly quite difficult to obtain traditional debt financing in this phase, especially since the financial crisis and the introduction of more stringent minimum capital requirements for the banks.

Most commonly, investors in this phase provide equity instead of debt capital, e.g. in the form of a silent partnership or a minority shareholding with additional funds provided by way of an unsecured, subordinate shareholder loan or shareholder's contribution. Crowd-funding is another way of raising additional equity in the start-up phase, which is becoming more and more popular.

Professional investors might provide venture capital or other forms of mezzanine financing, although generally such forms of financing are rather used in the growth

phase.

Finally, an entrepreneur might find a so called "business angel", who provides not only equity, but also know-how and business contacts to enhance the startupper's business.[2]

Providing debt capital in the start-up phase is usually considered a high risk investment for various reasons, such as:

- the start-up is very likely to not make any profits for the first few years after its coming into existence and even if profits are made they are generally immediately reinvested into the business;
- there might not be a lot of securities available; either assets are not yet available or must be kept free of liens to get the business started;
- a high number of start-ups fail within the first five years of business.

A private "FFF" investor will aim at supporting the entrepreneur rather than possibly making a profit from his investment. A family lender will most likely not request any collateral, accept little or no interest and flexible repayment terms (e.g. backended repayment) and/or subordinate its debt in case of insolvency. It might also be the case that the repayable interest is defined as percentage of the generated profits (i.e. profit-participating loans) meaning that no interest is payable when losses are made.

1.2 In your experience, is it common for professional investors to act as debt holders in this phase? If so, how is the different focus of professional investors typically reflected in the legal relationship? What are the legal instruments commonly used in your jurisdiction to protect their interests? For example, is it common for the professional investors to request a personal security by the entrepreneur in case the company does not yet have (a lot of) assets to secure a loan?

It is not very common that a professional investor provides debt financing in the start-up phase. If they do so, they will most likely only be interested to take on these risks if a well drafted, promising business plan, marketing plan, financial plan, market analysis and a SWOT (strengths, weaknesses, opportunities and threats) analysis are provided and if sufficient equity capital is existent to get the business started. Professional investors who provide debt financing in this phase will most likely be mezzanine lenders and have knowledge of the anticipated business. In return for taking on high risks, professional investors will expect a high return in case the investment pays off. Legally, this will very often be reflected by the agreement of high interest rates. In return, the legal relationship will be characterized by little or no

[2] In Austria, there is a business angels network called „i2", available online under www.business-angels.at.

collateral, possibly a deferred/backended repayment as well as subordination of the loan. Typical collateral in this phase might be a personal guarantee by the entrepreneur, restrictions on the distribution of profits, the obligation to create further collateral in the future or a pledge of shares or option rights to transform their debt into equity in case the investment might be at risk ("convertible loans").

2. Growth phase

2.1. In your experience, who provides debt in this phase and what could typically be their focus (e.g., high return on investment)?

- **Are the debt holders and their focus in the growth phase typically different from the ones in the start-up phase? Is it now mostly professional investors (and no FFF)?**
- **If there is a difference, how could this be reflected in the contractual relationship? For example, do the interest rates or the security for the debt change?**

2.2. What kind of security is commonly request by debt holders in this phase? For example, rather collateral (pledge, etc.) or personal guarantees by the entrepreneur? What is the reason for the preference of a specific kind of security?

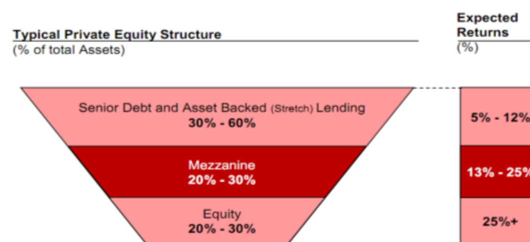
2.3. During the growth phase, the burn rate of the company may be quite high and the company may continuously be at the verge of over-indebtedness. Will investors usually be willing to subordinate their debt? Usually only the entrepreneur / FFF from the start-up phase or also professional investors?

2.4. Investors providing debt in this phase may wish to keep the possibility to participate in the potential valuation upside. How could this wish be accommodated in your jurisdiction? For example, are profit-participating loans or convertible loans commonly used instruments?

The more established a company / business undertaking gets, the more likely will it get interesting for professional / institutional investors. The risks that an investment into a growing company is lost, are lower than for the start-up phase; however, the undertaking can still not be considered stabilized and therefore taking out debt will still be more expensive for a company in the growth phase than for a well established matured undertaking.

The growth phase is most interesting for private equity institutions and particularly mezzanine financiers. Mezzanine financing is most commonly used when a positive cash flow was established and when the company has entered into the growth

and/or expansion phase. Their focus is on a high investment return (about 13% to 25%). A mezzanine loan will constitute an equity substitute for the entrepreneur in obtaining a traditional senior loan, thus being only one source of financing in the growth phase. Typically, the capital structure in the growth phase will look somewhat like this:



[3]

Typical characteristics of a mezzanine loan are

- involvement and assistance in the management of the company;
- subordination to senior loans;
- little or no collateral;
- flexible repayment, often backended and dependent on profits;
- high interest rates;
- term of financing usually between 5 and 10 years; and
- equity kickers.[4]

Typical instruments of mezzanine financing are convertible subordinated debt, subordinated loans, participating loans or high yield bonds.

Senior lenders in this phase will demand lower interest rates, but more security than mezzanine lenders. Also, a certain portion of equity will be required for the senior lender to provide the loan. As concerns the required collateral for obtaining such senior loan, this will depend on the venture to be financed, the assets and other collateral available and the debt-equity ratio of the undertaking. There seems to be a preference for "hard" collateral, meaning asset-backed financing rather than relying

[3] Source: Management Magazine, Bond Capital, Exhibit 2.

[4] An equity kicker is a type of equity incentive typically issued in combination with privately placed subordinated or mezzanine debt to improve the return for subordinated debtholders. Equity kickers can have a convertible feature exchangeable for shares or warrants to purchase shares at a set price at some point in the future.

solely on personal guarantees.

3. Maturity

3.1. In your jurisdiction, who is usually the debt holder in the maturity phase (e.g., banks)?

- **Are the debt holders and their focus in the maturity phase typically different from the ones in the start-up or growth phase?**
- **If there is a difference, how may this be reflected in the contractual relationship?**

The more an undertaking matures, the "cheaper" debt capital gets. A well established, matured company will have entered into the profit zone, will have acquired assets which can be used as collateral and will have established a certain trusted market, making it more likely for traditional debt holders, such as banks and investment banks or other institutional lenders to provide debt capital, whose focus is on lower risk investments.

Contractually, this is reflected in lower interest rates, more collateral, but, however, less involvement in the management of the company.

3.2. Before providing debt to a company, the potential debt holder may require information about the company's financial status to assess the default risk. What financial information is publicly available for potential new investors who wish to invest in a privately-held company? Are financial statements available from public registers? Excerpt from the debt enforcement register? Tax returns? Do companies have means to influence the amount of publicly available financial information?

The Austrian Commercial Register ("*Firmenbuch*"), which is publicly available to any interested party, provides certain information on privately-held companies. Depending on the size of the company (§ 221 UGB), the following information must be provided:

- Small limited liability company: reduced balance sheet plus annex pursuant to § 278 UGB by use of standardized forms;
- Small and medium-sized stock corporation, medium-sized limited liability company: reduced version of balance sheet, profit and loss statement and annex pursuant to § 279 UGB;
- Large limited liability company and stock corporation: annual report and management report pursuant to § 277 para 1 UGB; corporate governance

report; supervisory board report; proposal of the distribution of profits; resolution on the distribution of profits; the large stock corporation must further publish its annual report in the Vienna Public Gazette "*Amtsblatt der Wiener Zeitung*".

Very commonly potential debt holders also make an inquiry on the creditworthiness of a potential borrower with a credit check institution, such as the "*KSV 1870*". Enforceable debts are also available in a separate court register, the so called "*Exekutionsregister*".

3.3. In your jurisdiction, is it common for privately-held companies to issue notes? Could you provide a short overview of the requirements and the procedure relating to the issuance of notes? Is the focus of note-holders any different from other debt holders?

It is not very common for privately-held companies to issue notes, in Austria. It does, however, not seem that the focus of note holders would be any different than that of traditional debt holders in this phase. The interest lies in a rather low risk investment for a medium to long term with a stable return.

4. IPO / Listed

4.1. Once a company is listed, the debt holders have a considerably higher level of information regarding the company's financial situation. One could expect that this reduces the risk for the debt holder. Thus, in your jurisdiction, do listed companies usually have to pay lower interests?

4.2. In your jurisdiction, is it possible to list notes? Could you provide a short overview of the requirements and the procedure relating to the listing of notes? In your opinion, is the focus of holders of listed notes any different from the focus of other debt holders?

As mentioned before, Austrian companies rarely perform IPOs, so it is difficult to provide for generalized statements. There is no information available that listed companies usually pay lower interest rates.

It is possible to list notes in Austria, however, the market is not of great significance.[5]

5. Acquisition

5.1. In your jurisdiction, what is commonly the effect of a public tender offer on listed notes. Do they have to be redeemed? Can holders of listed notes

[5] Given the low importance of this tool in Austria, we have abstained from outlining the procedure of issuing and listing noted in Austria.

interfere in the process of a public tender offer? If so, by which means?

5.2. In your jurisdiction, what is the typical influence of a public tender offer on existing credit facilities?

We have abstained from elaborating on the questions under this section as this is not of great significance in Austria.

C. Interest of Management / Employees

1. Acquisition

1. Start-up phase

1.1 Which are the most commonly used means to ensure that the management / key employees will not leave the company until the company reaches the growth or maturity phase? Are warrants or similar incentives granted during this stage?

In our experience, warrants and similar incentives are not common in the start up phase of undertakings, rather management and key personnel will be granted a small direct stake in the company's equity.

Another common option might be the conclusion of fixed term contracts to avoid the premature termination by the employee.

1.2 It is likely that at this stage, there are not sufficient funds for remuneration of management / key employees. Is it common to grant warrant or stock incentive schemes in your jurisdiction? Is there any other scheme to liaise with this issue?

See already item C.1.1, in our experience it is rather rare to offer warrants or stock option schemes at the start up phase, also because the corporate forms usually used for start ups (LLCs or partnerships) make it difficult to implement such schemes. Rather, management and key employees are often offered equity. An even more common scheme would be to base a considerable part of the salary (bonuses) on key performance indicators that are dependent on certain economic indicators, e.g. EBIT.

2. Growth phase

2.1 In case new investors come on board in the growth phase and such investors request replacement of the current management: in such replacement, does the current management usually lose rights granted under an incentive plan? How broad are "bad leaver" provisions usually formulated?

Distinguishing between "good leaver" and "bad leaver" terminations is common with respect to employment agreements for key personnel. If the replacement of the initial management is triggered by (new) shareholders/investors, the termination will regularly be considered as a "good leaver" termination, so the terminating manager will regularly not loose rights under an incentive plan.

There is in our view no general standard for "bad leaver" provisions, but generally speaking bad leaver clauses try to include any termination of the employment relationship caused by the employee. This will usually include the termination by the employee without just cause, or the termination of the employment relationship by the company for cause. Usually "bad leaver" provisions are worded quite balanced.

2.2 Upon implementation of an incentive plan, the rights related to the shares that the management will be entitled to receive are usually subject to vesting. Is there any specific vesting period that is applied in your jurisdiction or is the vesting period usually linked to a liquidation event (such as an IPO)?

No, there are no statutory vesting periods and in our experience the vesting period is usually also not linked to liquidation events.

2.3 In certain jurisdictions the management may fall out of labor relationship since it is developing executive duties for the company and/or may hold certain stock of the company (it might fall in a special labor relationship or corporate relationship). Is this the case in your jurisdiction? If so, is the loss of labor rights compensated by special laws or by contractual means?

No, in Austria also the management is subject to (regular) employment law, but executive employees (*leitende Angestellte*) are exempt from certain employment law provisions, for example working time restrictions.

3. Maturity

3.1 In your jurisdiction, do the various corporate bodies (e.g., board of directors, directors, management) have

- **an obligation to "act in the best interest of the company"? If so, how is the "interest of the company" defined? Is it the interest of all stakeholders (including the interests of all equity holders (e.g., holder of non-voting shares), debt holders, management, employees and public) or just the shareholders? Are only long term interests taken into account or also short term interests?**
- **"fiduciary duties" or a duty to treat equity holders equally? How are these defined?**

In corporations (Stock Companies, LLCs) the management is subject to very strict fiduciary duties or duties to act in the interest of the company. There is no express catalog of duties, but in each case the managing directors have to manage the company with the care of a "prudent businessperson". The duties are generally very much focused on the interests of the company itself, and not so much on the interests of its shareholders. Austria also has very strict capital maintenance rules also applicable to non-listed stock companies and even small LLCs (that are in our experience much stricter than capital maintenance rules in most other European jurisdictions). These rules focus very much on leaving the company and its assets intact and prohibit any cash or asset transfers to the company's equity holders and affiliates that do not meet the arm's length standard (understood in a very strict way). The main focus of these rules is not the protection of equity holders, but the protection of the company's creditors.

On the other hand, the management of partnerships is subject to less strict rules, mainly because with respect to partnerships the managing partners are subject to an unlimited liability.

3.2 In your jurisdiction, how are conflicts of interest addressed by the law? Are the rules on conflicts of interests for listed companies applied to non-listed companies? Have the rules on conflicts of interests become more rigid in recent years?

The rules deviate to some extend between different forms of companies, but generally, applicable provisions require executives that are subject to a conflict of interest to have measures decided by non-conflicted board members or alternatively have such measures approved by other corporate bodies like the supervisory board or the shareholders meeting. Further, managing directors of corporations are subject to strict non-compete obligations set out in general employment law.

In addition, the strict capital maintenance rules applicable to corporations already mentioned above will usually also act as a deterrent for the management to act against the interest of the company, as any infringement of the very broadly understood arm's length principle will lead to a direct liability of the infringing managing director.

Recently, the legislator has also implemented certain further rules with respect to conflicts of interest in corporations, e.g. expressly requiring supervisory board approval for contracts with supervisory board members and implementing an express duty for supervisory board members to disclose conflicts of interest.

3.3 In your jurisdiction, is it common to put in place incentive plans for key management and employees or are they only entitled to receive a cash bonus (usually based on individual and overall performance)? Do incentive plans provide tax advantage for the company?

Although it is hard to quantify, we believe that incentive plans by way of direct equity participations or options are quite common in the "maturity" phase. There are no express tax advantages for options, which are considered to be part of the overall compensation. On the other hand, direct equity participations are subject to a different tax regime than regular salaries and under certain circumstances the applicable tax rates might be beneficial for the respective employee, but this very much depends on the details of the company and the situation of the respective employee.

4. IPO/ Listed phase

4.1 It is our understanding that when a company goes from a private to a public setting it implies considerable changes for management and employees. In your experience and within this framework, what is the most significant change for management and employees? Does going public usually increase the total amount of the compensation and/or does it usually change the structure of the compensation (cash, shares, warrants, etc.)?

We need to note that Austrian companies rarely perform IPOs, so it is difficult to provide for generalized statements.

We still think that usually going public will lead to an increase of the compensation of the management and will generally also lead to a shift of the compensation towards incentive based forms of compensation like for example stock options, or remuneration that is based on the share price. This is mainly because these instruments are more easily available and administered once the shares of the company are traded on a stock exchange.

4.2 Following the IPO the management is constantly assessed by the performance of the share price. Also the management's pay may to large extent depend on the share price performance. One could expect that management may abstain from taking any steps that are likely to weaken the share price – even if such steps are beneficial to the company in long term. In your jurisdiction, are there any measures that are commonly taken to address this conflict (i.e., incentives for long term strategies)? Is, for example, by law or by agreement a part of the pay paid in mid- to long term options?

Answered together with next question, please refer to item 4.3.

4.3 Is the management and/or employees bound by a mandatory lock up period upon the IPO? In the event the lock up period is not mandatory, please explain the common standards in your jurisdiction towards implementing a lock up period.

Again, due to the fact that IPOs are very rare among Austrian companies it is difficult to speak of general trends in this respect. Generally, we believe that the most common instrument to achieve incentives for a good long term performance of the company are (contractual) lock up or waiting periods for exercising options. There are no statutory rules providing for standard or mandatory holding periods, but the (non-binding) Austrian Code of Corporate Governance encourages that these instruments are implemented in a way to secure the long-term performance of the company.

5. Acquisition

5.1 The focus of the board of directors of a listed company may be set to a large extent on the share price performance. Usually, this should be in line with the corporate interest. However, in case a listed company is being approached by a potential bidder, the board of directors and the management of the potential target may face a conflict of interest: an acquisition that may be beneficial to the shareholders of the potential target, may at the same time require replacement or adjustment of the target's board of directors and management. In your jurisdiction, how is this conflict of interest addressed? For example, are there limits to the defense measures that the board of directors of the target may take?

Most notably, the Austrian Takeover Act explicitly sets out that the management board and the supervisory board must be objective and must not take any measures that might have an impact on the shareholders making a free and informed decision on the takeover bid. Therefore, the management board must not make wrong or unfounded statements that might influence the decisions of the shareholders, or withhold relevant information. Of course, also statements that might result in a market manipulation are forbidden.

Further, according to the Austrian Takeover Act any measures that might prevent the takeover have to be approved by the shareholders meeting (with the exception of the search for an alternative bidder). Such measures include acts that reduce the shares available for being acquired, the issuance of new shares or also the premature announcement of the offer. Further measures that will regularly need approval include the sale of material assets or participations, the acquisition of other undertakings or participations, or the conclusion of agreements with change of control clauses.

5.2 Which are the common alternatives in order to keep management / key employees focused and keen to continue in the company?

The most common solution to secure the continued commitment of management and key employees is quite obviously an increase of the remuneration, often paired with long term employment commitments and appropriate awards for remaining with the company (e.g. stock options that are only vested after a certain time period).

5.3 In parallel, is it common to reinforce non-competition and confidentiality undertakings of the management / key employees upon acquisition? Is it common to regulate a non-solicitation by the Seller and that it is enforceable (for which period)?

We do not think that non-compete or confidentiality undertakings of the management are usually of particular importance for acquirers of a company, because these issues are usually already dealt with by the existing employment agreements of the management. As already mentioned above, the focus usually lies more on the adaptation of remuneration based issues.

On the other hand, non-solicitation undertakings by the seller are frequently agreed by the parties. Restrictions for such undertakings mainly result from competition law prohibitions. There are no fixed maximum periods in this respect, but we would not recommend to exceed the periods usually allowed for non-compete clauses (2 or 3 years depending on the circumstances).

D. Interest of Advisors / Lawyers

1. Start-up phase

1.1. Which are the common difficulties you liaise with during this stage? How do you tend to structure your fees (for example, do you go below your standard rates and agree to have this difference compensated at a later stage when the company has become more successful)?

For advisors and lawyers, the most common difficulty is the entrepreneur's lack of funds in this phase for such services as legal advice. There are a lot of free services available to start-up companies, in particular through the *Wirtschaftskammer Österreich*, the Austrian Chamber of Commerce, which provides free legal advice on corporate law issues, social security, trade law matters and other relevant fields of law for startuppers. The so called "*Gründerservice*" of the Austrian Chamber of Commerce also provides and informs on certain benefits that start-ups may profit from (e.g. exemption of certain registration fees, state subventions and sponsorships).

For start-ups, which from the start are provided with better funds, and who wish to employ a lawyer from the start, we try to find an individual fee arrangement that takes into account the entrepreneurs possibilities, in order to establish a longer lasting relationship with the (new) client. For certain standardized tasks, such as the

establishment of a limited liability company or the draft of a standardized shareholder agreement, we sometimes also offer a flat rate, making our fees more predictable to the client.

1.2. In case you accept warrants / rights to shares as compensation for professional services rendered: how do you set the amount or the value of such warrants and rights? Do you rely on valuations of the company? If so, whose valuations? Is it common for an advisor in this situation to request that the company has previously successfully completed a minimum viable product ("MVP") stage which reduces the risk of failure (i.e., as part of the lean startup methodology it is advisable to diminish uncertainty for the project by means of developing an MVP to validate the project)?

We generally do not get involved in the management of the start-up. Also it is not common to accept rights to shares in return for professional services.

2. Growth phase

2.1. How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to the start-up phase)?

In the growth phase, the company will have established a positive cash flow and has possibly entered to profit zone. It will therefore be easier to agree on standard rates. Very often, we will provide tailored fee arrangements like fee caps for specific projects (e.g. acquisitions) in this phase or reduced rates when certain yearly fee thresholds are reached.

2.2. Is it common for advisors (in particular, lawyers) to take board positions during this phase? If so, how is such board member compensated? In cash? Or with exclusivity for providing legal services to the company?

It is generally not common that lawyers take on management board positions. However, should the company have a supervisory board, it might be the case that a lawyer is taken on as a supervisory board member. Such board member is compensated in the same way as any other board member. Should a lawyer accept a supervisory board position, there are certain restrictions that need to be respected for legal representation of the company, in particular may that supervisory board member (or his law firm) not act as legal advisor in matters, and as such, may not receive any fees with respect to services provided in such matters, which are legally regarded as being part of the supervisory board's duties. Furthermore, the supervisory board must approve any appointment of one particular supervisory board member as legal advisor of the company.

2.3. As the lawyer you may be asked by the entrepreneur to render advice on the

division of equity (in particular to FFF)? What is the basis for your advice regarding the division of equity?

When advising on the division of equity in the growth phase, it will largely depend on the extent of the involvement of the anticipated investor. Generally it will seem important for an entrepreneur to maintain control of his company, thus to maintain either a simple or qualified majority in the company.

2.4. In certain jurisdictions corporate law is rigid and does not allow to regulate certain rights of the shareholders in the by-laws of the company (such as, preferential preemptive rights, drag along or tag along rights). Please explain (succinctly) which is corporate legal scheme that applies in your jurisdiction. Is the shareholders agreement enforceable against third parties in your jurisdiction or is only binding between the relevant shareholders?

As regards the regulation of rights between the shareholders, there are basically two instruments which the shareholders may use to regulate their relationship in: the articles of association and a separate shareholders' agreement. The articles of association are a corporate document and published in the Austrian Commercial Register, thus, also being enforceable against third parties. Shareholders may however, wish to regulate certain rights in a non-public document, thus, in a separate shareholders' agreement. This agreement is generally enforceable only between the shareholders. It is therefore advisable to regulate certain rights (also) in the publicly available articles of association in order for them to take effect vis-à-vis third parties.

3. Maturity

3.1. How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to the start-up or growth phase)?

3.2. Are you able to become member of the board of directors of the companies? Do you tend to render more unique advice to companies (while the corporate counsel provides the typical ongoing corporate advice)?

There is no big difference in the way we structure our fees in this phase as compared to the growth phase. Same applies for taking on positions in the management or supervisory board of the company.

The type of advice rendered to companies depends on the company and the way the legal department of the company is structured (or whether there is a legal department at all). It may be that with some clients we are more involved in the day to day business (and, thus, also render the ongoing corporate advice) and with others, we only advise on certain topics or in larger projects.

3.3. From a lawyers' perspective, how is the conflict of interest of the management liaised with (are there any mandatory provisions that apply in your jurisdiction)?

In case of a possible conflict of interest between the company's interest and the individual managing director's interest, we must not represent the managing director and must advise him to appoint his own lawyer.

3.4. Does the anti-money laundering provisions in your jurisdiction have changed the form your render advice?

Not really. However, through the anti-money laundering provisions, more rigorous know your customer requirements for attorneys were introduced under the attorney rules of conduct, when handling funds for clients.

4. IPO / Listed

4.1. How do you structure your fees for an IPO?

The way we structure fees for an IPO /Listing is similar to other mandates. We invoice our services on the basis of the time spent in handling the matter, based on agreed hourly fees.

For certain tasks, such as the preparation of the prospectus, we might agree on fee caps or flat rates, depending on the complexity and extent of our tasks.

4.2. From a lawyers' perspective, which are the main regulatory aspects of offering equity to the public? Is it common that companies reach this stage (in certain jurisdictions becoming a listed company is less rigid)?

When becoming a listed company, the main regulatory aspect is the more rigid regulatory system, starting from the requirements a prospectus needs to comply with, to the regular additional information obligations that a listed company is subject to under banking and stock exchange regulations. In particular the obligation to report certain developments (so called ad hoc notifications) to the Financial Market Authority requires additional resources for a company.

4.3. Is there any specific secondary market in your jurisdiction that allows early startup companies to become listed with the aim of obtaining more equity (given the complexity of becoming a public company in certain jurisdictions a startup company can become listed in a specific market which is less rigid and allow it to obtain other sources of financing, among others)?

A company with less capital requirement may choose to go for a listing on the mid or standard market of the Viennese Stock Exchange, however, we are not aware of a specific secondary market for start-up companies.

4.4. Does the fact of becoming a listed company imply that the lawyers and/or advisors adjust rates their rates accordingly?

No, there is no difference in rates.

5. Acquisition

5.1. Which is most frequent scheme of implementing an acquisition (asset deal vs share purchase deal)?

The most common scheme of implementing an acquisition is by means of a share deal.

5.2. From a lawyers' perspective, which are the main differences within the process of acquiring a stake in listed companies versus private companies?

Whereas the acquisition of shares in a private company legally focusses mainly on corporate and contract law issues, the acquisition in listed companies requires more expertise and preoccupation with regulatory, administrative law issues. In particular, takeover law needs to be considered when acquiring larger stakes.

5.3. From a lawyers' perspective, which are the main steps in your jurisdiction in order that a public entity becomes a private entity as a consequence of an acquisition?

With respect to main steps to be taken for a delisting, please refer to item A.5.3. When certain thresholds are met, a majority shareholder can attempt a squeeze out of the remaining minority shareholders.

5.4. How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to other phases)?

Fees are structured in the same way as in other transactions, pursuant to the agreed hourly rates on the basis of our time expenditure. In an acquisition, very often an extensive fee estimate based on certain qualifications and assumptions will be provided to the client. Particularly in cases, where it can be assumed that the transaction will follow certain standardized proceedings, we will be able to provide a fee cap to the client.