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CJEU provides more clarity on how cross-border mergers affect loan agreements

In a recent judgment, the Court of Justice of the European Union ("**CJEU**") provided a useful explanation of the effect of a cross-border merger on a loan agreement.

In short, the case was as follows: Sparkassen Versicherung AG ("**Sparkassen**"), established under Austrian law, demanded the payment of interest under two subordinated loans that it had granted to Kommunalkredit International Bank Ltd ("**Kommunalkredit**"), established under Cypriot law. Sparkassen granted these loans before Kommunalkredit, as the disappearing company, entered into a cross-border merger with KA Finanz AG ("**KA Finanz**"), established under Austrian law, as the acquiring company. The loan agreements were governed by German law. Alternatively, Sparkassen claimed that, based on creditor protection rules for holders of securities, other than shares, to which special rights are attached, KA Finanz must grant Sparkassen rights of equal value. KA Finanz, on the other hand, argued that the loans were terminated as a result of the merger and no compensation was required under Austrian law.

In order to determine how the loan agreements should be treated following the cross-border merger, the national court of Austria submitted a request to the CJEU for a preliminary ruling on this matter. The Austrian court wished to resolve the issue of the law applicable to the loan agreements. In addition, it sought an interpretation of creditor protection rules in light of a cross-border merger.

The CJEU stated that, based on the EU directive on cross-border mergers, the consequences of a cross-border merger involve all assets and liabilities of the disappearing company being transferred to the acquiring company. The acquiring company automatically replaces the disappearing company as a party to all its contracts, without any need for novation. Consequently, the court ruled that the law applicable to loan agreements before the cross-border merger continues to apply after the merger. Therefore, in this case, German law remained applicable to the interpretation of the loan agreements, to the performance of the obligations under the contracts and to how those obligations are extinguished.

Furthermore, the CJEU determined that the rules protecting the disappearing company's creditors – on which Sparkassen relied in its alternative claim – are those of the national law applicable to that company. The court also clarified that the European creditor protection rules specifically applicable to holders of securities, other than shares, to which special rights are attached will only apply if the relevant securities grant their holders rights that are broader than the mere reimbursement of debts and stipulated interest. For example, this is the case with debentures exchangeable for shares or profit-sharing debentures. The court concluded by stating that these special creditor protection rules grant rights to holders of such securities, but not to their issuer.

As a result of this CJEU judgment, creditors of a company involved in a cross-border merger can now be assured that the merger will not affect the governing law of their loan agreements and, in addition, now have more clarity on which creditor protection provisions will apply.