Austria

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1. MARKET OVERVIEW

1.1 Types of investors

In Austria, private equity is mainly driven by governmental agencies and banks but, to a minor degree, by institutional investors as an asset class. Insurance companies have recently gained increasing importance in the Austrian private equity market.

According to the latest available data (for the year 2017) from the Austrian Private Equity and Venture Capital Organisation (AVCO), the allocation between investors may be summarised as follows:

- governmental agencies: 36.4% (2016: 100%; 2015: 21.2%; 2014: 76.4%);
- banks: 31.8% (2016: 0%; 2015: 0%; 2014: 0%);
- insurance companies: 12.9% (2016: 0%; 2015: 0%; 2014: 0%);
- corporate investors: 7.6% (2016: 0%; 2015: 0%; 2014: 0%);
- unclassified: 5% (2016: 0%; 2015: 0%; 2014: 0%);
- private individuals: 4.2% (2016: 0%; 2015: 74.3%; 2014: 23.6%);
- funds of funds: 1.5% (2016: 0%; 2015: 0%; 2014: 0%); and
- family offices: 0.5% (2016: 0%; 2015: 0%; 2014: 0%).

Pension funds (2017: 0%; 2016: 0%), academic institutions (2017: 0%; 2016: 0%), capital markets (2017: 0%; 2016: 0%), endowments and foundations (2017: 0%; 2016: 0%), other asset managers (including private equity houses other than fund of funds) (2017: 0%; 2016: 0%) and sovereign wealth funds (2017: 0%; 2016: 0%) were not relevant for the Austrian private equity market.

1.2 Types of investments

Fundraising increased from EUR 13 million in 2014 to EUR 197 million in 2017, which is now comparable to the level of 2012 (EUR 194 million). Investments dropped from EUR 106 million in 2014 to EUR 90 million in 2017—the lowest amount since 2013 (EUR 79 million).

According to the data published by the AVCO, private equity investments have been made to the following sectors:

- ICT (Communications, computer and electronics): 39.7% (2016: 25.7%; 2015: 23.6%; 2014: 21.3%);
- financial and insurance activities: 23.9% (2016: 9.6%; 2015: 22.3%; 2014: 10.1%);
- business products and services: 18.1% (2016: 26.7%; 2015: 19.8%; 2014: 26.5%);
- consumer goods and services: 7.4% (2016: 13%; 2015: 8.6%; 2014:

13.5%);
- biotech and healthcare: 7% (2016: 5.6%; 2015: 10.2%; 2014: 13%);
- transportation: 2% (2016: 3.1%; 2015: 0%; 2014: 0.9%);
- energy and environment: 1.2% (2016: 0%; 2015: 7.7%; 2014: 12.9%);
- chemicals and materials: 0.6% (2016: 0%; 2015: 6.7%; 2014: 0.9%);
- agriculture: 0.2% (2016: 0%; 2015: 0.2%; 2014: 0%);
- construction: 0% (2016: 15.7%; 2015: 0.2%; 2014: 0.8%);
- real estate: 0% (2016: 0%; 2015: 0%; 2014: 0%); and
- other: 0% (2016: 0.6%; 2015: 0.6%; 2014: 0%).

In terms of timing, private equity has been invested as follows during the life-cycle of enterprises regarding the invested amounts:
- growth capital: 43.9% (2016: 22.8%);
- buyout: 32.5% (2016: 29.6%);
- start-up phase: 11.6% (2016: 28.5%);
- later stage venture: 8.7% (2016: 15.4%);
- seed phase: 3.4% (2016: 2.2%);
- rescue/turnaround: 0% (2016: 0%); and
- replacement capital: 0% (2016: 1.5%).

2. FUNDS

2.1 Fund structures

The typical legal structures used for private equity funds in Austria are: (1) the "GmbH & Co KG", which is a special limited partnership (*Kommanditgesellschaft—KG*) with a limited liability company (*Gesellschaft mit beschränkter Haftung—GmbH*) as the general partner (*Komplementär*) or "AG & Co KG" if the limited liability company is replaced with a stock corporation (*Aktiengesellschaft—AG*) and the investors as limited partners (*Kommanditisten*); and (2) the stock corporation. Another popular Austrian legal structure, frequently used as special purpose vehicle but less often seen for private equity funds is the limited liability company. In general, the legal forms used to structure Austrian private equity funds are similar to structures frequently used in Germany and to some extent in Switzerland but differ considerably from those used in other countries. Below is a short overview of the main characteristics of these two types of legal structures.

Special limited partnerships—GmbH & Co KG/AG & Co KG

In a limited partnership, two types of partners may be distinguished:
- general partners with unlimited liability (*Komplementär*); and
- limited partners with limited liability (*Kommanditist*), typically the investors.

A limited partnership requires a minimum of one general partner and one limited partner. The general partner(s) is/are entitled to manage and represent the limited partnership. The involvement of limited partners is usually restricted to extraordinary business decisions such as the accession of new limited partners or the dissolution of the limited partnership. However, the articles of association of the limited partnership may contain deviating provisions.

The limited partnership's general partners are jointly and severally liable vis-à-vis third parties together with the limited partnership. The liability of a limited partner is limited to the amount determined as the partner's liability amount (*Haftsumme*) in the articles of association of the limited partnership. In general, limited partners who have provided their compulsory contribution (*Pflichteinlage*) equalling the liability amount into the limited partnership (e.g. in cash, in kind, by not withdrawing profits, set-off with claims or paying a creditor of the limited partnership) are no longer personally liable to the creditors of the limited partnership.

The main benefits of special limited partnerships are: (1) the protection of the investors under the corporate veil since only the general partner is a company with limited liability; (2) the uncomplicated transfer of shares and entry/exit of investors (no form requirement for the transfer of shares in a limited partnership, i.e. no notarial deed required (as compared to shares in a limited liability company); (3) a high flexibility with respect to corporate governance (in particular as compared to stock corporations) with few mandatory rights for investors; and (4) certain tax advantages. However, such special limited partnership features increased administrative costs for the installation and maintenance of a (at least) two tier-structure (limited partnership and limited liability company or stock corporation acting as general partner) as well as different types of partners.

Further, a special limited partnership offers certain tax advantages as it qualifies as tax transparent and, consequently, profits are taxed at the partners' level only. Further, an open fund can easily be created by using the special limited partnership for capital calls. Although there are few strings attached to the withdrawal of profits, attention must be paid to the (relatively strict) Austrian capital maintenance rules: shareholders in a limited partnership are entitled to dividend distributions and liquidation proceeds only; other payments or benefits may qualify as the repayment of capital contributions and may thus be invalid.

Stock corporation (Aktiengesellschaft)

Stock corporations are mainly chosen for: (1) the protection of the shareholders under the corporate veil; (2) their mandatory two-tier management system consisting of a management board (*Vorstand*) acting under the supervision of a supervisory board (*Aufsichtsrat*); (3) the mandatory legal provisions ensuring a comprehensive corporate governance, a certain level of shareholder rights and transparency; and (4) the uncomplicated transfer of shares (no notarial deed required). Further, the shareholdings in the stock corporation are only publicly available in case of a sole shareholder. However, the need for a two tier-management system and extensive corporate governance provisions result in increased costs for installing and maintaining a stock corporation.

The management board is responsible for managing and representing the stock corporation. It acts basically independently from the supervisory board and the shareholders. The management board is not subject to instructions from the supervisory board, the shareholders or the shareholders' assembly (*Hauptversammlung*), whose direct influence on the operations of the stock corporation is therefore limited. Limitations may be set out in the articles of association by the supervisory board or bylaws (*Geschäftsordnung*). In addition to handling the day-to-day business, the management board prepares the financial statements and is responsible for keeping all necessary books and records of the stock corporation. The management board reports to the supervisory board: (1) on an annual basis on fundamental questions of the business policy and the asset, financial and profit situation; (2) at least once per quarter about the course of business and the company's position in comparison to the forecast calculation taking into account future developments; and (3) promptly on critical matters and circumstances which are of significant relevance for the profitability or liquidity of the stock corporation.

Members of the management board are appointed by the supervisory board of the stock corporation for a maximum term of five years and such appointment can be renewed without limitation. The appointment of a member of the management board may be revoked by the supervisory board for good cause only.

The supervisory board is responsible for supervising the management board and consists of at least three members. Any single member of the supervisory board may request a report from the management board concerning matters of the stock corporation at any time. The supervisory board may also inspect and review all books and records of the stock corporation.

Certain important business decisions (as provided for by law and potentially in the corporation's articles of association or bylaws) require the prior consent of the supervisory board.

The members of the supervisory board are appointed by the shareholders' assembly. Members of the management board of the stock corporation or a subsidiary as well as employees of the company cannot be appointed as supervisory board members. Prior to the expiration of a supervisory board member's term of office, the appointment may be revoked by a resolution of the shareholders without cause. This resolution requires a three-quarters majority of the votes cast.

Apart from an annual shareholders' meeting required by law, which deals with the approval of the annual financial statements (if the matter is referred to it by the supervisory board), the distribution of profits and the discharge of board members, shareholders' meetings must also be called if requested by a minority of shareholders.

In general, resolutions passed at a shareholders' meeting must be passed by a simple majority. A qualified majority of three-quarters is required for certain subjects, in particular, amendments to the articles of association, capital increases and decreases, changes concerning the legal form of the company, other corporate restructurings such as demergers and mergers as well as voluntary termination of the company, the issuance of authorised or conditional capital, the issuance of convertible or participating bonds, exclusion of shareholders' subscription rights on newly issued shares (*Bezugsrechtsausschluss*) and conclusion of profit transfer agreements.

A listed stock corporation has various disclosure and reporting regulations to meet the demands of the prime market of the Vienna Stock Exchange. Those regulations include, e.g. ad hoc reporting obligations, reporting regulations of the Corporate Governance Code and directors' dealing reports.

2.2 Regulation of fundraising and fund managers

The legal framework for private equity funds in Austria changed significantly with the implementation of the EU Directive 2011/61 on Alternative Investment Fund Managers and amending Directives 2003/41 and 2009/65 and Regulations 1060/2009 and 1095/2010 [2011] OJ L174/1 (AIFM Directive) by way of the (new) Austrian Alternative Investment Fund Managers Act 2013 (*Alternatives Investmentfonds Manager-Gesetz* or AIFMG), the abolishment of the Participation Fund Act 1982 (*Beteiligungsfondsgesetz*) and the amendment of several other Austrian laws, including the Banking Act 1993 (*Bankwesengesetz* or *BWG*), the Capital Market Act 1991 (*Kapitalmarktgesetz* or *KapitalmarktG*), Financial Markets Supervision Act 2001 (*Finanzmarktaufsichtsgesetz*), Securities Supervision Act 2017 (*Wertpapieraufsichtsgesetz*), Investment Fund Act 2011 (*Investmentfondsgesetz* 2011 or *InvestmentfondsG*), the Real Estate Investment Fund Act 2003 (*Immobilien-Investmentfondsgesetz* or *Immobilien-InvestmentfondsG*) as well as certain tax laws to the extent relevant.

Most Austrian private equity funds qualify as alternative investment funds (AIFs), being collective investment undertakings which raise capital from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of such investors, without the capital serving a direct operational business and without being a UCITS (Undertakings for Collective Investments in Transferable Securities). The Austrian Financial Markets Authority (*Finanzmarktaufsicht* or FMA) is responsible for the supervision of managers of an AIF (AIFM) in Austria.

The AIFMG introduces primarily regulations on AIFMs, most importantly a requirement to obtain a licence by the FMA. However, an exemption exists for smaller AIFs whose assets under management do not exceed EUR 100 million (including assets acquired by using leverage) or EUR 500 million (for unleveraged funds with no redemption rights within five years following the date of initial investment), which need to register with the FMA only.

According to the FMA, as of 31 December 2016:

- 2,094 funds of Austrian investment companies or AIFMs were licensed for distribution in Austria;
- 21 investment fund management companies (of which 17 were licensed as AIFMs) with fund assets managed in the amount of EUR 167.10 billion existed;
- another four companies were licensed exclusively under the AIFMG and 20 registered AIFMs managed a fund volume in the amount of EUR 1.16 billion; and
- five investment companies for real estate (being alternative investment fund managers at the same time) with a managed fund volume of EUR 6.70 billion existed.

The AIFMG contains a number of structural and organisational requirements for AIFs in addition to defining their regulatory framework; for example, AIFMs need to appoint a custodian for each AIF they manage, which can in general be either a bank or a supervised securities services provider with its seat in the EU or, for AIFs with no redemption rights within five years following the date of initial investment and with the primary investment objective of acquiring control of non-listed companies, an escrow agent (typically a notary public or an attorney-at-law). The AIFMG does not provide for special training of hedge fund managers. In practice, the US qualification of a "Chartered Financial Analyst" (CFA) as well as its European equivalent "Certified International Investment Analyst" (CIIA) have become standard for private equity fund managers. Further, the Austrian "Certified Portfolio Manager" (CPM) qualification becomes increasingly recognised in the private equity sector.

Depending on the scope of activities and actual structure of private equity funds, other Austrian laws may be applicable as well; for example, private equity funds may be required to publish a prospectus according to the Austrian Capital Market Act (*KapitalmarktG*) if certain prerequisites are met.

2.3 Customary or common terms of funds

Private equity funds are generally categorised into closed funds and open funds. Closed funds are—either temporarily or permanently—closed to investors after the initial investment; open funds are open to further investments during the entire investment period of the fund. The incorporation of the fund is usually conditional upon a certain minimum amount of capital being aggregated in both structures.

Further, private equity funds may be differentiated into evergreen funds and closed-end funds based on their investment period and date of effective capital flow. Evergreen funds (or permanent capital vehicles) have an indefinite fund life and operate based on the principle of recycling realised investment returns back into the fund rather than distributing them to the investor. In contrast, closed-end funds have a specific fund life of 10–12 years. Closed-end funds require investors to make a capital commitment that is drawn down from time to time upon notice. At that time at which investors are admitted to the fund (i.e. at the closing), they usually do not fund any portion of their investment amount yet. As in most other jurisdictions, closed-end funds prevail considerably over evergreen funds in the Austrian private equity market.

Depending on the legal form of the private equity fund, the terms of the funds may vary to some extent but are generally similar to those in other jurisdictions. Usually, the management of a private equity fund is performed by a separate limited liability company or stock corporation. A management contract provides the details of the co-operation between the two companies and the responsibility of the management agreement as regards staffing and operation of the fund, the management of the investment process and the control of the investments. The terms of the management agreement are generally comparable to international standards.

Particularly with respect to venture capital, governmental agencies such as Austria Economic Service GmbH (*Austria Wirtschaftsservice GmbH*) and the Austrian Research Promotion Agency (*Österreichische Forschungsförderungsgesellschaft*) have also developed sample investment contracts and syndication agreements. These agreements are generally based on, and contain, contractual structures and provisions typically used in other jurisdictions.

3. DEBT FINANCE

3.1 Means of Financing

As in other jurisdictions, private equity investors typically use debt financing in Austria-related mergers and acquisitions (M&A) transactions to reduce the required equity contribution and increase their potential return on their investments. Recently, the predominant position of commercial banks as providers of acquisition financing, typically structured as syndicated loans, is being challenged by direct lending funds. These funds, while typically charging interest at levels higher than banks do, have the advantage of being able to move faster than banks and offer greater flexibility in terms of leverage, structure, repayment terms. Additionally, most direct lending deals only involve one fund which helps to streamline communication between the borrower and the lender. Since most direct lending funds only provide term debt, such funds have been seen teaming up with banks who provide working capital and ancillary facilities.

While the number of direct lending fund deals in Austria has been relatively low so far given the size of the Austrian market, the minimum ticket size of most direct lending funds being EUR 50 million plus and some legal uncertainties, the rise of this new type of financing has been a Europe-wide phenomenon with Deloitte listing 361 European mid-market deals in its Alternative Lender Deal Tracker for 2017 versus just 145 in 2013 and constantly rising since then. Out of those 361 deals in 2017, 81% involved a private equity sponsor, 65% were related to M&A transactions and 82% were structured as first lien, showing the growing importance of direct lending funds for the private equity market.

While there is clear appetite for lending into Austria by direct lending funds, there are still uncertainties around the legal framework applicable to such transactions in Austria. Although private funds are generally regulated at a European level under the AIFM Directive, it was and—for Austria it still is—unclear whether the origination of loans is permitted by AIFs.

Since 2011, the European legislator gradually issued regulations on special forms of AIFs, designed to provide finance to the real economy (European venture capital funds—EuVECA, European social entrepreneurship funds—EuSEFs and European long-term investment funds—ELTIFs). These acts clarified that the granting of monetary loans (i.e. direct lending) constitutes an eligible investment by these special funds. Absent any European legislation on direct lending by AIFs regulated under the AIFM Directive, the European Securities and Markets Authority (ESMA) has taken steps to progress a common European framework for loan origination by investment funds (ESMA, "Opinion on Key principles for a European framework on loan origination by funds", ESMA/2016/596 (2016)).

In Austria, granting of loans (on a commercial basis) generally requires a banking licenses under the Austrian Banking Act (irrespective of whether the lender also engages in deposit taking). Unfortunately, and unlike in many other jurisdictions, neither the regulator has published its view on the admissibility of direct lending of AIFs nor did the legislature issued clarifying legislatives acts. Absent any official guidance by the FMA, it can, therefore, not be ruled out with certainty that lending by AIFs in Austria does not require a banking licence (irrespective of: (1) the mentioned developments on European level and other Member States that would provide arguments why AIFs should be permitted to lend in Austria without requiring a banking licence; and (2) the mentioned ESMA opinion that contains a country annex according to which loan origination by funds is allowed in Austria without stating further details on what basis such conclusion is drawn). Clarification could be sought on a case-by-case basis by asking for the regulator's view to avoid legal risk. Alternatively, careful structuring of the debt financing may avoid the business to be qualified as constituting banking business in Austria.

Lending without a licence may have severe legal consequences which include:

- in case of natural persons (including the respective legal representative of legal persons) administrative fines of up to EUR 5 million or of up to twice the amount of the benefit derived from the breach where that benefit can be determined;
- in case of legal persons administrative fines of up to 10% of the (consolidated group) total annual net turnover or of up to twice the amount of the benefit derived from the breach where that benefit can be determined;
- any agreement on remuneration, in particular interest and commissions, associated with those transactions is void (while the transaction as such remains valid); and
- suretyships (and other accessory security interests) and guarantees associated with banking transactions conducted without the required license are legally invalid.

3.2 Restrictions on granting security

In the case of Austrian limited liability companies, stock corporations and partnerships, with one of the foregoing acting solely as unlimited partner (each a limited liability entity) to provide security or other financial support or assume obligations for the benefit of their direct or indirect shareholders or affiliates, the Austrian capital maintenance rules are applicable. These rules prohibit a limited liability entity incorporated in Austria from disbursing its assets to its shareholders in circumstances other than (most importantly) as a distribution of profits, by a reduction of share capital or as liquidation surplus upon liquidation.

Guarantees, share pledges and any other collateral granted by a limited liability entity to guarantee or secure the liabilities of a direct or indirect shareholder or affiliate are considered disbursements under Austrian corporate law, and thus are invalid and unenforceable if the granting of the guarantees or security interests by the Austrian guarantor or security provider were not on arm's-length terms, or for that guarantor or security provider's corporate benefit (an overall group benefit is not sufficient).

To reduce the risk of violating the Austrian capital maintenance rules and the resulting invalidity and unenforceability of upstream and side-stream security, limitation language is commonly used according to which the secured parties agree to establish and enforce the collateral against the Austrian guarantor or security provider only to the extent that such establishment and enforcement do not result in a breach of the Austrian capital maintenance provisions. It should be noted that limitation language does not enhance the value of the upstream and side-stream security but ensures that the entire security interest is not void.

The legal ramifications set out above generally do not apply to the extent that an Austrian entity secures amounts owed by itself in its capacity as borrower under the finance documents or, under certain circumstances, amounts which are on-lent and outstanding.

According to the Austrian Stock Corporation Act 1937 (*Aktiengesetz* or AktG), any agreement relating to the granting of an advance payment or a loan, or to the granting of security by a joint stock corporation to another person for the purchase of shares in the corporation or parent company of this corporation, is invalid. In addition, collateral provided by the target stock corporation for acquisition indebtedness in general violates the Austrian capital maintenance rules. Further, based on the AktG, even in cases where the capital maintenance requirements would not be violated, the participation of the target company in any financing by way of providing security interests would violate the Austrian financial assistance rules. Contrary to the capital maintenance requirements, such violation would not render the transaction null and void but it would result, at a minimum, in the potential liability of the management.

3.3 Intercreditor issues

Austrian law does not restrict the subordination of claims. Typical intercreditor issues encountered in other jurisdictions are therefore not relevant for Austria.

3.4 Syndication

Few banks are willing to take the risk of carrying out bigger deals all by themselves.

The underlying documentation is usually based on international standard documentation, in particular the standards of the Loan Market Association (LMA).

4. EQUITY STRUCTURES

4.1 Role of management

In recent years, private equity transactions in which the management is offered the opportunity to acquire (minority) shares in the target have become more frequent. Such structures are based on practical considerations since the investor usually has a strong interest in ensuring management's loyalty and commitment, in particular if the investor lacks the knowledge relevant for operating the business of the company or if the name of a management member is usually linked to the target company.

4.2 Common protections for investors

Typical protection mechanisms for investors (which would typically be set out in a shareholders' agreement or in the articles of association, which are publicly available) include:

- thresholds for decisions in the shareholder's meeting aligned with the

investors' stake in the company;
- nomination and removal of the management board and the supervisory board;
- transfer restrictions for other shareholders (e.g. tag along rights, rights of first refusal pre-emptive rights and anti-dilution provisions in favour of the investor);
- investment guidelines in relation to capital expenditures;
- step-in or swamping rights granting the investor additional voting rights in certain default situations;
- certain other restrictions on the management activities, including provisions for conflicts of interest; and
- reporting duties of the management on a regular basis and information rights in favour of the investor.

In order to facilitate a potential exit from any investment, drag-along rights are frequently agreed upon.

4.3 Common protections for management

If the management is holding shares in the target, the following provisions protecting the management may frequently be agreed upon:
- tag-along rights (enabling management members to sell their shares at the same time and under the same conditions as the majority shareholder(s));
- veto rights concerning certain important decisions; and
- anti-dilution provisions primarily designed to prevent a squeeze-out of the management (pursuant to the Austrian Squeeze Out Act 2006 (*Gesellschafter-Ausschlussgesetz*) since a 90% shareholder in a limited liability company or stock corporation may decide on a squeeze-out of the minority shareholders.

In addition, management holding a minority interest in the company will usually try to protect their function as managing directors by adapting the respective provision in the target's articles of association and/or shareholder's agreement in order to prevent the management from being revocated without factual justification.

Notwithstanding the above, the shareholder rights of managers are usually bounded.

4.4 Management warranties

Management's warranties do not seem to be of particular importance in Austrian private equity transactions. However, private equity investors usually expect to receive a confirmation of the correctness and accuracy of representations and warranties both from the selling entity and the management.

4.5 Good leaver/bad leaver provisions

Typical good leaver provisions agreed upon in Austrian private equity transactions include in particular the following triggering events:
- retirement or death of the manager;
- (lasting) occupational disability of the manager;
- ordinary termination of the manager's employment contract by the

company;
- mutual termination of the manager's employment contract; and
- extraordinary termination of the manager's employment contract for good cause by the manager.

Typical bad leaver provisions include in particular the following triggering event:
- the opening of insolvency proceedings over the manager's estate;
- termination of the manager's employment contract for good cause by the company; and
- termination of the manager's employment contract by the manager other than for good cause.

Whereas the mutual option rights of a good leaver usually provide for the market value of the shares to be paid to the manager, a bad leaver will usually only receive the initial purchase price or even book value of the shares.

4.6 Public to private transactions

Public to private transactions are uncommon in Austria. However, increased interest in such transactions by internationally acting private equity investors has been seen very recently.

5. EXITS

5.1 Secondary sales

A secondary sale is an exit strategy whereby a private equity investor sells its shares held in a company to another private equity investor. There exist various reasons for a private equity investor to choose a secondary sale as exit strategy. In some cases, the private investor may no longer be willing to or simply cannot finance the company anymore but the company is not yet ready for a trade sale or an initial public offering (IPO). In other cases, the company reaches the next stage of its development, requiring a larger private equity investor with sufficient financial resources to fully exploit the potential of the developing business.

5.2 Trade sales

Another common exit strategy is the trade sale whereby a private equity investor sells its shares held in a company to a strategic investor (i.e. someone who is operating in the same industry as the company).

A trade sale may create higher revenues for the selling private equity investor than a secondary sale due to certain synergy effects which the acquisition may create for the buyer within the same industry sector. A disadvantage of a trade sale compared to a secondary sale may be seen in the potential know-how transfer to the potential buyer being a company's competitor during the buyer's due diligence exercise.

Both secondary sales and trade sales can be carried out rather fast, whereas realised gains are usually lower than in an IPO. Most exits in the Austrian market therefore take place in the form of secondary transactions or trade sales.

5.3 Initial public offerings

IPOs are the preferred exit strategy for private equity investors since there are good chances: (1) to achieve a fairly high revenue; and (2) that the target's management supports the IPO (as other exit strategies would create more uncertainty for the management regarding their future employment by the company). On the other hand, an IPO requires substantial preparation both in terms of time as well as costs and entails various liability issues in connection with the prospectus. Further, due to contractual lock up provisions, private equity investors may often only partially exit from the investment by way of an IPO. Even 10 years after the financial crisis, the statistics shows that the Vienna Stock Exchange has a low level of activity but, in 2017, BAWAG Group AG had a successful stock exchange listing.

5.4 Refinancings

Leveraged recapitalisation

A leveraged recapitalisation is an exit method whereby a company being held by a private equity investor issues new debt in order to repurchase its own shares from the private equity investor. The company raises the necessary capital by taking out a bank loan or by issuing bonds. Under Austrian law, the acquisition of own shares underlies very restrictive provisions and is possible for stock companies (*Aktiengesellschaften*) only. Such exit strategy is thus very uncommon in Austrian legal practice.

5.5 Restructuring/insolvency

Liquidation

A liquidation is often used as a last resort since the selling private equity investor does not benefit from the company's going concern value. The private equity investor decides either voluntarily, or becomes forced by insolvency proceedings, to terminate the company's business and liquidate the company subsequently. Rapidly expanding companies which are not able to come up with the necessary liquidity are exposed to a high risk of ending up in liquidation.

6. TAX

General

Individuals having a domicile (*Wohnsitz*) or their habitual abode (*gewöhnlicher Aufenthalt*) in Austria are subject to income tax in Austria on their worldwide income. Individuals having neither a domicile nor their habitual abode in Austria are subject to income tax only on income from certain Austrian sources. Individual income tax is generally levied at progressive rates of currently up to 50% for annual income above EUR 90,000 and of up to 55% for annual income above EUR 1 million (the 55% maximum rate is designed to be applicable until 2020).

For certain types of income, such as specific types of income from investments (*Einkünfte aus Kapitalvermögen*), special tax rates and rules for the determination of profits and losses exist.

Corporations having their place of management (*Ort der Geschäftsleitung*) or their legal seat in Austria are subject to corporate income tax (*Körperschaftsteuer*) in Austria on their worldwide income. Corporations having neither their place of management nor their legal seat in Austria are subject to corporate income tax only on income from certain Austrian sources. Austrian corporate income tax is generally levied at a rate of 25%.

Both in case of unlimited and limited (corporate) income tax liability, Austria's right to tax may be restricted by double taxation treaties.

6.1 Taxation of fund structures

Investment funds

Based on the Investment Funds Act (*InvestmentfondsG*) or the Real Estate Investment Funds Act (*Immobilien-InvestmentfondsG*) in combination with the Income Tax Act 1988 (*Einkommenssteuergesetz*), a domestic investment fund (or real estate investment fund) generally is subject to a special tax law regime with the core feature that the investment fund itself is not considered a taxable entity and thus not subject to taxation. Rather, the respective income of the fund is allocated to the investors that are generally taxed at that level (according to the "transparency principle").

The special tax regime is applicable if an Austrian investment vehicle actually qualifies as an investment fund or as a real estate investment fund under regulatory law. If an Austrian investment vehicle does not qualify as an investment fund, the tax treatment follows the general tax rules applicable to the respective legal form (see the following points).

As regards a foreign investment vehicle, it is decisive whether it falls within the scope of the definition of a "foreign investment fund" in the sense of the Investment Funds Act (respectively as a foreign real estate investment fund in the sense of the Real Estate Investment Funds Act). In order to ensure that the general taxation regime of an investment fund is applicable also to a foreign investment fund, the management company has to ensure that the earnings of a fund are correctly reported to the *Oesterreichische Kontrollbank*. Otherwise, a less favourable tax treatment would apply.

Middle-Class Investment Companies (Mittelstandsfinanzierungsgesellschaften—MFGs)

After the preferential tax regime for Middle-Class Investment Stock Companies (*Mittelstandsfinanzierungsaktiengesellschaften*—MFAGs) was abolished following a ruling of the European Commission and after the subsequently issued tax regime for Middle-Class Investment Companies (*Mittelstandsfinanzierungsgesellschaften*—MFGs) ended on 31 December 2013, the Austrian legislator in summer 2017 enacted the Middle-Class Investment Companies Act 2017 (*Mittelstandsfinanzierungsgesellschaftengesetz* 2017) with which a new version of the known Middle-Class Investment Company was introduced.

Under certain requirements (at the level of the MFGs and the target), the new regime grants tax benefits to the investors in the MFGs (e.g. dividends from MFGs up to EUR 15,000 per year are tax exempt for individual investors) and the MFGs (e.g. capital gains from certain investments are tax exempt from corporate income tax).

The new provisions seek to give advantages to small and medium-sized businesses in their foundation and growth stadium. However, the Austrian Government notified the new rules as state aid with the European Commission. The new rules coming into effect, therefore, depends on the Commission's approval which has not yet been given.

Corporations

Investment vehicles organised in the form of a private limited company or stock corporation are liable to corporate income tax at a flat tax rate of 25%, provided that a minimum annual corporate income tax in the amount of EUR 1,750 for private limited companies (with certain exceptions and reductions for newly established corporations) and in the amount of EUR 3,500 for stock corporations has to be paid if the regular corporate income tax is below such amounts. Austrian corporate tax law provides under certain conditions (e.g. parent company must own directly or indirectly more than 50% of the shares in the subsidiaries) for the possibility for two (or more) companies to form a tax group. In case of a tax group, all of the taxable results (profits and losses) of the domestic group members as well as losses of foreign subsidiaries are attributed to their respective parent, respectively the group parent. Losses of foreign group members are only attributable to the extent of 75% of the profit of all domestic group members only in the proportion of the shareholding quota in the foreign group member. They are further subject to recapture taxation at the time they are utilised by foreign subsidiary in the source state or in the moment the group member withdraws from the Austrian tax group.

Dividends distributed by an Austrian corporation are generally subject to withholding tax at a rate of 27.5% in case of distributions to individuals and of 25% in case of distributions to corporations. Dividends distributed to beneficial owners which are domestic or EU corporations (or corporations in certain European Economic Area (EEA) Member States) may be exempt from such withholding taxation (depending on the level of the shareholding and the holding period, either no withholding tax must be levied by the corporation at all, or the withholding tax must in a first step be levied, but is then credited against the corporate income tax burden of the shareholder, respectively refunded to the corporate shareholder upon request). Certain conditions and anti-abuse provisions apply. For dividend distributions to non-resident individuals and corporations, withholding tax reductions or exemptions might further be available under applicable tax treaties.

At the level of an individual shareholder, no additional income tax is levied over and above the 27.5% withholding tax levied by the amount of tax withheld (final taxation). The aggregate tax burden of profits earned by an Austrian corporation which are then distributed to an Austrian individual shareholder thus typically amounts to 45.63%.

Increases in value in the shares realizsd by the individual shareholder, such as, in particular, capital gains realised upon an alienation of shares or increases in value upon an exit of the shareholder from Austria under certain conditions are generally also subject to a special 27.5% income tax rate, unless the shareholder holds the shares as business assets and the realisation of capital gains is the main focus of such shareholder's business activity. In case of a corporation as shareholder, dividends are generally excluded from the tax base at the corporate shareholder's level. This exemption provision applies to dividends only, not to capital gains which generally are taxable if realised on the shares in an Austrian company. Capital gains realised on the shares in qualifying foreign participations might be exempt under the international participation exemption regime, subject to certain conditions.

Partnerships

Taxation of partnerships (i.e. general partnerships or limited partnerships) does not take place at the partnership's level but at the level of the general and limited partners of the partnership only (transparency principle).

Certain differences in the tax treatment of the derived income may arise depending on whether the partnership is considered to be carrying out commercial activities (*gewerbliche Tätigkeiten*) or as merely carrying out passive asset management (*Vermögensverwaltung*). The classification of the investment vehicle depends on the individual circumstances and structuring of the partnership. Typical restructurings as well as the leveraging of transactions would, however, be considered as an indicator for commercial activities. Such distinction generally is made on the basis of the partnership's activity and does not depend on whether or not a corporation acts as general partner.

Accordingly, income from mere asset management partnerships is deemed to be income from those assets the partnership is managing. For example, dividend income from shares held by the partnership would be qualified as income from investments (*Einkünfte aus Kapitalvermögen*). Income derived from partnerships carrying out commercial activities is deemed to be income from an active trade or business (*Einkünfte aus Gewerbebetrieb*). This difference might, in particular, be relevant for the tax treatment of potential losses due to the partnerships activity.

Silent partnerships

Silent partnerships are non-corporate legal forms in which an individual or a corporation makes a contribution in cash or in kind to the commercial enterprise of another person.

The silent partnership will not be entered into the commercial register and not disclosed to the public (except for a general disclosure in the annex to the financial statements). The commercial code only contains basic rules and grants considerable leeway for silent partnerships.

For tax purposes, one has to distinguish between typical silent partnerships (*typische stille Gesellschaft*) and atypical silent partnerships (*atypische stille Gesellschaft*).

The typical silent partner only participates in the profits of the company and does not take part in the management or representation of the company, whereas the atypical silent partner also participates in the value of the company.

From a tax point of view, silent partnerships may be compared with the partnership since taxation takes place in the asset of the investors instead at the fund level. Revenues from atypical silent partnerships may be classified as income from commercial activities (*Einkünfte aus Gewerbebetrieb*), whereas revenues from typical silent partnerships generally generate investment income (*Einkünfte aus Kapitalvermögen*). Income from silent partnerships (regardless of the qualification as typical or atypical) derived by an individual is generally subject to income tax at the regular progressive tax rates of up to 55% (and not to a special tax rate of 27.5%).

6.2 Carried interest

The tax treatment of carried interest depends on the structure of the respective model. Generally, all benefits received by an employee from its employment contract are, for Austrian tax purposes, treated as income which is taxed at a progressive rate of up to 55%. This applies to both monetary benefits, such as regular cash remuneration, and non-monetary benefits, such as the free or discounted issuance of shares. However, a qualification as income from capital, taxed at the special rate of 27.5%, might, under certain circumstances, be possible.

In this context, Austrian tax law provides for certain disallowances of tax deductibility which apply to management salaries and golden handshakes. Generally, the amount of salary exceeding EUR 500,000 per year is not deductible.

6.3 Management equity

The benefit from a free or discounted attribution of equity to employees, which generally would constitute taxable income from employment (see ss.6: "General" and 6.2 above), is, under specific circumstances, exempt from taxation up to a maximum amount of currently EUR 3,000 per year.

Under certain circumstances, the tax authorities may requalify payments intentionally made in connection with management equity, which is in the most cases taxed at the special rate of 27.5%, as income from employment taxed at the progressive rate of up to 55%. Conversely, if a manager holds a stake in a capital corporation or a limited partnership with a corporation as general partner, a consideration paid by the company to the manager which exceeds arm's-length terms could be considered as illegal repayment of capital as well as a hidden distribution of dividends.

6.4 Loan interest

Interest from loans granted by the investment vehicle is subject to personal or corporate income tax according to the general principles of taxation as described above.

However, interest payments to shareholders or parties related to shareholders are subject to arm's-length standards. Therefore, interest charged at excessively high rates on loans granted by shareholders or affiliates may (partly) constitute an illegal repayment of capital as well as a hidden profit distribution. If the shareholder is an individual, interest from granting loans would be taxed at the regular progressive income tax rates of up to 55% as, in the case of income from loans not subject to a banking transaction (*Bankgeschäft*), the special tax rate of 27.5% is not applicable.

6.5 Transaction taxes

A transfer of shares is not subject to transaction taxes under the Austrian tax regime. Further, capital duty has been abolished as per 1 January 2016. However, stamp duty (*Rechtsgeschäftsgebühr*) could be triggered in a transaction environment.

Stamp duty pursuant to the Austrian Stamp Duty Act 1957 (*Gebührengesetz*) is linked to the private law qualification of agreements. The following types of agreements, among others, are subject to stamp duty if certain conditions are fulfilled: tenancy agreements for business purposes; assignments (other than in the course of factoring arrangements); suretyship agreements; accessions to debt agreements; mortgages; and settlement agreements.

The stamp duty on loan financings, whether by shareholders or external financing entities, has already been abolished as per 1 January 2011.

Austrian stamp duty is generally only triggered if a document evidencing a dutiable transaction is either:

(1) established in Austria;
(2) established outside of Austria but all parties to the dutiable transaction are Austrian residents for stamp duty purposes (i.e. having a place of management, a representative office, a permanent establishment or a branch in Austria) and either: (a) the transaction concerns an asset located in Austria; or (b) one or more of the parties is entitled or obliged to fulfil its obligations in Austria (e.g. payment of the purchase price, notification of an Austrian debtor etc); or
(3) established outside of Austria but the document is brought into Austria and either: (a) the transaction concerns an asset located in Austria; (b) one or more of the parties is entitled or obliged to fulfil its obligations in Austria (e.g. payment of the purchase price, notification of an Austrian debtor etc); (c) on the basis of the agreement, legally relevant acts are undertaken in Austria; or (d) it is used before a public authority in Austria.

A stamp duty sensitive document evidencing a dutiable transaction might not only be the agreement regarding the transaction itself (or a certified copy thereof) but any documentation (e.g. written confirmations, notifications, reports, protocols, correspondence (including e-mails and facsimile messages), notices etc) which contains certain information about the dutiable transaction, potentially even if it is only signed by one of the parties to the transaction.

7. CURRENT TOPICAL ISSUES/TRENDS

In legal practice, the use of insurance in M&A transactions is gaining popularity among deal professionals in Austria. Influenced by an increasing popularity in other prominent jurisdictions, the number of private equity transactions involving warranty and indemnity (W&I) insurance also increased significantly in Austria. Most popular in auction sales and private equity secondary transactions to bridge the gap between the seller and the buyer on what gets indemnified, the length of time the seller will be liable and, of course, the maximum cap amount that can be recovered by the purchaser, such W&I insurance is also seen stapled in auction sales, i.e. the seller already provides for a specific W&I insurance in the auction process and the purchaser, to remain competitive, must assume such W&I insurance during the process and include it in its offer. The little flexibility remaining for the purchaser concerns the insurance amount as the seller will only accept a very limited (symbolic) cap amount for liability vis-à-vis the purchaser.

Due to the increasing complexity of the regulatory framework for financial institutions, many banking institutions have decreased their investment activities, leaving a gap which cannot be (entirely) closed by private equity investors. In combination with the lack of a suitable legal framework, a considerable decrease in private equity investments has been noticeable despite continuous lobbying activities encouraging the development of a suitable legal basis. After federal elections in 2017, however, the new Austrian Government declared in its government programme (which has political rather than legal relevance) its intention to strengthen the private equity sector as a part of its strategy to bolster the economic position of Austria. Vienna—as Austria's economic centre—thrives to position itself as a hub for Central and Eastern Europe (CEE) private equity activity.[1] For example, Vienna hosts the 0100 conference each year, which is a one-day event covering the range from venture capital and growth capital to buyouts and secondary transactions.

[1] *Zusammen: Für unser Österreich—Regierungsprogramm 2017–2022* available at: *https://www.oevp.at/download/Regierungsprogramm.pdf* [Accessed 26 September 2018].