

A New Life for Bonds under the Reformed Company Law



Gisèle Rosselle
Partner
gisele.rosselle@strelia.com



Cédéric Devroey
Associate
cederic.devroey@strelia.com

Companies can obtain financing not only by issuing shares or by entering into bank financing. It can also obtain financing through the issuance of bonds, which seems to be a popular alternative for acquiring funds, especially for start-ups and capital-intensive sectors such as biotech and high-tech. The information published by the Financial Services and Markets Authority (FSMA) shows that the sums of money collected through bonds reached EUR 605 million in 2017, compared to EUR 495 million in 2016. In the context of the overall modernization and flexibility of Belgian company law, the latest version of the preliminary draft law dated 12 December 2018 and entitled the Code of Companies and Associations (**BCCA**), which reforms the current Belgian Companies Code, provides for more flexible issuance possibilities for bonds. It is now therefore high time to recall and discuss these instruments and to explain the impact that the BCCA could have on all of this.

What is a bond?

A bond is a security that is issued by a company when a loan is taken out in the context of a private or public investment. The bond (i) is a security right that the holder has for the exchange of interest payments and (ii) grants certain rights to the its holders, such as the right to information and participation as an observer at the general meeting. A bond is distinguished from A warrant because a warrant enables the holder to subscribe, under certain conditions, to the shares of the company. However, a warrant can also be linked to a bond. Such an instrument is called a "*bond cum warrant*".

There is also a special type of bond called the convertible bond. It can be converted into shares under certain conditions. The convertible bondholder enjoys the rights attached to the ordinary bond and has the possibility (sometimes the obligation) to switch from bondholder status to shareholder status. A convertible bond should not be confused with the so-called convertible loan, however. The latter is not a security but rather a mere contract that is in principle not governed by the Belgian Companies Code and that stipulates that, under certain conditions, such as in the event of a change of control, the loan can be used as contribution by the creditor towards the company's capital, and whereby the company issues shares in exchange for the contribution.

Why a bond?

The bond is popular because, contrary to traditional bank financing, often no guarantee is provided to the creditor-bondholder, so it's easy to combine it with traditional bank financing. The bond is used to finance the organic growth of the company or to finance specific projects such as an acquisition or a merger. For the shareholders, there is no dilution as to what concerns the ordinary bonds, and the dilution is postponed over time with regard to convertible bonds. Finally, the convertible bond can even be used in certain cases to avert a hostile takeover.

Under the new Belgian Prospectus Law, a sum of EUR 500,000 can be collected under certain conditions through bonds without specific additional requirements. For more than this sum, a prospectus or information note will need to be published, depending on the circumstances. Furthermore, bonds require sufficient repayment capacity (read: turnover) and reputation in order to attract investors.

Who decides to issue the bond?

Under the current law, bonds can be issued by all types of companies, unlike the convertible bond, which cannot be issued by the private limited liability company (BVBA) and the cooperative company (CV).

What is innovative in the BCCA is that it stipulates that the private limited company or the BV, which replaces the BVBA, can now issue convertible bonds. Now that the BCCA makes the private nature of the BV optional, there is indeed no reason to maintain the prohibition to issue convertible bonds. The BCCA does keep the prohibition on issuing convertible bonds valid for the CV because the cooperative nature of this company type is incompatible with the free inflow of potential shareholders.

What are the new terms?

The BCCA states that the conversion can be requested not only by the bondholder but also by the company (*reverse convertible bonds*) or can be automatic, for example, if the stock price is above a certain price for a particular period of time or in case of a change of control. In doing so, the BCCA adheres to the legal doctrine that states that the bondholder's optional right to convert is not an essential characteristic of the convertible bond and the absence thereof does not prevent the qualification of it as a bond within the meaning of the Belgian Companies Code.

In addition, as a deviation from ordinary law (*gemeen recht*), the BCCA provides that bonds with a perpetual term and that cannot be terminated unilaterally prematurely and with a reasonable notice period can be issued. In the same vein, the BCCA states that the conversion period of the convertible bond does not need to be limited to ten years.

Furthermore, under the BCCA, the provisions on the general meeting of bondholders will no longer be mandatory. This means that the company can deviate from these provisions when determining its bond issuance conditions. Under the current law, the general meeting of bondholders unites all bondholders and can, through a majority decision, accept changes to the bond agreement or the substitution through shares. The workings of such general meeting of bondholders are often perceived as cumbersome. But the BCCA will allow the meeting of bondholders to be set aside and provide for other negotiation techniques in the conditions for bond issuance.

If the Parliament approves the BCCA, it will enter into force on 1 May 2019. Companies that are incorporated after that date will be able to benefit immediately from the flexible system offered by the BCCA. Companies that already exist will be able to benefit from the new system for the issuance of new bonds, provided that the company first aligns its articles of association with the BCCA requirements.