

Sweden

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1. MARKET OVERVIEW

1.1 Types of investors

Investors in Swedish private equity funds are typically international and domestic pension funds, insurance companies and other institutional investors but also, in particular with respect to venture capital funds and smaller buyout funds, private individuals. Swedish buyout funds also obtain investment commitments from funds of funds.

Swedish national pension funds are large investors in Swedish private equity and in particular the Sixth AP Fund, which, by the end of 2009, had SEK 1.8 billion in fund capital and ownership interests in approximately 350 companies (both held as direct investments and as indirect investments through private equity funds) (*Sixth AP Fund's year-end report for 2009*).

A relatively new trend is that some Swedish private equity funds have set up publicly traded (or over-the-counter traded) vehicles targeted towards retail and other investors. Such vehicles are typically set up as a 'paid in' structure with the aim of creating liquidity for investors.

In 2008, pension funds (39 per cent), funds of funds (26 per cent) and insurance companies (14 per cent) accounted for the largest part of the SEK 76.5 billion raised by Swedish buyout funds, while corporate investors (40 per cent), private individuals (34 per cent) and pension funds (16 per cent) accounted for the largest part of the SEK 1.5 billion raised by Swedish venture capital funds (according to figures in the Swedish Venture Capital Association's (SVCA) report, *Risikkapitalåret 2008*, the 'SVCA 2008 Report'). From a geographical perspective, 88 per cent of the capital committed to Swedish buyout funds in 2008 came from non-Swedish investors (46 per cent represented investors in other European countries and 30 per cent US investors). For Swedish venture capital funds the situation is the opposite and Swedish investors are by far the most important source of capital representing 88 per cent of the capital committed in 2008 (SVCA 2008 Report).

In 2009, the total amount committed by investors was significantly lower than during previous years and thus the investor situation in 2009 is not representative of the typical investor situation in Sweden. In 2009, banks (37 per cent), funds of funds (23 per cent) and the public sector (16 per cent) accounted for the largest part of the SEK 1.8 billion raised by Swedish buyout funds, while the public sector (51 per cent), 'others' (18 per cent) and corporate investors (16 per cent) accounted for the largest part of the SEK

2 billion raised by Swedish venture capital funds (according to the SVCA's report, *Risikkapitalåret 2009*, the 'SVCA 2009 Report'). From a geographical perspective, 87 per cent of the capital committed to Swedish buyout funds in 2009 came from non-Swedish investors (77 per cent represented investors in other European countries and 9.5 per cent US investors). For Swedish venture capital funds, Swedish investors remained the most important source of capital, representing 86 per cent of the capital committed in 2009 (SVCA 2009 Report).

1.2 Types of investments

The Swedish private equity market is well developed and encompasses all types of private equity transactions, ranging from seed-financing by venture capital funds to leveraged public to private transactions by large buyout funds.

Out of the SEK 10 billion invested by Swedish private equity funds during the first half of 2010 (H1 2010), 86 per cent was invested in buyout and the remaining 14 per cent was invested in venture capital, divided on seed-financing (0.9 per cent), start-up (seven per cent) and expansion (six per cent) (according to the SVCA's report, *Analys av risikkapitalmarknaden första halvåret 2010*, the 'SVCA 2010 Report').

Out of the SEK 14 billion invested by Swedish private equity funds in 2009, 79 per cent was invested in buyout and the remaining 21 per cent was invested in venture capital, divided between seed-financing (0.5 per cent), start-up (10 per cent) and expansion (10 per cent) (SVCA 2009 Report). Out of the SEK 36 billion invested by Swedish private equity funds in 2008, 86 per cent was invested in buyout and 14 per cent was invested in venture capital (SVCA 2008 Report).

The Swedish market has not witnessed many public to private transactions by private equity funds during recent years. However, a few large private equity-backed public offers were made in 2008, such as private equity firm EQT's public offer for Securitas Direct, an alarm monitoring company; private equity firm Segulah's public offer for Gunnebo Industrier, an international manufacturing group; and EQT's unsuccessful public offer for Q-Med, a biotechnology/medical device group. In 2009, only mandatory public offers were made, such as the mandatory public offer by the Swedish-listed investment company Traction for Nilörngruppen, a European leader in labels, and the mandatory offer by the listed private equity company Hakon Invest for Hemtex, a Nordic home textile chain. In 2010, several private equity-sponsored public offers have been announced: in April the US-based private equity fund Providence Equity Partners and EQT each made a public offer for Sweden's largest private educational company AcadeMedia; in June the listed private equity company Ratos invested in HL Display, a supplier of products and solutions for in-store communication and merchandising, and made a mandatory public offer to the remaining shareholders; and in September, following the listed industrial company Alfa Laval's public offer for Munters, a global leader in energy efficient air treatment solutions and restoration services, Nordic Capital, a group of private equity funds focusing

primarily on investments in the Nordic region, made a competing offer for Munters.

The use of leverage in Swedish private equity transactions is highly dependent on the type of transaction and the use of leverage has also been affected by the financial crisis. Leverage is rarely used in Swedish venture capital transactions, but often in buyout transactions. Even if the debt levels have started to increase during H1 2010, they are lower now than before the credit crunch in 2008.

2. FUNDS

2.1 Fund structures

General

The structures most commonly used for large buyout funds in Sweden are offshore limited partnership structures (which in many aspects are similar to the Swedish limited partnerships (*kommanditbolag*)). These structures are tax transparent and well known to foreign investors and thus often viewed as more attractive than Swedish structures, which can be perceived by some foreign investors as complicated, mainly as a result of lack of experience.

Sweden does not have a specific legal form or tax regime for private equity funds. Historically, Swedish limited partnerships were used as the legal structure for private equity funds. However, in 2003 the participation exemption regime was introduced for Swedish limited liability companies, which thus became the most common Swedish legal structure used in recent years. From 1 January 2010, the participation exemption regime is also available for Swedish limited partnerships and this may result in an increase in limited partnership fund structures established in Sweden.

In addition to the traditional private equity fund structures with partner-owned management or advisory companies, there are several other private equity investment structures in Sweden, eg, funds of funds, listed private equity firms (or investment companies) such as Ratos, Hakon Invest and Bure Equity, listed permanent capital vehicles such as East Capital Explorer, state-owned firms and foundations (*stiftelser*) such as Industrifonden and private equity firms owned and financed by large industrial corporations such as Volvo.

Swedish limited liability companies

A Swedish limited liability company is formed by one or more founders, through a memorandum of association, and becomes a legal entity upon registration with the Swedish Companies Registration Office. Shareholders are not personally liable for the company's obligations.

Limited liability companies are regulated by the Swedish Companies Act (Companies Act), which, *inter alia*, includes provisions regarding corporate governance and provisions safeguarding shareholders' rights, such as provisions regarding unlawful dividends, equity protection and minority protection. The corporate governance is based on a three-tier structure: general meetings of shareholders, board of directors and management. The board of directors is the principal decision-making organ.

The shareholders' rights are exercised at the general meetings of shareholders. Most resolutions are passed by simple majority vote but certain resolutions, eg, amendment of the articles of association and new issues of shares with deviation from the shareholders' preferential rights, require higher majority. The relationship between a company's shareholders can also be regulated in a shareholders' agreement. However, such an agreement is in general valid between the shareholders only and not the company.

The board of directors of a Swedish company can comprise both executives and non-executives. However, non-executive directors are more common. The board of directors is responsible for the organisation of the company and the management of its affairs, including the appointment and dismissal of the chief executive officer (CEO). The board members have a general obligation to act in good faith and in the best interests of the company and all its shareholders. The board members are elected at the general meeting of shareholders (with certain exceptions).

The corporate governance regime set out in the Companies Act is perceived by Swedish and other Nordic investors as more robust and investor-friendly than the offshore limited partnership structures since it is based upon clear and transparent rules.

Swedish limited partnerships

A Swedish limited partnership is formed through a partnership agreement between at least one general partner and one or more limited partners, and becomes a legal entity upon registration with the Swedish Companies Registration Office. The general partner has unlimited liability for the debts and liabilities of the partnership, whilst the limited partners' liability is limited to the amount of capital they have committed to contribute to the partnership.

Limited partnerships are regulated by the Swedish Partnership Act (Partnership Act), which includes few mandatory provisions and allows the partners considerable freedom to regulate their affairs in the partnership agreement. As a main rule, the general partner represents the limited partnership, while a limited partner cannot *per se* act on behalf of the limited partnership in order not to jeopardise the limited liability (unless otherwise agreed in the partnership agreement).

2.2 Regulation of fund raising and fund managers

Fund raising

The Swedish regulations on fund raising are set forth in the Financial Instruments Trading Act (Trading Act). Through the Trading Act, Sweden has implemented the European Union's prospectus directive. The Trading Act sets forth rules regarding prospectuses and offer documents to be issued in connection with public offerings and public offers. In order to avoid the prospectus requirements in the Trading Act, private equity firms typically offer fund interests to a limited number of qualified investors through a private placement or has a minimum investment target which exceeds the thresholds for being required to prepare a formal prospectus.

Fund managers

In general, there are no Swedish regulations that specifically regulate or govern private equity funds. There are specific rules for different categories of investment funds, such as undertakings for collective investment in transferable securities (UCITS) and non-UCITS (which are special funds that are subject to the domestic laws and regulations in Sweden). However, private equity funds are not covered by the UCITS directive and are not classified as non-UCITS or 'funds' by the Swedish Financial Supervisory Authority (SFS).

Pursuant to the Securities Market Act, which constitutes the Swedish implementation of the markets in financial instruments directive (MiFID), 'investment firms' that, *inter alia*, provide investment advice within the scope of the Securities Market Act, have to be authorised by the SFS. The investment advice rendered by a private equity firm is typically not considered to be investment advice within the meaning of the Securities Market Act. Consequently, private equity firms generally do not require SFS authorisation (unless they conduct any other business which requires authorisation).

There is currently no statutory transparency nor any corporate governance rules specifically aimed at the Swedish private equity sector. In general, the main duties and obligations of the private equity fund managers, irrespective of the legal structure of the fund, will primarily be governed by the fund agreement with the investors. For funds structured as limited liability companies, the corporate governance regime of the Companies Act applies (as described in section 2.1 above). Corporate governance and transparency have been debated in the Swedish private equity sector and the SVCA is working towards the private equity sector providing greater transparency to its investors and adequate disclosure to broader stakeholders (eg, by the issuance of a code of conduct).

The AIFM directive

In 2009, the European Commission presented the proposed directive on alternative investment fund managers (AIFM directive), with the purpose of establishing a common regulatory and supervisory framework for all investment managers of alternative investment funds (including, *inter alia*, hedge funds and private equity funds) promoted to investors in the EU that are not currently subject to regulation at European level.

The AIFM directive has been subject to substantive criticism and serious concerns remain. As of today, it is difficult to predict the outcome of the final proposal, however, if the AIFM directive is approved, it is clear that the Swedish private equity industry will be affected.

2.3 Customary or common terms of funds

General

The terms of Swedish private equity funds are getting more and more standardised and the commercial terms of private equity funds on the Swedish market do not differ significantly from the rest of the world.

In addition to the Companies Act or the Partnerships Act, a fund is generally governed by a shareholders' and investment agreement or a limited partnership agreement, depending on the legal structure of the fund. There are no statutory limits in Sweden regarding investment periods, amounts or transfers of investments in private equity funds. The agreements usually contain provisions regarding, *inter alia*, corporate governance, investment policy, fees and profit sharing, transfer restrictions, as well as term and termination events.

Buyout funds

The management company of the fund will typically make a commitment to the buyout fund representing a percentage of the total committed capital. The commitment is dependent on a variety of factors, but at least one per cent of the total capital raised by the fund is generally perceived as a 'standard'. The management fee paid by the fund to the management company is generally in the range one to two per cent of the committed capital during the investment period, after which it can be lowered (or remain the same) (the SVCA's Directory and Yearbook 2008-2009, 'SVCA Yearbook 08/09').

The profit sharing between the investors and the private equity firm is generally split 80/20. Typically, the investors are entitled to receive the capital invested together with a preferred return (often corresponding to about eight per cent) on the capital invested before any carried interest is paid or, as is sometimes the case, a 'catch up' is paid to the carried interest holder before the 80/20 split is applied (SVCA Yearbook 08/09).

Venture capital funds

In general, the commercial terms of venture capital funds are structured similarly to those of buyout funds. However, as the fund size of and investments made by venture capital funds are normally smaller than for buyout funds, both the commitment made to the fund and the management fee would typically represent a higher percentage than compared with a buyout fund, eg, committed capital would typically range from three to five per cent of the total capital raised by the fund and the management fee from two to 3.5 per cent of the committed capital (SVCA Yearbook 08/09).

3. DEBT FINANCE

3.1 Restrictions on granting security

According to the Companies Act, an acquisition may not be financed either in whole or part by the acquired limited liability company itself. Thus, the target company is not allowed to grant loans or securities in connection with an acquisition of its shares. In brief, a loan or security granted in violation of these rules is invalid and shall be reversed. Also, this prohibition is subject to criminal liability, ie, it is a criminal offence for the representatives of a target company to participate in such lending.

These rules effectively preclude the possibility of acquiring the target company on the basis of a self-financing structure. However, it is possible for

the acquisition finance loans that have been provided to an acquirer to be 'pushed down' subsequent to the acquisition, provided that the acquisition financing was provided independently from the subsequent push down.

Upstream securities or guarantees from the target company in favour of the buyer's creditors providing the acquisition financing may be made after the completion of the transaction as long as they are not regarded as being in breach of the provisions on financial assistance and not in interference of the rules in the Companies Act on value transfers from a company. These rules, however, are complicated and always subject to detailed analysis.

Various other methods for providing upstream securities for acquisitions financing have been established in the Swedish market place, such as, eg, pre-closing commitments from the buyer and inclusion of limitation language in the financing documents. However, such methods should be carefully scrutinised. In this context, it should be noted that there are no formal whitewash procedures in Sweden.

Statutory mergers between the acquisition vehicle and the target company may be used in order to satisfy the lenders' requirement to have the loans where the cash-flow is. However, a statutory merger could in practise only be effected between private companies, since statutory mergers involving a public company are heavily restricted.

3.2 Inter-creditor issues

Under Swedish insolvency law all creditors have equal right to payment pro rata the size of their claim. However, according to the Swedish Rights of Priority Act (Priority Act) some prioritised and secured creditors have the benefit of payment before other creditors. There are two types of priority rights: (i) specific priority rights which attach to, *inter alia*, pledges and possessory liens, floating charges and mortgages in real property; and (ii) general priority rights, which relate to all property in the debtor's estate. Claims that do not carry any of the above mentioned priority rights or exceed the value of the security provided for such a claim, are non-prioritised and rank *pari passu* as against each other. A claim can also be subordinated, but this requires that the creditor contractually undertakes to be subordinated, for example, by entering into an inter-creditor agreement stipulating such subordination.

In large private equity transactions, with two or more classes of creditors, contractual subordination normally occurs pursuant to an inter-creditor agreement, according to which the junior creditors are subordinated and will not have any rights in insolvency or bankruptcy proceedings until the senior creditors have been repaid in full. As mentioned above, only the actual parties to the inter-creditor agreement are subject to the contractual subordination.

Structural subordination is not common in Sweden; however, it occurs in relation to large leveraged buyout transactions involving international banks. Also, financial assistance issues must be carefully considered in connection with structural subordination.

3.3 Syndication

In general, banks syndicate their loans after completion of the transaction. Syndication before the transaction is completed is very uncommon. As a result of the financial assistance rules, the target company is not allowed to take part in the financing until after the transaction is completed.

3.4 Alternative means of financing

An alternative means of financing, particularly when access to financing is more limited, is to raise funds on the Swedish capital market by issuing bonds, including zero coupon bonds, commercial papers or convertible debt instruments.

Earn-out mechanisms are often used in Swedish private equity transactions, not only to bridge a valuation gap between buyer and seller, but also as an alternative source of financing. Depending on the circumstances, an earn-out mechanism may have adverse tax or competition law implications and should therefore be carefully analysed.

Securitisation is considered expensive and difficult to obtain and is currently not a preferred source of financing in the Swedish market. In addition, it is highly dependent on the activities and assets of the company involved in the securitisation.

4. EQUITY STRUCTURES

4.1 Role of management

Management has a key role in private equity investments. Management's control and influence over a portfolio company is typically exercised in the daily operations of the company rather than through formal board meetings.

It is common for management of the target company to be invited, or required, to invest alongside the private equity investor in the investment vehicle, either by acquisition of shares, warrants or other securities. In connection with such investment the management individuals would be required to enter into a shareholders' agreement with the other shareholders. The shareholders' agreement typically imposes transfer restrictions, good and bad leaver provisions and exit provisions. These agreements should be carefully tailored in order to achieve the desired tax treatment for management's investments (see section 4.5 below).

The employment contracts for management would generally contain non-compete, non-solicitation and confidentiality undertakings. It is also common to stipulate relatively long notice periods should management wish to terminate their employment. Other ways to retain management individuals include long-term incentive programmes and lock-up/in provisions for its equity participation.

4.2 Common protections for investors

The level of protection for an investor in a Swedish limited liability company depends on the level of ownership achieved as a result of the investment. As a general rule, the investor will want to control the board of directors or, if

being a minority shareholder in the portfolio company, at least have board representation and veto rights against important decisions. The investor will also want to secure that a future exit is duly catered for, eg, by drag along provisions and transfer restrictions.

When drafting and negotiating shareholders' agreements, the Companies Act needs to be taken into consideration since a shareholders' agreement is effective between the shareholders only and, in general, not against the company. Depending on the situation, it may be advantageous for an investor to rely on the statutory provisions under the Companies Act. In addition, certain transfer restrictions and other provisions can be included in the articles of association of the portfolio company, thereby securing potential enforceability issues should the parties rely solely on a shareholders' agreement.

4.3 Common protections for management

As described in section 4.1 above, management typically exercises its control in the daily operations of the portfolio company. The level of contractual protection for management is therefore often very limited.

4.4 Management warranties

The warranties provided by management vendors are typically focused on pushing disclosure in the investment process rather than providing financial recourse. Therefore, the scope of the warranties is as a general rule as broad as possible. However, should the management vendors represent a large group of individuals, it would not be uncommon to significantly limit the scope of the warranties (eg, title and capacity) in an attempt to obtain full acceptance of the transaction.

The liability for breach of management warranties is generally very limited compared to other vendors, should the investor wish to retain the existing management team.

4.5 Good leaver/bad leaver provisions

Leaver provisions, together with transfer restrictions, have been subject to debate in Sweden for many years due to the Swedish tax regime. The Swedish Tax Agency has been of the opinion that leaver provisions, and other provisions or restrictions connecting a security to employment, could postpone the acquisition date of the security, or even remove its status as security for tax purposes, and result in capital gains and dividends deriving from the security being taxed as employment income (marginal income tax rate (58 per cent) plus social security charges). However, the Swedish Tax Agency has revised its opinion due to recent rulings from the Swedish Supreme Administrative Court (the highest administrative court), which indicate that standard restrictions and leaver provisions should not result in adverse taxation of the security. The consequence would be that, as a general rule, an acquisition of a security would not trigger taxation if acquired on market terms and any capital gains and dividends deriving from the security should, irrespective of leaver provisions or transfer restrictions, be taxed

as capital income (25-30 per cent). However, the rulings include certain specifics and both lever provisions and transfer restrictions must always be carefully tailored in close co-operation with tax specialists in order to limit adverse tax effects.

4.6 Public to private transactions

General

Swedish public offers are primarily regulated by the Swedish Takeover Act, which is constituted of the Swedish implementation of the European Commission takeover directive, the Trading Act and the Swedish takeover rules as amended and adopted by the two regulated markets in Sweden; NASDAQ OMX Stockholm and Nordic Growth Market NGM. From 1 January 2010, regulations largely corresponding to the takeover rules have been adopted by the non-regulated markets in Sweden; Aktietorget, First North and NordicMTE. The takeover rules are influenced by the UK City's code on takeovers and mergers.

A Swedish public to private transaction is structured as follows; the offeror makes a public offer to the shareholders of the public target company to acquire their shares, normally subject to certain conditions (most importantly the 90 per cent acceptance condition, see section below regarding compulsory squeeze-out procedure). Under the takeover rules, the financing of a public offer shall be in place prior to the offer, thus securing the financing is a key issue that arises in public to private transactions.

Management buyout

In a management buyout, certain special requirements apply for the offer, eg, the target company must obtain a fairness opinion from an independent expert and make that opinion public.

Stake building etc

There are no legal restrictions in Sweden on a potential offeror's freedom to build a stake in a potential target company by acquiring shares in the market. However, the Trading Act requires disclosure of shareholdings in case certain thresholds are achieved. In addition, according to the takeover rules, all acquisitions of shares in the target outside the offer during a period commencing six months prior to the offer and ending six months following closing of the offer may trigger top-up obligations. In addition, the Takeover Act includes a mandatory bid obligation, which is triggered if the offeror has purchased shares in the target outside the offer to such an extent that the offeror controls more than 30 per cent of the voting capital in the target company. The introduction of an additional mandatory bid obligation at 50 per cent is currently being considered.

Compulsory squeeze-out procedure

The Companies Act permits a compulsory acquisition of minority shareholdings (squeeze out) if a shareholder (either alone or together with its subsidiaries) owns more than 90 per cent of the shares of a limited liability

company. In a compulsory squeeze-out procedure an arbitration panel will decide on the fair market value of the shares, but if more than 90 per cent of the shares have been acquired through a public offer there is a presumption that the fair market value is the price in the offer.

In order to obtain control of the minority shares without having to wait for the finalisation of the squeeze-out procedures, the offeror would normally make an advance acquisition of the minority shares against providing security for the purchase price and settlement of the minimum price agreed (normally the price in the offer).

5. EXITS

In the wake of the financial crises, the number of exits within the Swedish private equity sector decreased significantly compared with the number of exits in 2007 and 2006. However, in late 2009 and during H1 2010 the exit environment has started to pick up (see section 7.1 below).

During recent years, trade sales have been the most common exit route for Swedish private equity funds. The second most common exit route in 2008 and during H1 2010 was secondary sales, and in 2009 so-called negative exits were most common (see section 7.1 below).

5.1 Secondary sales

Secondary sales differ from trade sales and IPOs insofar as the selling private equity fund's counterparty is not an industrial buyer or a group of potential public shareholders, but one or several other private equity funds.

Secondary sales were very common a couple of years ago when the Swedish private equity market was booming and very competitive. During this period 'clean break' share purchase agreements, with limited warranties, were common. Because of the competitive market, a potential buyer could never be certain of being the preferred buyer, and thus often tried to limit its costs by conducting only limited confirmatory due diligence at a late stage in the process. This resulted in higher transaction risks.

After the credit crunch in 2008, the number of secondary sales decreased significantly. In 2010, several Swedish private equity funds have a lot of unused committed capital, and during H1 2010 the number of secondary sales has increased compared to 2009. However, the key driver for secondary sales is access to leverage financing and even if the access to leverage financing improved in the first nine months of 2010, it is still different from 2007 and early 2008.

5.2 Trade sales

Trade sales are the most common exit route for Swedish private equity funds and refer to the sale of the shares or the assets of a portfolio company to a strategic industrial buyer. Trade sales typically provide a full exit for the investors and are less time consuming than an initial public offering (IPO). However, trade sales often require approvals from competition authorities because of the activities of the buyer.

In a trade sale, the industrial buyer often expects more extensive

representations and warranties from the seller than in a secondary sale. Previously, when the market was very competitive, the terms of a trade sale would often not differ from a secondary sale. Today, after the first nine months of 2010, the terms of the deals differ significantly and it is difficult to say what should be considered as 'normal' in a Swedish trade sale.

There is an increased number of controlled actions and dual track transactions in the Swedish market, which is a clear indication of the exit environment picking up. Compared with a 'normal' trade sale, the prevailing view is that controlled auctions maximise the purchase price, minimise the contractual liabilities of the seller and shorten the sales process; however, this is not always the case and whether a controlled auction will be successful or not is highly dependent on the quality of the asset as well as the market situation.

5.3 IPOs

The number of IPOs of private equity sponsored companies has been small over the last years, and during 2008 and 2009 not a single private equity sponsored company went public (SVCA Report 2009). In 2010, several Swedish private equity firms indicated their intention to take portfolio companies public, and, during H1 2010, six private equity sponsored IPOs were announced (SVCA Report 2010).

IPOs hardly ever provide a full immediate exit for the investors, as investors typically are subject to lock-up periods following an IPO. However, compared to a secondary or trade sale, an IPO has the advantage that it enables the investors to exit without providing any warranties except for what may be agreed in the placing agreement.

As part of the IPO process, the portfolio company must prepare a prospectus and undergo a due diligence review. Compared with a secondary or trade sale, IPOs are costly and more time consuming. The management team of the portfolio company will not only be tied up during the IPO process but the listing itself will result in increased financial and other reporting requirements as well as the company becoming subject to the Swedish code on corporate governance, which applies to all companies listed on a Swedish regulated market.

5.4 Refinancings

Prior to the credit crunch in 2008, private equity firms often refinanced their portfolio companies to further increase debt in order to facilitate dividend payments and thus recover part of the invested capital. Due to the current market situation, refinancings are no longer as common.

There are no thin capitalisation rules in Sweden. However, pursuant to the Companies Act, a company is forced to enter into compulsory liquidation if its equity falls below one-half of the registered share capital and the equity is not restored to the registered share capital level within a certain period of time. This rule must be monitored when debt levels rise in portfolio companies.

Due to the financial assistance rules described in section 3.1 above, a

refinancing may not be linked to the initial acquisition of the portfolio company.

5.5 Restructuring/insolvency

Insolvency is obviously the least favourable exit for investors, but might be the last resort for an unsuccessful portfolio company. In 2009, the number of negative exits significantly increased compared to previous years, however, in 2010 the number of negative exits seems to be decreasing as only one negative exit was made during H1 2010 (SVCA 2010 Report).

As described in section 5.4 above, the Companies Act includes provisions regarding compulsory liquidation in certain situations. If the board of directors fails to fulfil its duties pursuant to the Companies Act in connection with a threatening compulsory liquidation, the board of directors will become personally liable for the company's obligations incurred subsequent to such failure.

A complex issue relating to Swedish insolvency law is to what extent agreements or other arrangements of a portfolio company can be enforced against a bankruptcy estate. Furthermore, transactions (in certain circumstances and subject to specific time limits) can be reversed after being subject to recovery claims. In situations where the other party to an agreement or other arrangement is a closely related party to the portfolio company, and provided that a claim of recovery (clawback claim) can be made, there is no time limit for bringing a claim of recovery.

6. TAX

6.1 Taxation of fund structures

As described in section 2.1 above, both Swedish limited liability companies and limited partnerships now qualify for the participation exemption regime. This means that both structures can be used for many types of private equity funds without giving rise to taxation at the fund level when divesting portfolio companies. Instead, divesting proceeds (capital gains) from portfolio companies will in general only be taxed at the investor level.

The taxation at the investor level depends on each investor's tax situation. For Swedish investors, tax is rarely an issue. For foreign investors in Swedish private equity structures, the situation will have to be analysed for each category of investors. However, Sweden does not normally tax capital gains received by foreign investors and does not levy withholding tax on interest payments. In addition, Sweden has an extensive network of double taxation treaties (more than 80) eliminating or reducing withholding tax on outbound dividend distributions.

When structuring a Swedish fund, value added tax (VAT) issues need to be carefully analysed as the use of a separate management entity may trigger an obligation to pay VAT on the management fee paid by the fund entity.

The Swedish rules on permanent establishment will always have to be analysed in non-Swedish private equity fund formations.

6.2 Carried interest

As described in section 4.5 above with respect to management individuals, there are various issues to consider when structuring contracts for the investment executives in order to avoid adverse tax effects. For obvious reasons, it is very important for the investment executives that the contracts are structured in order to qualify for capital gains taxation of all carried interest and that is the normal way of structuring such contracts in Sweden. One of the key concerns in this respect is that the investment executive must always pay 'market value' for each share or interest acquired and that the share or interest constitute a security.

It is also important that the carried interest qualify for capital gains taxation and is not taxed as employment income as the latter would give rise to an obligation for the employer to pay social security charges (currently about 32 per cent).

6.3 Management equity

The tax issues relevant to Swedish management individuals are similar to those of investment executives described in section 6.2 above. All equity investments are typically made at 'market value' and with the aim of qualifying for capital gains taxation.

6.4 Loan interest

The taxation on interest payable on loans granted by investors to the private equity fund will depend on the tax situation for each investor. For Swedish investors, interest will, in general, be taxable. For foreign investors, there is no withholding tax on outbound interest payments.

For the Swedish fund structures, there are no thin capitalisation rules and as a general rule interest payments at arm's length are deductible in full. However, certain restrictions apply for profit-sharing loans and interest payments between related parties.

6.5 Transaction taxes

In Sweden, there is no transfer tax or stamp duty payable with respect to transfers of shares in a limited liability company or a partnership. For asset deals, the purchaser will have to pay VAT on the purchase price if the assets do not represent an entire business or business area. For VAT exempt businesses (eg, businesses in the financial sector, education or healthcare) asset deals can trigger VAT on the purchase price. There is no net asset value tax (or similar tax) for private equity funds structured as Swedish limited liability companies or limited partnerships.

7. CURRENT TOPICAL ISSUES/TRENDS

7.1 The current fund raising and deal-doing environment

In 2009, Swedish private equity funds raised SEK 3.8 billion, which is 95 per cent less than the SEK 78 billion raised in 2008, and the lowest level of funds raised since 2002 (SVCA Report 2009). In 2010, fundraising remains challenging for Swedish private equity firms and during H1 2010, only

Swedish venture funds have raised capital in Sweden, in the relatively low amount of SEK 257 million (SVCA 2010 Report). However, new funds are raised by Nordic private equity firms, for investments in Sweden, for example in September 2010, the Finnish listed private equity company CapMan announced the first close on €60 million of its new fund Mezzanine V, which will invest in mid size companies in the Nordic region; and in June the Danish private equity company Polaris announced the close on DKK 2.7 billion of its new fund Polaris Equity III, which will focus on investments in mid size business in Denmark and Sweden.

As in other jurisdictions, the Swedish private equity market suffered from the financial crisis and, in 2009, showed a decline in fund raising, amount of capital invested and the number and size of transactions. In 2010, activity in the Swedish private equity market has increased, and in terms of number of investments made, the levels are approaching the levels before the financial crisis (SVCA 2010 Report).

The Swedish private equity exit environment was described as 'almost non-existent' in late 2008 and 'slow' in 2009 (the SVCA's Swedish Private Equity Review 2008 and the SVCA's report *Risikkapitalbolagens aktiviteter och finansiering i tidigare skeden – kvartal 1 & 2, 2009*). In 2010, the exit environment has started to look more positive, with almost 50 exits in total during H1 2010, out of which most were trade sales or secondary sales followed by IPOs and only a few were negative exits and write offs (SVCA 2010 Report). Recent deals include, among others:

- Private equity firm EQT's SEK 4.4 billion divestment of Aleris, a leading pan-Scandinavian healthcare service operator, to the listed Swedish investment company Investor.
- UK-based private equity firm 3i Group Plc's €850 million divestment of the Swedish healthcare group Ambea to UK-based private equity firm Triton Partners.
- The IPO and listing on NASDAQ OMX Stockholm of private equity firm Altor's portfolio company Byggmax, a Nordic low-price supplier of building materials.
- The IPO and listing on NASDAQ OMX Stockholm of the Finnish listed private equity company CapMan's portfolio company MQ, a leading Swedish brand chain.

In 2009, the total number of exits increased to 129, compared with 102 exits in 2008; however, the total number of exits still remained low compared to the 181 exits in 2007 and the 186 exits in 2006.

The number of negative exits (such as bankruptcies, write downs and divestments at nominal value) increased in 2009 to 19 compared with seven negative exits in 2008, six negative exits in 2007 and three negative exits in 2006) have decreased during H1 2010, when only one negative exit was made (according to SVCA's reports for the relevant years).

In 2010, activity in the Swedish private equity market, especially the buyout market, is increasing and given the low activity in 2009 and the large amount of capital raised by Swedish private equity funds in 2008, several funds currently have a large amount of unused committed capital to invest,

which, in combination with improved access to leverage financing, creates an improved deal-making environment. Recent deals include, among others:

- private equity firm Altor's portfolio company Carnegie Investment Bank's acquisition (and the subsequent merger) of HQ Bank and HQ Fonder from HQ, a Swedish financial group listed on NASDAQ OMX Stockholm;
- US-based private equity fund Providence Equity Partners' SEK 2 billion public offer for Sweden's largest private educational company AcadeMedia, in April 2010 being the first large private equity-sponsored, non-mandatory public offer in Sweden since 2008, followed by EQT's SEK 2.3 billion competing public offer for AcadeMedia a few days thereafter; and
- Nordic Capital's (a group of private equity funds focusing primarily on investments in the Nordic region) SEK 5.4 billion competing offer for Munters, a global leader in energy efficient air treatment solutions and restoration services listed on NASDAQ OMX Stockholm, following listed industrial company Alfa Laval's public offer for Munters.

7.2 Regulatory changes

The most topical issue which may have an impact on how private equity is carried out in Sweden is the implementation of the AIFM directive. Even if it is difficult to predict the outcome of the final proposal, it is clear that the Swedish private equity industry will be affected when the AIFM directive is implemented.