

# Acquisitions and takeovers

## EU Company Law

### Exam question

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Explain and discuss the various ways a company/business can be acquired, including advantages and disadvantages of the various ways, as well as relevant rules concerning takeovers.

### Introduction

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3<sup>rd</sup> directive

#### How are economic decisions of business enterprises coordinated?

2 extremes:

- Coordination by the market via contracts to buy or sell, lend or hire, etc.
  - Apart from reaching an agreement on terms of a contracts, this form of cooperation **requires little cooperation** between business enterprises.
- Full integration in the form of full business / asset transfer, share transfer, merger
  - complete control by one business enterprise over the activities of another business enterprise

#### Strategic co-operation

Challenges in international markets:

- Large exposure to new competitors
- Large investment requirements for development and research
- Product cycles are shortened by new innovations urging businesses to realize quicker return on investment
- Modern technology complex, expensive
- Need for building cross-border exchange of knowledge

→ for this reason (cross-boarder) cooperation may be indispensable (uundgåelig)

- (e.g. hereby cooperating enterprises can share the cost of research and development, can strengthen manufacturing, marketing and distribution position, etc)

Where cooperation has a long-term impact on the competitiveness of enterprises involved while retaining their independence and identity. → identified as strategic co-operation. E.g. Joint ventures is a specific form hereof.

### Cross-border acquisitions

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#### Process

Negotiation with one buyer only

Auction process

Confidentiality agreements

Exclusivity agreements

Seller prepares a “data room”

Buyer conducts a “due diligence”

## 2 forms of acquisitions

- Asset deals
  - Buy the assets /liabilities in company.
  - Buy out the assets of the company.
  - Full assets deal.
- Share deals
  - Buy the controlling shares of the company.

## Letter of intent

Letter of intent (“LoI”)/ Heads of agreement / Memorandum of Understanding (“MoU”)

Indhold

- Framework
- General terms
  - Subject matter
  - Price range.
  - Deadline → When the agreement must be finished
- Conditions
  - Ex due diligence.
  - Others.

Are letter of intents **binding**?

- E.g. England: An agreement is void if uncertainty of major terms are not agreed upon.
- E.g. Netherlands: LoI may have legal consequences; parties can be forced to continue negotiations or the LoI may even be qualified as a contract.
- Might even qualify as a partnership!
- Often they are non-binding.
  - Due to inserted clause.

When is the agreement closed?

- Signed agreement (betings aftale) is not necessary a closed agreement.
- When the conditions in the agreement are met, the agreement is closed. (endelig aftale)
  - Conditions can be:
    - Authorities.

## The choice of acquisition method

Acquisition methods:

- Asset deals / business transfer
- Share deals
- Mergers

What often dictates the choice of acquisition method?

- Tax
  - In certain countries share deals may be tax exempt whereas the gain stemming from asset deals in the same country will be taxable and for this reason a seller may in these countries perhaps prefer a share deal.

- The buyer may prefer an asset deal for depreciation (afskrivning) reasons if the buyer cannot depreciate the purchase price of shares according to local law.
  - Assets selling
    - The company will be taxable of the selling of assets.
    - Change of debtors demands approval.
      - Not like the merger, where we have universal succession.
  - Selling shares
    - Personally taxable med det samme
    - Holding company.
- Practicality
  - Share deals are in general easier to carry out than asset deals. Cross-border merger procedures are relatively lengthy. In share deals contracts and permits of the target company continue (exemption: change of control provisions) as no change of debtor/creditor.
- Risk takeover
  - With a share deal the buyer indirectly takes over all the risks of the past activities of the target company.
  - Generally it is more risky to take over the shares.
  - Assets can be cherry picked.
  - Clause of warrants (indemnifying)
    - Make the seller write statements on the company's responsibilities.
    - Making the seller responsible for unexpected liabilities.
      - The should by damage.
      - Installments !
      - Deposit
      - Bankgaranti

## Acquisition forms

### Assets deal:

- Advantages:
  - Flexible method
    - Does not automatically lead to acquisition of all assets and liability of the company (contrary to what is the fact in mergers and share deals).
      - **Cherry picking.**
        - Leaving the liabilities of the company.
      - I.e. the buyer is as a starting point only liable for the specific liabilities/debts it assumes.
      - Note: In Germany the buyer is liable for debts of former owner of a commercial business (unless agreement to the contrary is registered with the German Commercial Registry).
  - Tax – Depreciate(afskrivningsmulighed)
- Disadvantages:
  - Tax issues.
  - Complexity.
  - Every single asset has to be transferred in accordance with applicable rules of national law.
  - There is no universal succession of title to the purchaser. Change in debtor.
    - The transfer of all existing / ongoing contracts / permits require consent.

Directive 2001/23/EC on the safeguard of employees' rights and obligations from employment contracts are automatically transferred to the buyer through an asset deal & a sale may not in itself constitute grounds for dismissal.

#### Share deal:

- Advantages:
  - Often less complex than asset deals (and mergers).
  - (Tax)
- Disadvantages:
  - Takeover of all liabilities of the company (including e.g. environmental liabilities, product liability, etc.).
    - Potentiel as well as actual.
  - (Tax)

## Takeover directive and takeover bids

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Starting point: Shares are freely transferable (sellable)

- A takeover is the acquisition of the shares of a company in such quantity as represent at least a controlling percentage of the voting rights.

### Takeover bids

With regards to listed companies, takeover bids are regulated in order to provide for transparency, disclosure and proper procedures to enable shareholders to decide on the merits of the bid, thus safeguarding the interests of shareholders and securing the proper functioning of the capital market.

#### Source of law:

- 13<sup>th</sup> Directive 2004/25/EC (The take-over directive)
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### Information concerning bids (art. 6)

Art. 6 of the Takeover Directive:

- “Member States shall ensure that a decision to make a bid is made public without delay and that the supervisory authority is informed of the bid. They may require that the supervisory authority must be informed before such a decision is made public. As soon as the bid has been made public, the board of the offeree company and of the offeror shall inform the representatives of their respective employees or, where there are no such representatives, the employees themselves.
- Member States shall ensure that an offeror is required to draw up and make public in good time an offer document containing the information necessary to enable the holders of the offeree company's securities to reach a properly informed decision on the bid [...]”
- **The offer document shall at least contain:**
  - “the **terms** of the bid;
  - the **identity** of the offeror and, where the offeror is a company, the type, name and registered office of that company;
  - the securities or, where appropriate, the class or classes of **securities for which the bid is made**;
  - the **consideration offered for each security** or class of securities
    - in the case of a mandatory bid
      - the method employed in determining it, with particulars of the way in which that consideration is to be paid;
  - the compensation offered for the rights which might be removed as a result of the breakthrough rule laid down in Article 11(4)

- with particulars of the way in which that compensation is to be paid and the method employed in determining it;
- the maximum and minimum percentages or quantities of securities which the offeror undertakes to acquire;
- [...]
- **the offeror's intentions** with regard to **the future business** of the offeree company
  - in so far as it is affected by the bid
    - the offeror company and with regard to the **safeguarding** of the jobs of their **employees** and management
      - including any material change in the **conditions of employment**
      - and in particular the offeror's strategic plans for the two companies and **the likely repercussions on employment**
      - and the locations of the companies' places of business;
- the **time** allowed for acceptance of the bid
- [...]
- the national law which will govern contracts concluded between the offeror and the holders of the offeree company's securities as a result of the bid and the competent courts."

## Mandatory bids

Art. 5

- Any person who acquires a specific percentage of the voting rights
  - → must make a bid with a view to acquire **all** the shares, at an equitable price.
    - The highest price for "same securities" over a period of 6-12 months.

## Time allowed for acceptance of bid (art. 7)

Art. 7:

- "Member States shall provide that the time allowed for the acceptance of a bid may
  - **not be less than 2 weeks**
  - **nor more than 10 weeks** from the date of publication of the offer document."

## Board neutrality rule (art. 9)

Opt-in for the MS

- MS can opt to use this rule or not.
- So can the company.
- Art. 12(2)

Why have this rule?

- Angst for at miste deres position i bestyrelsen / som direktør.
  - Incentive to obstruct (ruin) the bid.

Art. 9(2):

- From the moment the decision to make a bid is received by the board (or made public),
  - **the board** of the offeree company **must obtain authority** from the general meeting **before taking any action** that may result in the frustration of the takeover bid
    - with the exception of seeking alternative bids.

- The board may (of course) still be allowed to be against the takeover and e.g. try to make other third parties give another competing bid – but it may not itself bar a takeover.
- E.g. the board must obtain authority from the general meeting before issuing shares to raise the costs of the takeover bid.
  - They should anyway according to the capital directive.

#### “Opt in” mechanism – art. 12

- MS need not to apply the board neutrality rule in Art. 9(2) and (3)
  - on the condition that they grant companies the option of applying the board neutrality rule.
- The decision shall be taken with the rules applicable to amendment of statutes.

#### Publication of the *boards opinion of the bid*: art. 9(5)

- “The board of the offeree company shall draw up and make public a document
  - setting out its opinion of the bid and the reasons on which it is based,
    - including its views on the effects of implementation of the bid on all the company’s interests and specifically employment, and the offeror’s strategic plans for the offeree company and their **likely repercussions on employment** and the locations of the company’s place of business [...]
    - The board of the offeree company shall at the same time communicate that opinion to the representatives of its employees or, where there are no such employees, to the employees themselves. [...]
- Opinions from the employees must be appended to the document.

## Takeover defenses

The Takeover Directive contains rules on takeover defense measures.

#### Pre-bid defense

- Clause in shareholder agreements (bob bob better in articles of associations) - to prevent thirdparty takeover
  - Preemptive rights – right of first refusal.
  - Approval – from board, general meeting etc.
  - Lock up period – Ban against selling for a period.
  - Ownership ceilings (grænse for hvor meget man kan eje).
  - Voting ceilings
    - Way to minimize the transferable power of the company.
  - Share classes. (A and B shares)
    - Way to control the power.

#### Post-bid defense – (board-neutrality?)

- Share capital increase after bid come in.

## Information about takeover defenses (art. 10)

Full transparency of all provisions which may impede the takeover of a *listed* company through a public bid.

- whether in the statutes or in contracts

Art. 10:

- Listed companies shall publish detailed information on takeover defenses such as:
  - Share classes (and the rights and obligations attached hereto)
  - Restrictions of the transfer of shares (requirement of transfer approval from the company, ownership ceilings)

- Restriction on voting rights (voting ceilings)
- Golden parachute agreements with the board or employees in the case of a takeover bid (e.g. severance pay, extended termination period)
  - Special protection on named persons.

Publication where?

- Annual report, cf. Art 10(2)
- Explanatory report to the shareholders at the annual general meeting, cf. Art 10(3)

Which kind of companies often operate with voting right ceilings?

Which kind of companies often operate with ownership ceilings?

Which kind of companies often operate with share classes?

## The breakthrough rule (art. 11)

Pre-bid defenses may be set aside on a temporary basis.

- Sammenhæng med tilbudets løbetid.
- Most companies

Pre-bid defenses may be set aside (on a temporary basis) according to Art. 11 of the Takeover Directive.

- **Restrictions on the transfer of shares** (securities)
  - Shall not apply vis-à-vis the offeror during the period in which the bid can be accepted.
  - all restrictions on transferability
    - provided for in the shareholder agreements entered into after the adoption of the Takeover Directive or in the statutes of the offeree company
- **Restrictions on voting rights**
  - At the general meeting which decides on post-bid defense measures (in accordance with Art. 9 (the board neutrality rule))
    - all restrictions on voting rights
      - - provided for in the shareholder agreements entered into after the adoption of the Takeover Directive or in the statutes of the offeree company
    - → shall have no effect.
    - And multiple-vote shares shall carry only one vote each on this general meeting.
- **If the offeror holds 75% (or more) of the voting share capital**
  - all restrictions on *transferability* shall have no effect,
  - all restrictions on *voting rights* shall have no effect and
  - all extraordinary rights of shareholders regarding *appointment / removal of board members*
    - shall have no effect;
  - *multiple-vote shares* shall carry only one vote each
    - at the first general meeting following closure of the bid called by the offeror in order to amend the statutes or remove / appoint board members.
  - To this end the offeror shall have the right to convene a general meeting at short notice.
- Compensation
  - If any **shareholder suffers losses** by having its legal rights reduced due to the breakthrough rule, **equitable compensation** shall be provided, cf. Art. 11(5).

**“Opt in” mechanism**

- Art. 12(2) allows Member States not to apply the breakthrough rule in art. 11
  - On the condition that they grant companies the option of applying the breakthrough rule.
- The decision shall be taken with the rules applicable to amendment of statutes.

### **Reciprocity principle (Art. 12(3))**

- with regards to the board neutrality rule and the breakthrough rule

Art. 12(3) of the takeover directive:

- Member States may exempt companies which have adopted the board neutrality rule (Art. 9) and/or the breakthrough rule (Art. 11) from applying these rules, if they become subject of an takeover offer by a company which does not itself comply with the neutrality rule (Art. 9) and/or the breakthrough rule (Art. 11).

### **Status**

Most Member States have imposed the board neutrality rule.

Most Member States have not imposed the breakthrough rule. Exception: Baltic States.