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The New German Acquisition of Securities and Takeover Act

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The attempt by the European Union to establish a Europe-wide framework for company takeovers failed in 2001 when the European Parliament rejected Directive 13. This failure was partly due to the inability of finding solutions to numerous national legal barriers – such as the "golden share".

Shortly after the European Parliament vote – on July 11, 2001 – the German government presented a draft takeover law which dealt with public offers for the acquisition of securities and company takeovers (Act on the Acquisition of Securities and Takeovers – *Wertpapiererwerbs- und Übernahmegesetz - WpÜG*). This draft was, *inter alia*, based on the experience with the takeover of Mannesmann AG by Vodafone/Airtouch Plc. After its passage into law the WpÜG came into force on January 1, 2002.

The WpÜG covers all public bids for the acquisition of securities issued by a stock corporation (*Aktiengesellschaft, AG*) or a partnership limited by shares (*Kommanditgesellschaft auf Aktien, KGaA*) domiciled in Germany, the shares of which are accepted for trading on an organised stock exchange in Germany or another European Union member state. The law sets forth detailed guidelines on voluntary public and mandatory takeover bids. This includes the takeover bid procedure, the duties of the offeror and the target company, as well as the consideration. The new law replaces the voluntary Takeover Codex of the Exchange Expert Commission (*Börsensachverständigen-kommission*) at the Federal Ministry of Finance.

The WpÜG is intended to provide a regulated procedure for a takeover of a company, as well as to allow possible defence procedures to run on legally secure ground. Overall, the new law is to promote the international competitiveness of the German securities market.

I. Public Bid

The law defines three types of bids: voluntary bid, takeover bid and mandatory bid.

A *voluntary bid* (*freiwilliges Angebot*) is a public bid to purchase shares in a target company, provided the bid is not directed to acquire control of the target company. Pursuant to the WpÜG, control exists where 30 percent of the voting rights in the target company are held.

An offeror intending to obtain direct or indirect control over a target company is obligated to publish a *takeover bid* (*Übernahmeangebot*) to (all other external) shareholders for their shares (Sections 29 *et seq.* WpÜG).

Where a shareholder, who already owns or controls 30 percent of the voting rights, intends to increase his stake, he has to submit a *mandatory bid* (*Pflichtangebot*) to the other shareholders (Section 35 WpÜG). This section is aimed at providing shareholders in a company the opportunity of leaving the company in return for compensation in the event that the ownership changes hands (protection of minority shareholders).

With regard to the takeover and mandatory bid the WpÜG does not differentiate between direct or indirect control. The application of the WpÜG can thus not be circumvented by using an intermediary holding company as acquisition instrument.

A takeover offer bid is distinguished from the mandatory bid as follows: the former applies where the offeror holds less than 30 percent of voting rights at the time of the bid; in the event the stake of the offeror is at least 30 percent at the time of the bid, the rules regarding the mandatory bid will apply. The takeover bid, which overall is less regulated, does not turn into a mandatory bid even if the 30 percent threshold is exceeded during the course of the bid. In this case the rules of the takeover bid are still applicable. The following differences between the takeover bid and the mandatory bid can, *inter alia*, be identified:

- the mandatory bid cannot be made subject to conditions;
- only mandatory bids must be published;
- voting rights are not considered when this is applied to the relevant authority; and
- release from the obligation of making a mandatory bid is possible.

However, the rules on the consideration to be offered are identical for both kinds of bid (Section 31 WpÜG in connection with Sections 3 *et seq.* of the WpÜG Offer Regulation) and cover cash and share offers. Offers must provide *reasonable consideration*, not below the following criteria:

- the average weighted share trading price of the target company during the last three months; and
- price for the acquisition of shares by the offeror during the last three months prior to publication of the offer.

Although these are only principles, there are no provisions prescribing the competence of the relevant authority (Federal Supervisory Office on Financial Services (*Bundesanstalt für Finanzdienstleistungsaufsicht – BAFin*) to release an offeror from

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the consideration requirements. The WpÜG deviates – with respect to the reasonable consideration – from Rule 9.5 of the City Code and Rules Governing Substantial Acquisitions of Shares which covers a dispensation from the highest price to be provided. This inflexible concept is a critical point, which might hinder some takeovers. However, in the case of a mandatory bid, Section 37 of the WpÜG provides for the possibility of releasing an offeror from the obligation of making a bid in cases of narrowly defined exceptions.

In accordance with Section 31 paragraphs 4 and 5 of the WpÜG, acquisitions by the offeror during or one year after the bidding phase lead to automatic increases in the value of the bid (so-called duty of improvement, "improvement period"); *i.e.*, the offeror is obliged to settle the different amount paid by the offeror during a former bid and the acquisition price during the improvement period.

II. Bid Procedure

Pursuant to Section 10 paragraph 1 of the WpÜG, an offeror must immediately publish his decision to make a takeover bid. With multiple-stage decision processes, this obligation is triggered by the resolution of the "last" body of the company. The offeror must inform the BAFin and the executive boards of all stock exchanges where the securities of the offeror and the target company are accepted for trading. Furthermore, the bid is to be published in at least one supra-regional official stock exchange gazette (*Börsenpflichtblatt*) or via an electronically-operated information system (*e.g.*, Internet). After publication, the offeror must inform the executive of the target company with respect to the intent to make a takeover bid.

Within four weeks after publication of the bid, the offeror must file the bid documents with the BAFin. This deadline may be extended by a further four week period, if, *inter alia,* a cross-border bid is involved. If the bid documents are not delivered within this deadline, the bid will not be admitted (Section 15 paragraph 1 of the WpÜG) and will be blocked for the period of one year.

These bid documents must be published immediately, if the BAFin authorises publication, or, if following receipt within 10 banking days if no prohibition has been issued. The review by the BAFin only addresses formal completeness of the documents and obvious infringements. Following publication of the bid, the offeror generally has no right to withdraw his takeover bid, unless he has made a reservation in the publication (Section 10 of the WpÜG).

III. Bid Documentation

After notification of the bid the offeror must compile and publish the bid documents. These must contain all the necessary information to decide on the bid (Section 10 paragraph 1 of the WpÜG). The documentation must, *inter alia,* contain:

- business name, domicile and the legal form of the offeror;
- name, domicile and legal form of the target company;
- securities which are subject of the bid;
- type and amount of the consideration offered for the securities of the target company;
- conditions precedent (if any) of the bid;
- start and end date of the acceptance period.

In addition, the following information must be provided in the documentation:

- the securing of financing of the compensation,
- the expected effects of a successful bid on the assets of the target company,
- the financial and profitability situation of the offeror,
- the intentions of the offeror with regard to employees and members of the management, as well as
- information about the consideration granted or offered to the board of management of the target company.

In the case of cash bids, the financial certificate concerning the availability of the required funds for the acquisition of the securities by an independent securities services company (*Wertpapier-dienstleistungsunternehmen*) must be included in the bid documents. This information is complemented by a further extensive catalogue of supplementary information according to an offer regulation. Parallel with the offer documents, the parties involved can publicly advertise. In order to counter grievances or abuse in such advertising, the authority can prohibit certain types of advertising.

The offeror and all individuals or entities who have assumed responsibility for the issue of the bid documents are liable for the accuracy and completeness of their content, including the liability of the securities service company, which must provide the finance certificate as part of the bid documents.

The acceptance period commences upon publication of the bid documentation (Section 16 of the WpÜG); in general this period cannot be extended after publication. During the acceptance period, the public must be informed by the offeror on a week-by-week basis, and in the last week of the acceptance period on a daily basis, about the number of acquired shares.

The offeror must offer valuable consideration to the shareholders of the target company, which may not generally be less than the average stock exchange price for the period. The consideration can be of a cash or non-cash (liquid shares) nature. The latter, however, may not be used if the offeror had, in return for cash, acquired either in total at least five percent of the shares in the target company during the last three months prior to the publication of the bid documentation or if the offeror has acquired in total one percent of the shares in the target company after the publication and prior to the expiry of the acceptance deadline. The offeror must not necessarily offer his own shares but may also offer the shares of other companies listed on a stock exchange.

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Further, the offeror has the obligation to improve the bid. In the event of a further acquisition of shares in the target company within a year after the publication of the bid documentation outside of the stock market, the offeror is obligated to pay the difference between the subsequent payment and the amount of the consideration of the basis of the bid (Section 31 paragraph 5 of the WpÜG). This does not apply, however, if the subsequent payment is a result of settlement or compensatory claims under the Stock Corporation Act (*Aktiengesetz, AktG*) or the Act on Reorganisation (*Umwandlungsgesetz*).

IV. Defence Tactics

In the event of a so-called hostile takeover, the takeover law provides several possibilities for the executive board of a target company to defend company takeovers. In establishing such defences for the executive board, the German law deviates from the key point of the E.U. Takeover Directive, namely the duty of the board of management to remain neutral. Although the stockholder as addressee of the takeover bid must decide in the general shareholders meeting whether he wants to take defensive measures, the board of management is not barred from implementing counter measures when a proper and diligent executive of a company which is not subject to a takeover bid would also have implemented them. This is in principle meant to guarantee that the company can continue its daily business regardless of the takeover bid. This allows wide-reaching measures, the limits of which are, as a rule, seen only upon the circumvention of the takeover. The executive board of the target company may additionally undertake such measures as have been approved by the supervisory board. This means that defensive steps can be taken without calling for an extraordinary general meeting. However, it must be noted here that measures which are not in the interests of the company considerably increase the risk of personal liability of the board of management and supervisory board.

The general meeting furthermore has the possibility of adopting resolutions (*Vorratsbeschlüsse*) which can apply for a maximum of 18 months and which must list each measure in detail. These can thus include defensive measures such as the acquisition of own shares, the so-called "Crown Jewel Options", "Golden Parachutes", "Pacman" or the search for a "White Knight". In order to minimise the liability risk of the executive board when deciding to take defensive steps, it may be advisable to call an ad-hoc general meeting. The WpÜG contains simplified provisions with regard to the notice period and further modalities in this case. If a general meeting is called, the acceptance period for the offer is extended to ten weeks. The executive board of the target company must inform the BAFin and the offeror that a general meeting has been called. The offeror must then publish this in a supra-regional official stock exchange gazette (Section 16 paragraph 3 of the WpÜG).

The offeror and any other persons acting in concert are prohibited from granting or promising inappropriate monetary benefits or other inappropriate monetary advantages in connection with the offer to members of the board of management or supervisory board.

V. Legal Protection

As an obvious advantage for potential bidders, the new law offers no legal instruments for companies and shareholders to stop or delay the bidding process, *provided that* all technical steps have been prepared properly (which was the key agreement of the recent ruling of the District Court of Berlin in the *Condat* case which stopped a takeover bid because of insufficient information provided by the bidder Texas Instruments). In detail, the following legal actions are available:

In Sections 48 *et seq.*, the WpÜG provides legal remedies against action taken by the authority. Under Section 48 of the WpÜG, an applicant can file a complaint with the Court of Appeal (*Oberlandesgericht*) of Frankfurt against any activity or inactivity of the authorities. Both the offeror and the target company can be affected by this. For example, in the case of an order of prohibition of a bid in accordance with Section 15 of the WpÜG, the offeror can file an application for approval of the takeover bid. On the other side, in the case of a formally or materially deficient takeover offer, the target company has the right to force the authority through a compulsory claim (*Verpflichtungsbeschwerde*) or a preliminary injunction (*einstweilige Verfügung*) to issue an order against the offeror or to prohibit the relevant bid document.

Section 12 paragraph 1 of the WpÜG furthermore provides a right to claim damages. The offeror and any person acting with him must compensate for damages suffered by a shareholder from accepting the bid.

Besides the WpÜG, both the offeror (or its shareholders) and the shareholder of the target company may have legal recourse under civil and corporate law. The boards of management of the companies involved must apply their offensive and defensive tactics in accordance with the interests of their company if they do not want to risk being held personally liable (Sections 93, 147 AktG).

Finally, the shareholder may take action against countermeasures of the executive board through an action for a cease and desist order or, where the measure is based on a resolution of the general meeting, through an action to have the resolution set aside (*Anfechtungsklage*).

VI. Final Remarks

The new Act on the Acquisition of Securities Acquisition and Takeovers will have a significant impact on friendly and hostile takeovers in Germany. During the first quarter of this year, 22 public bids have been notified to the BAFin. Several of these bids have attracted considerable public attention (*e.g.*, takeover bid by

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Barilla Group with regard to Kamps AG). We expect an increased number of takeovers within the next months. This tendency will be, *inter alia*, supported by the recent golden-share ruling of the European Court of Justice.

For the first time, the new German Act on the Acquisition of Securities and Takeovers provides a binding legal framework for takeovers of stock listed companies in Germany. Although it has been announced by the government as an instrument to defend takeovers of German companies, the new code in fact meets international standards and is a significant step towards an conformity of the German to Anglo-Saxon style capital market legislation. Because this has been identified as an issue in several transactions, we hope that an amended WpÜG will provide a high degree of flexibility with regard to the compensation soon.

Because minority shareholders are not in a position to stop or delay the bidding process *provided that* all technical requirements have been fulfilled, each bid can be finalised within a defined time frame. In contrast to that, the relatively inflexible consideration model, without the possibility to apply for a waiver, might hinder several takeovers. Therefore, the new code will have a lasting influence on the conduct and strategy of both financial and strategic investors in Germany.

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