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Ready for Takeover 2.0?

German issuers' readiness for public takeovers –
A renewed assessment

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Editor: Deutsches Aktieninstitut e.V.
Senckenberganlage 28
D-60325 Frankfurt am Main
www.dai.de

In co-operation with: White & Case LLP
Bockenheimer Landstraße 20
D-60323 Frankfurt am Main
www.whitecase.com

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Foreword

The M&A market is facing multiple challenges that resulted in a notable decline in public takeover activities last year. In particular, the Russian war against Ukraine, the energy crisis, the turnaround in interest rates, supply chain issues, and the changing geopolitical environment are noteworthy.

A good time to take a closer look at the current public takeover market by focusing on the following lead questions: How do German listed companies assess the current environment and its dynamic development, whether from a potential bidder's or from a potential target's perspective? How are bidders and target companies prepared for the scenario of a public takeover? When making their preparations, what is considered important and what is considered less important?

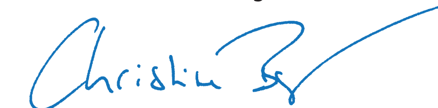
The present study summarizes the results of a survey among German listed companies that form part of the German lead indices DAX40, MDAX, and SDAX. As the current study is a new edition of the previous study published by Deutsches Aktieninstitut and White & Case in 2018, we have not just analyzed the current situation but compared key drivers as well as changes in the period from 2018 to 2023: What has changed in the last five years? Which trends can be observed?

Two main conclusions can be drawn from the current survey. First, in the view of the survey participants, although the current environment is difficult for potential bidders, the market for takeovers continues to provide various opportunities. Opportunities for bidders include using takeovers as a tool to help overcome the challenges stemming from the energy crisis and the march of digitalization. Second, the trend towards further professionalization among market participants continues unabated. Preparatory measures that were considered "nice to have" five years ago have now become standard.

The new study aims to support potential bidders and target companies and help them make their own assessments. The findings of the study are examined in greater depth in an editorial section where legal experts and practitioners share their insights on various aspects identified in the survey.

We hope you find it interesting reading!

Dr Christine Bortenlänger



Managing Director
Deutsches Aktieninstitut e.V.

Dr Alexander Kiefner

Partner
White & Case LLP

Part 1

German issuers' readiness for public takeovers as bidders or potential target companies – a renewed assessment five years after the takeover study 2018

Dr Norbert Kuhn
Dr Claudia Royé
Deutsches Aktieninstitut e.V.

Dr Alexander Kiefner
Sabine Kueper
White & Case LLP

1 Background and key findings

The German takeover market is declining and has shown clear signs of having been affected by the current economic and geopolitical environment. The number of takeovers and the total offer volume have both fallen significantly. While there were as many as 33 takeovers with a total volume of EUR 67.1 billion in 2021, there were only 18 with a total volume of EUR 5.3 billion in the first 11 months of 2022. Even KKR and Vodafone's acquisition of Vantage Towers, a radio tower infrastructure company, in December 2022 only increased the total volume for 2022 to EUR 21.4 billion – just under a third of the previous year's volume. Moreover, nine of the transactions (some combined with takeover/mandatory offers), representing half of the takeover volume, were delisting acquisition offers. This shows another weakness in the M&A market last year: delisting acquisition offers involve compensation payments to shareholders when their companies are delisted and are not "real" takeover offers.

These figures provide reason enough to look for the causes of the decline, and they raise the following questions: How is takeover activity being affected by Russia's war against Ukraine, the lingering global effects of the COVID-19 pandemic and the central banks' decisions to raise base rates (thereby signalling the end of the era of low interest rates)? How are M&A strategies changing in response to the crises that are currently troubling us? And how do companies assess the risk that they themselves might become the target of a takeover and are they ready?

In this report, we answer these and other important questions based on a survey of listed companies included in the DAX40, MDAX or SDAX indices. 32 listed companies took part in our survey. Just under half of the participants were listed in the DAX40 index, with listings in the MDAX or SDAX indices each making up about a quarter. This report is a follow-up to our 2018 report, "Ready for Takeover?"[1]. This has allowed us to compare the current situation with the findings of our last survey wherever the questions remained the same as those asked five years ago.

Our presentation of the survey's findings begins by considering the perspective of bidders in the takeover market before moving on to look at the perspective of the target companies. The last section presents the participants' assessments of the role of advisors in the takeover process. This empirical part is followed by articles by expert legal practitioners from the law firm White & Case, who discuss and analyse the details of the survey's findings.

[1] See Deutsches Aktieninstitut/White & Case: *Ready for Takeover? Marktübliche Prozesse und Vorbereitungsstand deutscher Unternehmen als potenzielle Bieter und Zielgesellschaften* [Standard processes and state of readiness of German companies as potential bidders or target companies], Frankfurt am Main 2018.

The key findings of the survey can be summarized as follows:

- **The takeover market is fairly calm:** Only half of the participants feel that the central banks' turnaround in interest rates, which is leading to a significant deterioration in financing conditions, has affected their takeover activity. Just under 40 percent are going to reduce their takeover activity because of the energy crisis, and 30 percent will do so because of the sanctions regime associated with the Russian war of aggression against Ukraine. This suggests, conversely, that many of the participants are fairly relaxed about takeovers in the current macroeconomic and geopolitical environment. They continue to see takeovers as a strategic response to megatrends. More than half the participants want to use takeovers to achieve digitalisation, and more than a third to deal with the energy revolution.

- **The trend is to stay private:** Almost three quarters of the participants prefer private M&A transactions and are therefore not looking for public takeovers. Five years ago, the picture looked a lot different. At that time, not even a third of the participants included private transactions in their acquisition strategies. This shows that in these times of volatile stock market prices off-market transactions are gaining traction. The observable trend towards delisting confirms this tendency to prefer companies to go from public to private (see *A snapshot of the German takeover market in 2022*, page 34).

- **ESG is on the rise:** Financial criteria such as EBIT margin or minimum return on investment continue to dominate the selection of potential takeover candidates. However, in addition to these economic requirements pre-defined ESG criteria are now playing an increasingly important role as well.

- **Cash is king and equity is queen:** 40 percent of the participants prefer a pure cash offer as consideration for the target company's shareholders. Conversely, it follows that 60 percent of the participants would like to finance their transactions with at least a combination of cash and shares. In practice, however, share for share exchanges currently play no role at all in Germany, due to the country's strict legal requirement for the shares to be liquid. This shows that German case law is frustrating the desire which many companies have, namely to use their shares as currency for their acquisitions (see *Are exchange offers experiencing a renaissance?*, page 52).

- **Minimum acceptance thresholds as obstacles to takeovers:** Recent M&A transactions have shown that index funds and the tactical behaviour of hedge funds can prevent bidders from exceeding minimum acceptance thresholds. The result has been that bidders have either had to waive the minimum acceptance thresholds before the end of the acceptance periods or else reduce them drastically. Many takeovers have therefore needed several attempts before reaching a successful conclusion. More than 40 percent of the participants are therefore in favour of a change in the law regarding minimum acceptance thresholds (see *Some suggestions from the advisory practice for amending the WpÜG*, page 100).

- **Activist shareholders are being taken seriously:** 80 percent of the participants make sure they are prepared to deal with activist shareholders in the context of the takeover process. This is a significant improvement compared to our survey of five years ago. The DAX40 participants are ready. More than two thirds of the SDAX participants are ready, too. This represents significant progress for these smaller companies, which usually have significantly fewer resources than the large DAX40 companies. Five years ago, only a third of the SDAX participants were ready (see *Communication with, and potential responses to, activist investors*, page 42).

- **The risk of a takeover is underestimated:** Only a few of the participants believe that they are likely to be taken over in the next three years. However, potential bidders have already approached a large proportion of the participants – especially those listed in the MDAX or SDAX indices. This shows the same discrepancy between aspiration and reality that we identified five years ago. However, a comparison with 2018 also shows that, when it comes to analysing the likelihood of being taken over, not only do the participants see the standard measures as significantly more important than they did five years ago, they are also using them. Having said that, there is room for improvement as regards the precautionary measures that would need to be taken very quickly in the event of a bidder making an unexpected approach.

2 The bidder's perspective

2.1. Turmoil in the takeover market?

We asked the participants whether the current capital market trends or geopolitical developments have affected their takeover activity – and found the result astonishing. Many of them do not feel that the ongoing geopolitical upheavals have significantly constrained takeovers.

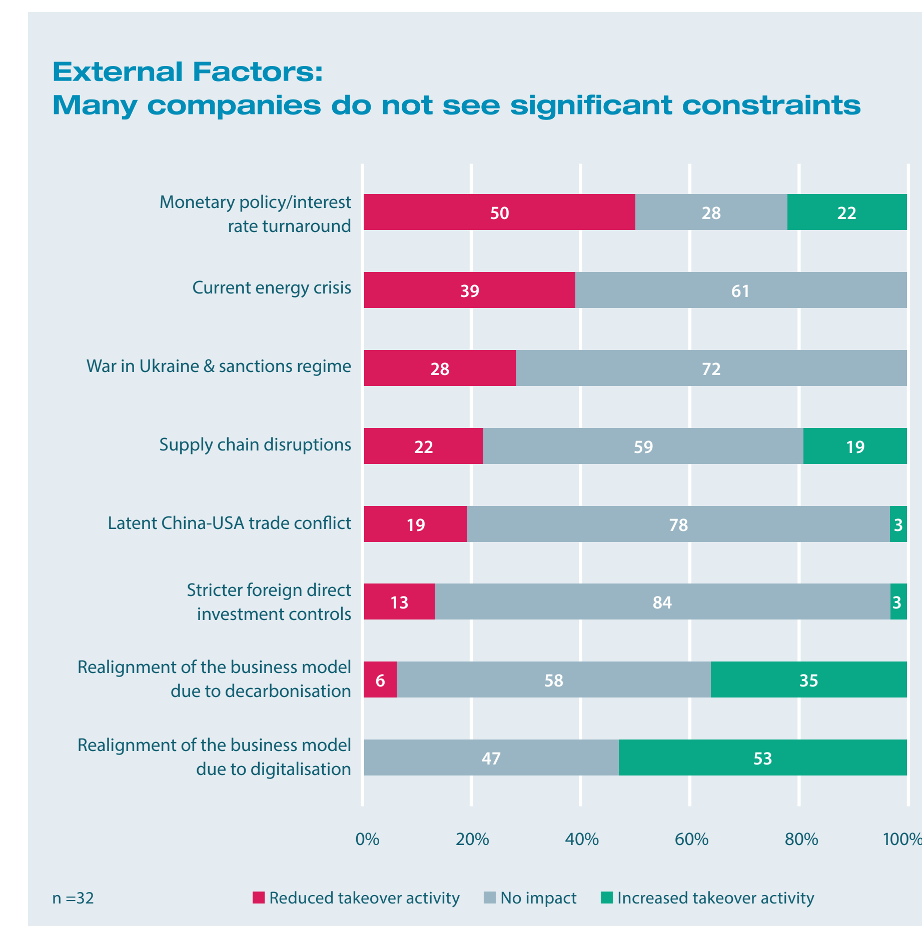


Figure 1: Impact of current market and geopolitical developments

The 2018 survey found that the low interest rate environment was a key driver in the takeover market. Today, half the participants see the interest rate turnaround in the major central banks' monetary policies as a brake on their takeover activity (see Figure 1). The response from the other half is, however, surprising. Almost a third of the participants do not expect the worsening credit conditions to affect their takeover activity. This suggests that some participants still have large available cash reserves. Five years ago, the participants still saw cash reserves as a key driver of takeovers. This suggests that they are less dependent on debt financing than they were, and that many of them see higher interest rates as bearable. However, the SDAX participants in particular see higher interest rates as a constraint on their takeover activity – probably because they have smaller cash reserves.

We note that more than a fifth of the participants expect their takeover activity to increase as a result of the central banks' U-turn on interest rates. They evidently expect that rising interest rates will unsettle equity investors, and that this may lead to selling pressure and falling share prices. They also appear to see lower entry prices on the stock markets as a good opportunity to increase their own investment portfolios.

One important driver for takeover activity is the digital transformation, which is forcing companies to realign their business models. More than half the participants think that they can gain know-how in the IT sector by acquiring one or more companies. Three quarters of the MDAX participants give digitalisation as a reason for boosting their activity in the takeover market.

Decarbonisation and the energy revolution are also generating takeover activity according to more than a third of all participants and half of the DAX40 participants. The drivers in this case are likely to be similar to those in the case of digitalisation. Many participants see targeted investments as the best way to gain the know-how they need to adapt more rapidly to the energy revolution.

So far at least, the latent trade conflict between China and the USA has had almost no impact on takeover activity for 80 percent of the participants. Nor have the current energy crisis or Russia's war of aggression against Ukraine (a war which has resulted in an extremely restrictive sanctions regime against Russia) impaired the takeover market for the vast majority of the participants. We can only speculate about the reasons.

The results were similar when we asked about the impact of the supply chain disruptions that severely affected global trade at the height of the COVID-19 crisis. Although supply chains have improved somewhat – especially since China ended its zero-COVID strategy - they are still not functioning smoothly. Yet only slightly more than a fifth of the participants say that they are reducing their takeover activity as a result. Conversely, one in five expect that the supply chain disruptions will result in increased takeover activity. It appears that experiences over recent years are leading companies to increasingly questioning their dependence on supplies from certain regions. This trend is associated with an increase in M&A activity with respect to targets in regions where supply chains are expected to remain more stable.

2.2. What is the impact of stricter investment controls

Complying with investment control regimes requires companies to expend additional time and resources when engaging in cross-border takeovers. Other rules, such as banking supervision law, rarely affect M&A transactions (see *FDI screenings as showstopper?*, page 58).

Many countries have tightened up their investment control regimes significantly in recent years as they are afraid that takeovers could allow domestic know-how to flow abroad. They are also keen to decrease their dependence on foreign capital.

Despite this tightening-up, most of the participants in our survey consider that as far as takeovers are concerned the investment controls in the key jurisdictions are either completely irrelevant or else not (particularly) obstructive (see Figure 2). The new EU Regulation 2022/2560 on foreign subsidies distorting the internal market (the Foreign Subsidies Regulation) is another important hurdle, but its impact could not be considered in the survey as it only came into force at the beginning of 2023.

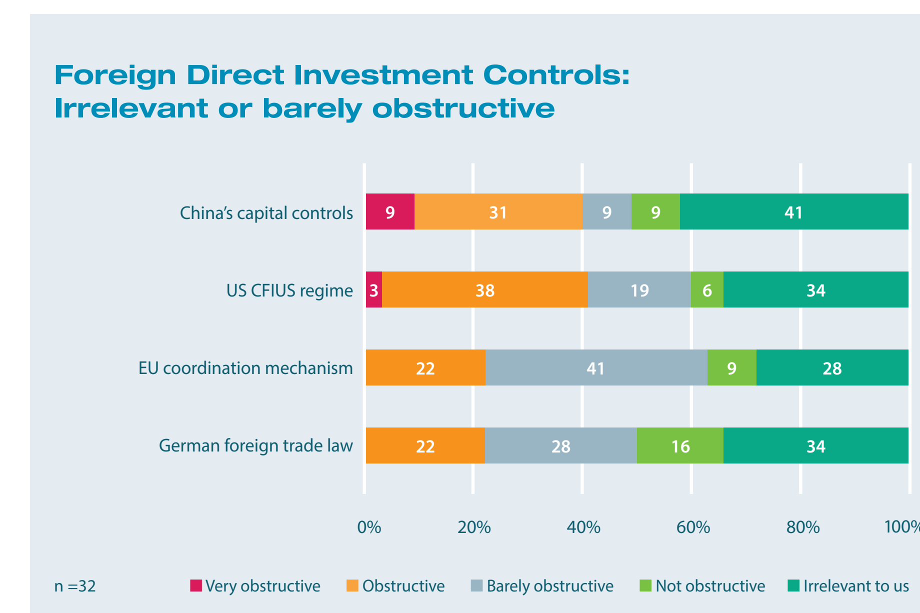


Figure 2: Assessment of investment control regimes

However, this should not obscure the fact that around 40 percent of the participants consider China's capital controls and the Committee on Foreign Investment in the United States (CFIUS) regulations to be obstructive or very obstructive. As the Chinese rules are concerned, this finding is in line with the assessment by the participants in 2018. However, the US rules are rated much more critically than they were five years ago. One reason may be the fact that almost two thirds of the participants are looking for potential takeover targets in the USA and are therefore having to grapple with the US investment controls. This is exacerbated by the fact that, under certain conditions, the CFIUS regime requires a review process even for non-US target companies – for example if the target company holds any real estate in the USA.

2.3. What takeover strategies do companies have?

Companies seeking to expand their business models can achieve this goal through purely organic growth – i.e. without taking other companies over. However, only just over a quarter of the participants have adopted this strategy (see Figure 3).

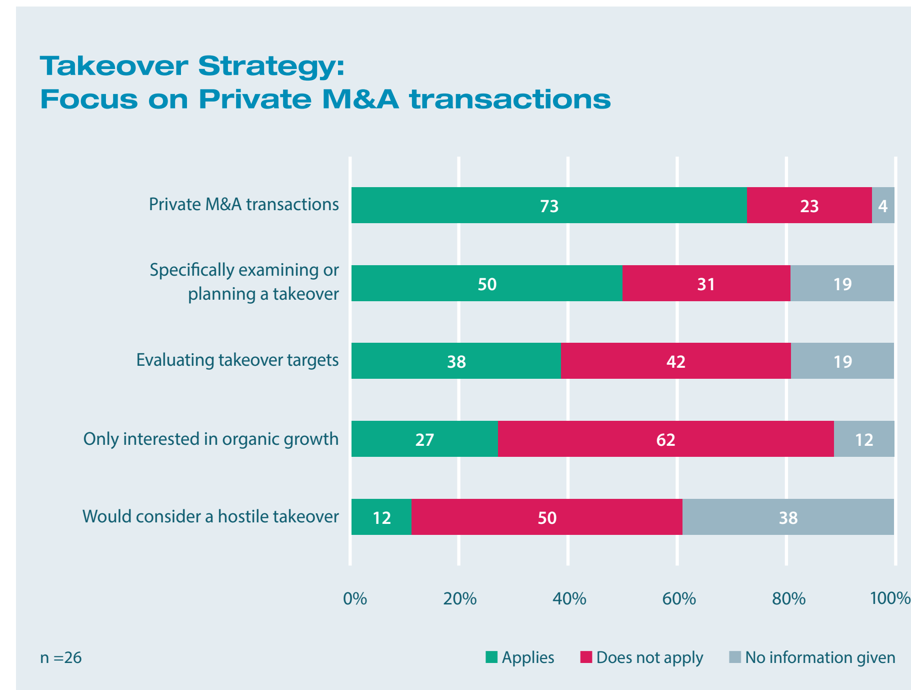


Figure 3: Takeover planning and strategy

The vast majority of the participants want to grow through takeovers and have a strategy to do so. More than two thirds of the participants in our current survey are focussed on private M&A transactions. The picture was different in 2018. At that time, the takeover strategies of fewer than a third of the participants had private transactions, i.e. acquiring unlisted companies, at their forefront. The market for public takeovers sometimes involves great uncertainty (e.g. because stock market prices are more volatile), and a private transaction is therefore a safer option at the moment. The process involved is also significantly less costly in terms of both time and resources and the universe of potential private takeover candidates is much larger – especially in Germany –.

Almost two fifths of the participants regularly evaluate the M&A market regarding public takeovers. In the last five years, half of the participants have followed up on a general search of this kind by examining the specific possibilities of taking over a listed company or are planning to do so in the near future. Both responses are roughly in line with the responses given in 2018.

More than a tenth of the participants would consider a hostile takeover. Five years ago, it was no less than a fifth. This decline is probably mainly due to the currently uncertain market conditions deterring companies from taking the risks involved in hostile takeovers.

The fact that participants from different indices reach different assessments shows that a company's size is key to determining its strategic orientation on the takeover market. Almost four fifths of the DAX40 participants have specific takeover plans, while just over a tenth of the SDAX participants have them. Conversely, almost half of the SDAX participants say that they want to grow organically, while the figure for the DAX40 participants is just a tenth.

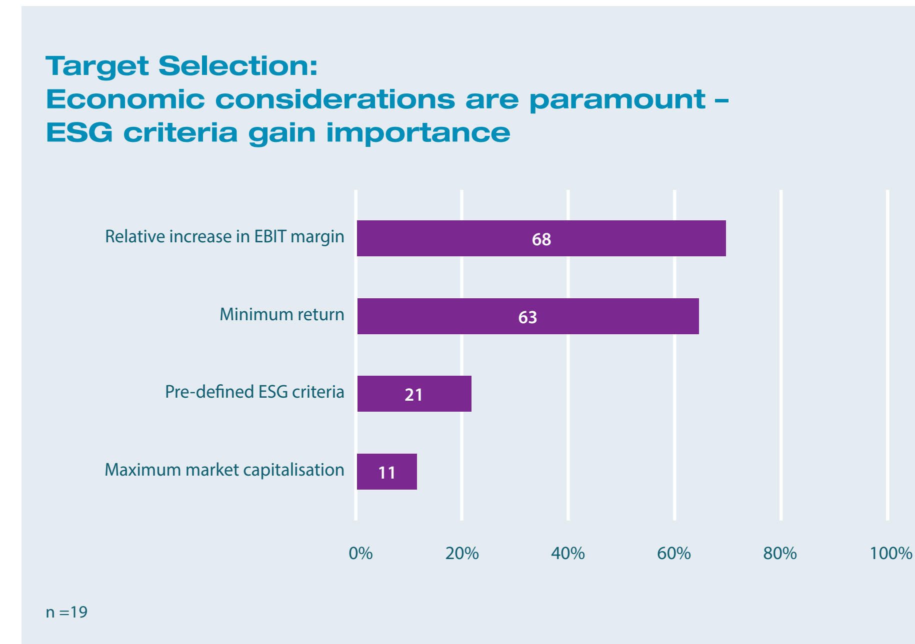


Figure 4: Selection criteria for takeovers

Evaluating is one thing but finding an attractive takeover candidate is quite another. What are the key criteria in the selection process? The participants say that economic considerations are paramount (see Figure 4). More than two thirds say that target companies must have achieved a relative increase in their EBIT margin and a minimum return on investment. Sustainability is another topic which is gaining traction in the takeover market, and as many as a fifth of the participants now consider pre-defined ESG criteria to be important.

2.4. How are transaction risks mitigated and information obtained?

The participants are generally not overawed by the current drivers of uncertainty – such as monetary policy, the war of aggression against Ukraine and the energy crisis. Nevertheless, the drive to mitigate the risks involved in a takeover offer, and thereby increase the likelihood of the transaction's success, has increased slightly compared to 2018 with respect to all of the measures that we asked about.

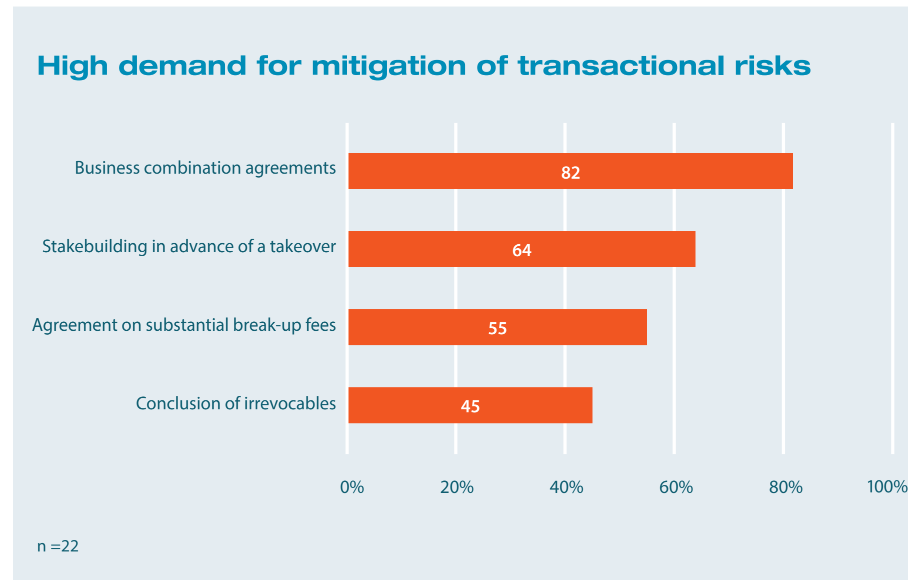


Figure 5: Measures to increase transaction certainty (multiple selections possible)

More than four fifths of the participants say that they want to use business combination agreements (BCAs) in advance of their takeovers in order to mitigate their transaction risks (see *New trends in business combination agreements, delisting agreements, etc.*, page 74) (see Figure 5). The second measure of choice is stakebuilding in advance of a takeover, i.e. building up a significant stake before making an offer, which two thirds of the participants name as important. Almost half mention the conclusion of irrevocables. These are irrevocable undertakings by shareholders with a significant stake in the target company that are given in advance of a takeover offer, committing the shareholders to sell their blocks of shares to the bidder.

Contractual clauses within the framework of the offer conditions that would allow a bidder to withdraw from the transaction are also gaining in importance. More than two thirds of the participants consider it important to make their offers conditional on the absence of an actual or potential Market Material Adverse Change, Target Material Adverse Change, compliance breach and/or insolvency. Just under half consider it important to include a condition making it a requirement not to plan any corporate actions.

Market Material Adverse Change clauses refer to events such as environmental or natural disasters, military conflicts, global pandemics, or even to developments on the stock markets – i.e. they are not company-specific. These clauses have, for obvious reasons, become much more important in recent years. On the other hand, Target Material Adverse Change clauses tend to be used to protect against uncertainties in the target company's industry environment or with regard to its economic development.

Companies are reacting to the increased uncertainties by requiring additional information in order to avoid unpleasant surprises. Only a small minority is willing to rely entirely on publicly available information. Four fifths of the participants see a need to conduct at least a red flag due diligence review (in which the target company and its business areas are analysed using non-publicly available data) when preparing a public offer. In 2018, only two thirds of the participants did this.

2.5. How are takeovers financed?

Financing must be in place before a takeover can be launched. The usual methods are financing with debt and/or existing cash reserves. The participants consider the two methods to be equally important. Despite the central banks' interest rate turnaround, four fifths of the participants rely on loan commitments by their banks (see *Financing public takeover offers with debt*, page 84). The same result emerged for participants using their own cash reserves. This underlines the finding described in section 2.1 above that many companies have sufficient financial reserves to finance takeovers with their own funds.

All in all, both sources of cash have become more important since 2018. At that time, only three fifths of the participants reported having sufficient cash reserves. Only half had prepared for a potential takeover by obtaining a credit commitment from a bank consortium.

Once its takeover plans are definite, an acquiring company must decide how to acquire the target company's shares. It has three options:

- a payment of cash from its own liquidity reserves and/or external financing through bank loans,
- an exchange of its own shares following a capital increase, or
- a combination of both.

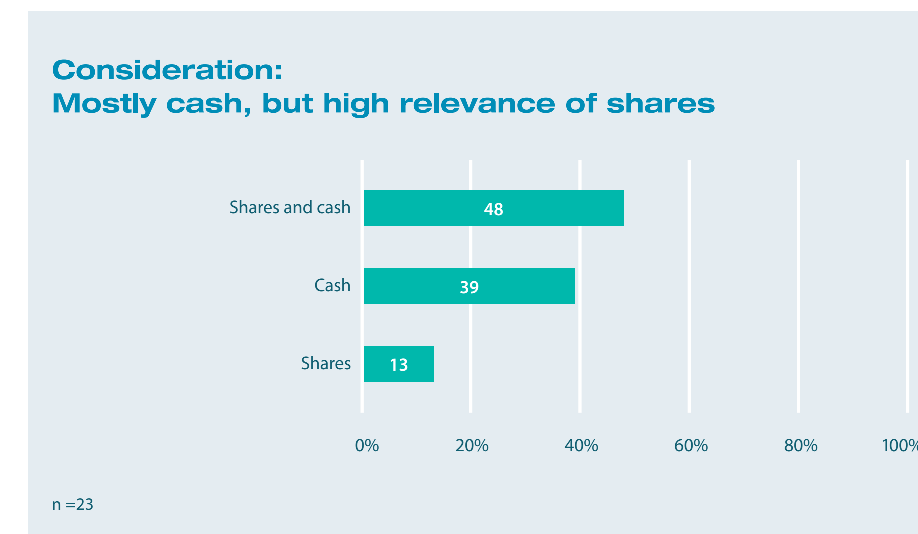


Figure 6: Preferred consideration for the target company's shareholders

Almost half of the participants said that in a public takeover they would offer the target company's shareholders a combination of shares and cash (see Figure 6). It is also interesting to note that almost two thirds see shares as at least part of the consideration. Exchange offers preserve liquidity but are significantly more difficult to implement in Germany – especially in view of the current practice of the German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin) following a recent judgment of the Frankfurt Higher Regional Court (see box). This is also why the use of shares as an acquisition currency has not achieved a breakthrough in Germany. This is confirmed by practice. In 2022, not a single takeover offer in Germany included an exchange offer. In 2021, there was just one mixed offer and one exchange offer in 33 takeover proceedings.

Case law is making share for share exchanges increasingly difficult – especially for smaller companies, as their shares are usually less liquid. Nevertheless, one third of the SDAX companies said they would prefer to offer just shares and half a mix of cash and shares. Two thirds of the MDAX companies said that a mix of shares and cash is their method of choice. While the companies would like to use share for share exchanges, a judgment by Frankfurt Higher Regional Court has made it much more difficult for them to do so.

Shares as consideration

In accordance with the statutory framework, consideration may consist of a cash payment in euros or liquid shares that are admitted to trading on an organised market. If holders of voting shares are offered shares as consideration, such shares must confer voting rights. BaFin may prohibit the offer if the shares do not qualify as "liquid". The criteria for assessing whether a share qualifies as liquid have become significantly stricter following the judgment of the Frankfurt Higher Regional Court in the Biofrontera case on 11 January 2021 (ref. WpÜG 1/20). According to the Frankfurt Higher Regional Court, a share must, to qualify as liquid, be traded daily and have a free float of at least EUR 500 million. In addition, the average daily number of transactions in the share must be at least 500 and the average daily transaction volume in the share must be at least EUR 2 million. Although BaFin has adopted this judgment in its administrative practice, it has continued to be criticised in academic publications for significantly overshooting the mark (see, for example, Kiefner/Kiesewetter, Die Liquiditätsanforderung bei öffentlichen Tauschangeboten gem. § 31 Abs. 2 Satz 1 WpÜG [Liquidity requirements in public exchange offers pursuant to section 31 para. 2 sentence 1 of the German Securities Acquisition and Takeover Act (Wertpapiererwerbs- und Übernahmegesetz, WpÜG)], Bank and Capital Market Law Journal (BKR) 2021, p. 265 et seqq., as well as Diehl/Heinrich, Are exchange offers experiencing a renaissance?, page 52).

These requirements deprive smaller companies especially of the option to make exchange offers, because their shares are less liquid within the meaning of the requirement.

2.6. How are minimum acceptance thresholds, the need for legislative reform and integration measures viewed?

Public takeovers are often subject to the condition that a certain number of shares in the target company must be tendered to the bidder. Such a minimum acceptance threshold will facilitate further integration measures regarding the target company, for example a delisting, a squeeze-out or the conclusion of a domination and profit transfer agreement. These measures all presuppose the acquisition of different minimum portions of a target company's share capital.

Several takeover attempts have failed in the recent past, at least at the first attempt, because the minimum acceptance thresholds were not reached. Bidders often had to waive or reduce the thresholds so that the takeovers could proceed.

The investment regulations of index funds are a major reason for offers failing to reach minimum acceptance thresholds. These regulations often only allow the funds to tender shares in response to offers when it is certain that the target companies will leave the relevant indices. In practice, this means that they cannot tender their shares during the initial acceptance period, but only during the two-week extension that occurs after the expiry of the original acceptance period (the so-called "fence-sitting rule" (*Zaunkönigregelung*). As index funds are becoming increasingly important as shareholders, their shares are often needed to reach or exceed minimum acceptance thresholds. In addition, one of the favourite tactics deployed by hedge funds in takeovers is to tender as late as possible, betting right up to the last moment on an increase in the offer price or on a further supplement as part of the integration measures after the offer has expired.

These experiences are probably one reason for the participants planning with lower minimum acceptance thresholds than they did in 2018. At that time, more than a third of the participants aimed to acquire at least 90 percent of the target company's registered share capital. In our new survey, only just under a fifth of the participants consider it necessary or possible to reach a 90 percent threshold. Just over a third of the 2022 participants said their aim now is to reach a minimum acceptance threshold of at least 75 percent of the registered share capital. Exactly the same proportion aim to acquire at least 50 percent.

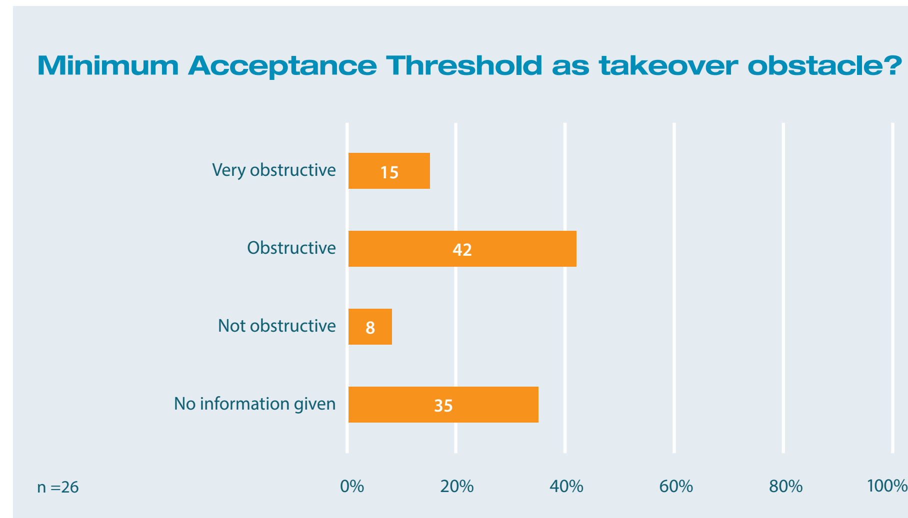


Figure 7: Assessment of index funds' investment regulations and hedge funds' tactical behaviour

So how do participants assess index funds' investment regulations and hedge funds' tactical behaviour? More than half of the participants describe both as obstacles to takeovers (see Figure 7). Interestingly, this view is expressed mainly by MDAX and SDAX companies. We find this surprising, as larger bidders tend to focus on larger target companies and index funds tend to be invested in larger companies.

More than 40 percent of the participants therefore consider the need for amendments to the WpÜG to be great or very great. Only a tenth of the participants see no need for the WpÜG to be amended, and half do not express a view. Interestingly, the SDAX participants not only see themselves as most affected by the index and hedge funds but also see the greatest need for the WpÜG to be amended.

Reform regarding minimum acceptance thresholds?

If a takeover offer is subject to a minimum acceptance threshold, the bidder can waive it up to the working day before the expiration of the acceptance period. However, it is difficult to predict how the target company's investors will behave at that time. Many larger investors wait until the last day for acceptance before deciding whether to tender their shares or not. Hedge funds often bet on a higher offer in the later stages of takeover proceedings. Due to their internal regulations, invested index funds cannot usually tender their shares in a target company, unless and until the bidder has announced that it has more than 50 percent of the voting rights.

If the minimum acceptance threshold is not reached, the offer fails. If the bidder wishes to continue its offer, it has no choice but to submit a new takeover offer. In this case, the WpÜG generally provides for a one-year delay period. However, BaFin can exempt the bidder from the delay period, upon written application, if the target company agrees to the exemption.

The takeover proceedings regarding Vonovia/Deutsche Wohnen are a well-known example of an offer failing because the minimum acceptance threshold was not reached. Vonovia's first offer in June 2021 achieved only 47.62 percent of the registered share capital rather than the required 50 percent. This was attributed in part to the fact that index funds could only have tendered their shares if the acceptance period had been extended. Vonovia announced a further offer in August 2021 and waived the minimum acceptance threshold in September 2021. It completed the takeover in October 2021. By the end of October 2021, Vonovia had acquired 87.6 percent of Deutsche Wohnen's registered share capital.

There have been several similar cases in recent years, so the legal framework regarding minimum acceptance thresholds is facing increasing levels of criticism. Some amendments to the WpÜG have already been proposed in this context (see Kiefner/Kiesewetter, Some suggestions from the advisory practice for amending the WpüG, page 100; see also Verse/Brellochs, Der Verzicht auf die Mindestannahmebedingung im Übernahmerecht [Dispensing with the minimum acceptance condition in takeover law], ZHR 186 (2022), page 339 et seqq.).

While the minimum acceptance threshold is less important for 90 percent of the participants, more than 80 percent regard the squeeze-out, which the German Transformation Act (Umwandlungsgesetz, UmwG) only permits with a shareholding of 90 percent or more, as a key integration measure. This is followed by the domination and profit transfer agreement, mentioned by just under 70 percent of the participants.

The fact that the participants attach great importance to squeeze-outs, which ultimately result in delistings, is in line with transaction practice: there is a trend to move from public to private (see *A snapshot of the German takeover market in 2022*, page 34).

3 The target company's perspective

In the following sections, we consider the participants' perspectives as potential target companies. This includes how the participants assess the risk of being taken over and how they prepare for such an eventuality.

3.1. How likely is your own company to be taken over?

While the takeover market offers companies opportunities to improve their own competitive situations by buying attractive target companies, they also face the constant risk of themselves getting into bidders' sights as target companies. How do the participants assess the likelihood of being taken over in the next three years?

Only slightly more than a tenth think that they are likely to be taken over (see Figure 8). No participants ticked the "Very likely" box in the questionnaire. Five years ago, 5 percent of all participants, and as many as 11 percent of the SDAX participants, replied by saying that a takeover was very likely.

Smaller companies are more likely to expect to be taken over. Unsurprisingly, no SDAX participants said that a takeover was unlikely. About a fifth of the MDAX and SDAX participants felt that a takeover was likely. When asked where a bidder might come from, most participants answered: the USA.

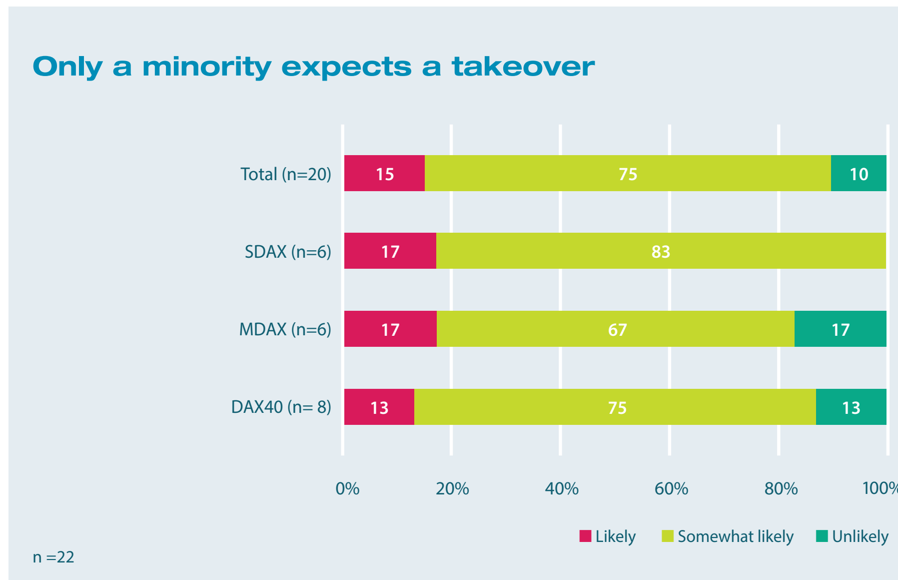


Figure 8: Likelihood of a takeover attempt in the next three years

As with our 2018 survey, the current survey shows a certain discrepancy between the statements. On the one hand, few participants believe they are likely to be taken over. On the other hand, almost two thirds of the participants stated that potential bidders had approached them – which could indicate that their companies were likely to be taken over. This also suggests that the number of approaches by potential bidders has increased significantly since 2018, when only 40 percent of the participants answered this question in the affirmative.

Potential bidders are more likely to approach the smaller companies: about 80 percent of the MDAX and SDAX participants say they have been approached, compared to only half of the DAX40 participants. It therefore appears that companies with smaller market capitalisations are more likely to be targeted for takeovers.

About 70 percent of the participants had been approached by strategic bidders, and just under 30 percent by private equity investors. In 2018, as many as 90 percent of the participants had been approached by strategic bidders, and the rest by private equity investors. Strategic bidders have held back over recent years because of companies' high valuations on the capital markets, and this may be why the participants have seen a drop in approaches from this source.

3.2. How are companies preparing for potential takeovers?

Even though most of the participants do not expect to be taken over, many have already been approached by potential bidders. Companies should use appropriate measures to assess the likelihood of takeover attempts and their chances of resisting them successfully.

3.2.1. Measures for assessing the risk of being taken over

We asked about seven measures for assessing the risk of takeover attempts (see Figure 9). Well over 60 percent of the participants ranked six of them as important or very important. Almost all of the participants rated analysing their own share price and shareholder structure, and entry and exit prices, as important or very important. The next most popular measures were analysing relative performance compared to competitors, and analyst reports and investor feedback.

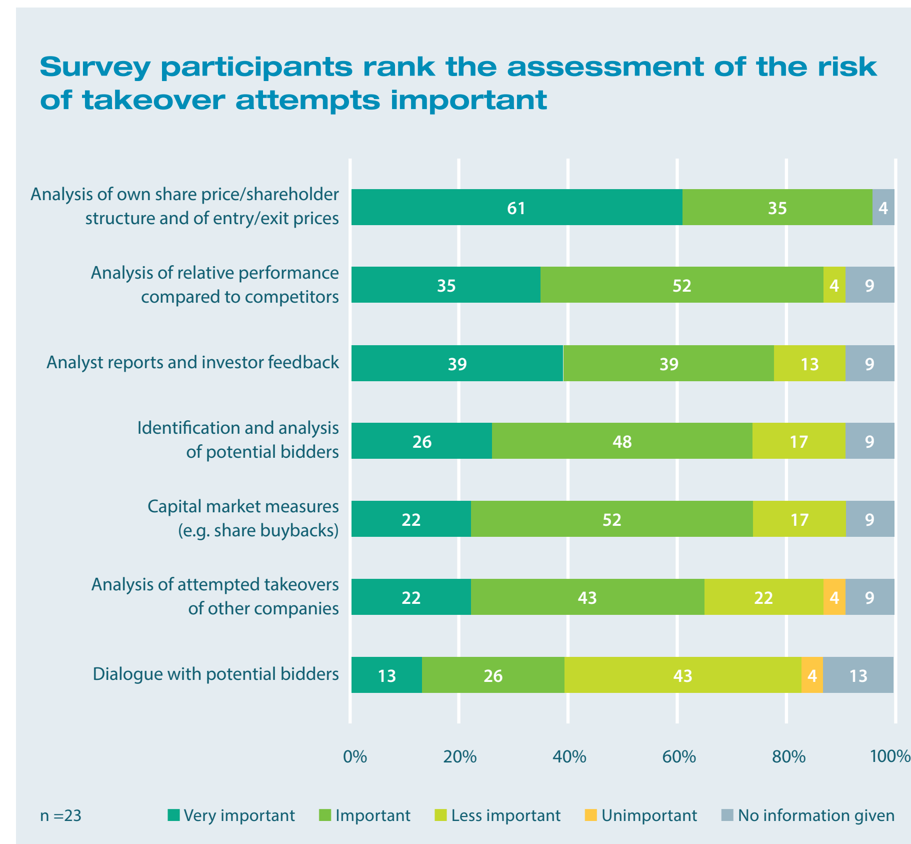


Figure 9: Measures for assessing the risk of takeover attempts

Most of the measures are currently rated as more important than they were in 2018. The analysis of capital market measures (e.g. share buybacks) has experienced an enormous increase in importance. Today, almost 75 percent of the participants see these as important or very important, compared to only half in 2018.

We also asked the participants whether they actually use these measures. The replies show that aspiration and reality are largely aligned in this case. The measures that the participants rate as very important or important are generally also the ones that they use the most. The only significant gap that we found between their assessment of a measure's importance and their actual use of that measure was in their dialogue with potential bidders. Almost 40 percent of the participants rate this measure as important or very important, but only 22 percent actually have engage in dialogue with potential bidders.

3.2.2. Preparing for a bidder's approach

Assessing the risk of a takeover is one thing but responding swiftly with appropriate measures if a bidder makes a surprise approach is quite another. Companies should be prepared for such an approach so that they can immediately respond. Again, we asked the participants how important they thought the various measures were and whether they actually used them.

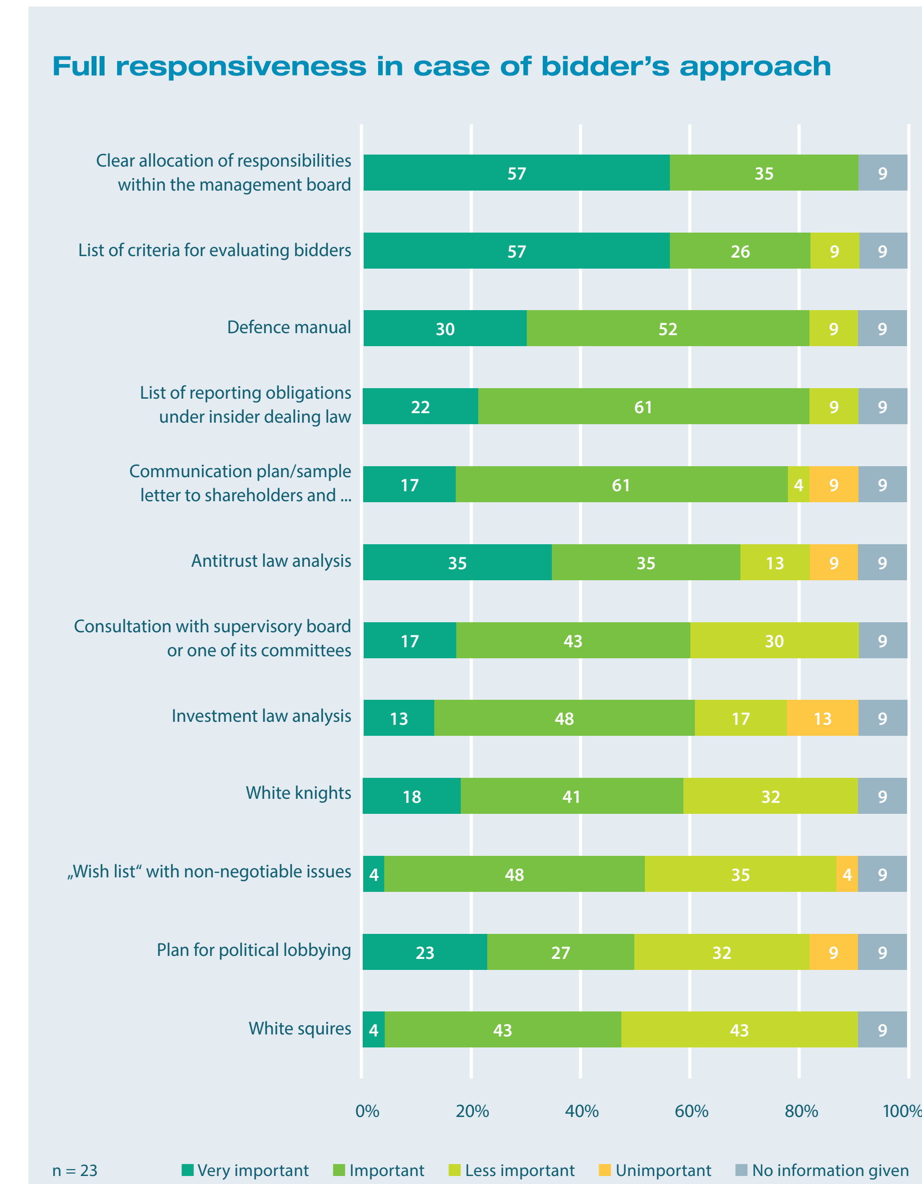


Figure 10: Measures for responding to approaches by potential bidders

Almost all of the participants said that a clear allocation of responsibilities within the management board for takeover issues was important or very important (see Figure 10). Over 80 percent think that a defence manual, i.e. a handbook or guidelines on measures to be taken (especially in the first 48 hours after an approach), is important or very important. The same proportion think that preparing for the reporting obligations that a company must observe under insider dealing law when subject to a takeover offer and the list of criteria that potential bidders must meet are important or very important. Almost 80 percent of the participants regard a communication plan to inform shareholders and other stakeholders about a takeover attempt and (if the management board and supervisory board consider an attempt to defend the company to be worthwhile) to mobilise them as important or very important.

The list of criteria for evaluating potential bidders has grown in importance since 2018. At that time, just under half of the participants rated this measure as important. Now, over 80 percent regard it as important or very important. 92 percent now consider that a clear allocation of responsibilities for takeover issues is important or very important, compared with more than 70 percent five years ago.

3.2.3. How much are these measures actually used?

While almost all participants regulate responsibilities within the management board for responding to a bidder's approach, only just over 40 percent maintain a list of criteria for evaluating potential bidders. This means that more than 40 percent of the participants consider this measure to be important or very important, but do not actually use it. There is a similar discrepancy in the case of a white knight, i.e. a company that could submit a competing offer in response to a takeover offer. Although almost 60 percent of the participants consider white knights to be important or very important, less than a fifth have any idea specifically who might act as one on their behalf.

Almost half of the participants consider that support from an anchor shareholder (known as a "white squire") to block a hostile takeover offer is a useful measure for fighting off a hostile takeover. However, not even a fifth of the participants have a list of white squires who could come to their rescue in the event of a takeover.

The participants also have little enthusiasm for a so-called "wish list" – a list of requirements that a target company will insist upon when negotiating a takeover and concluding a business combination agreement. Just over half of the participants think that a wish list is important. But implementation is lagging behind aspiration in this case as well, because less than a third of the participants actually have such a list.

Gaps between aspiration and reality are also evident with the list of reporting obligations under insider trading law, the defence manual and the communication plan. While 80 percent of the participants consider these measures important or very important, only about two thirds actually use them.

4 What role do activist shareholders play in takeovers?

Activist shareholders will continue to keep listed companies on their toes in the future. They buy into companies via minority stakes and then campaign for changes to the companies' strategic directions. They generally try to influence companies' strategic directions by means of minority shareholdings rather than takeovers. Since this is a topical issue, we included it in the questionnaire.

The takeover proceedings relating to Vantage Towers, a radio tower infrastructure provider, show just how topical this issue is. Oak Holdings, a bidding consortium led by KKR (a private equity investor) and Global Infrastructure Partners (an infrastructure fund), launched a takeover offer in November 2022 in cooperation with Vodafone. At the end of January 2023, following the expiry of the offer period, Elliot (an activist investor) took a voting stake of over 5 percent in Vantage Towers. On 20 March 2023, Vantage Towers announced that it had entered into a delisting agreement with Oak Holdings, which at that point held 89.3 percent of the shares in Vantage Towers after completing its takeover offer. The next step is to offer Vantage Towers' shareholders EUR 32 per share – the same price as in the voluntary takeover offer – pursuant to the delisting acquisition offer. Whether the delisting succeeds will depend, among other things, on what the activist shareholder Elliott does.

The takeover offer made by the Advent, Centerbridge and Canada Pension Plan Investment Board trio of investors for Aareal Bank at the end of 2021 also initially failed due to resistance from activist shareholders – in that case two hedge funds. The takeover proceeding eventually succeeded in May 2022, after the bidders had secured the support of important shareholders.

The participants report having adapted to the presence of activist shareholders. Now only a fifth say that they have not prepared for campaigns by activist investors, compared with a quarter in 2018 (see Figure 11).

Figure 11: Activist shareholders

The participants who take precautions focus on continually analysing weak points on which they could be attacked. For example, they may analyse the development of their share prices or possible weaknesses in their corporate governance arrangements. Just over a third actively seek dialogue with critical institutional investors.

In particular the larger companies are already prepared: all of the DAX40 participants say that they have taken precautions. But an increasing number of smaller companies are also adapting to activist shareholders. 70 percent of the SDAX participants say that they are ready. Five years ago, the situation was exactly the opposite. Back then, two thirds of the SDAX participants said that they were not preparing for an approach from activist shareholders (see *Communication with, and potential responses to, activist investors*, page 42).

5 What role do advisors play?

A takeover is a complex process in which different advisors offer their services at different stages. These include introducing potential candidates for acquisitions. Such introductions are mostly made by investment banks (according to about 90 percent of the participants) or M&A advisors (according to just under half).

All participants named banks when asked which advisors they generally rely on in M&A transactions. Many also named law firms and auditors. As in 2018, communications consultants play a less important role.

This does not mean that communication consultants are underestimated in general. Indeed, more than 60 percent of participants rate the services of communications consultants as important or very important – especially when companies find that bidders have them in their sights as candidates for takeover (see Figure 12).

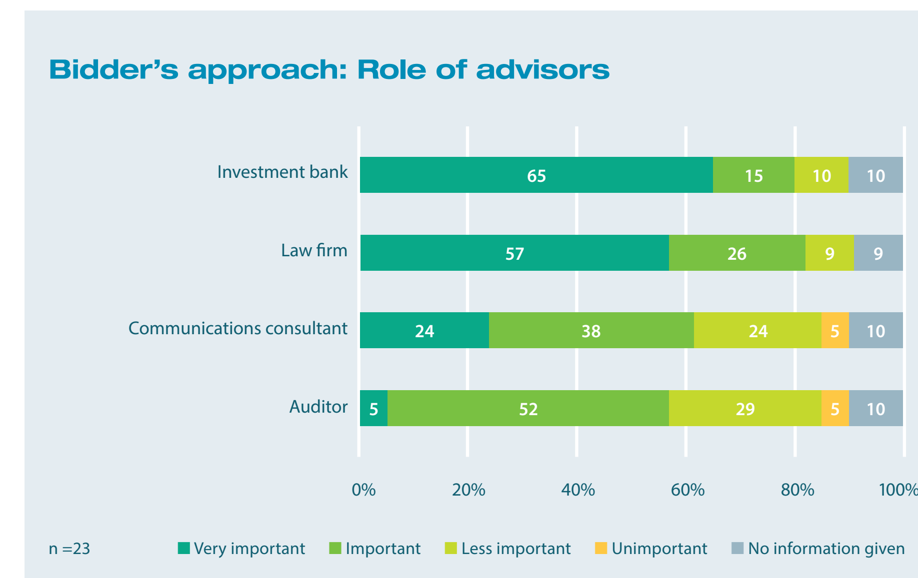


Figure 12: Retention of advisors in the event a bidder approaches

This indicates that communicating with the market and the public is an essential measure from a target company's perspective – especially in the case of a hostile takeover. From a target company's perspective, only investment banks and law firms are more important than communications consultants.

The importance of advisors was also evident when we asked the participants whether they would seek fairness opinions to confirm their own valuations when targeted by bidders. More than 90 percent of the participants say they would commission an external expert to give an opinion on the fairness of the purchase price in a takeover proceeding. 40 percent of the participants say that they would even obtain separate fairness opinions for their management boards and supervisory boards.

The participants' statements about obtaining separate fairness opinions for their management boards and supervisory boards are not (or not yet) in line with transaction practice. In 2022, one or more fairness opinions were obtained in nine cases in German takeover proceedings – as fairness opinions are usually dispensed with in the case of pure delisting offers. It is standard for management boards and supervisory boards to submit joint statements pursuant to section 27 WpÜG, and these usually rely on one or more jointly obtained fairness opinions.

Part 2

Recommendations from legal practice

1 A snapshot of the German takeover market in 2022

Dr Alexander Kiefner
White & Case LLP

Sabine Kueper
White & Case LLP

The 2022 German takeover market was characterised by a small number of transactions overall, a drastic slump in transaction volumes, an increasing role played by private equity bidders, a large number of delisting offers, as well as fewer cases involving takeover premiums and a predominance of friendly transactions with positive support provided by management. Notwithstanding the considerable drop in stock market prices in 2022, the takeover market was also seen as being in crisis by potential bidders.

The turning point signalling the end of familiar certainties came when Russia attacked Ukraine on 24 February 2022, a change which - combined with stringent (albeit recently lifted) restrictions imposed by the Chinese government in response to the COVID-19 pandemic and their implications for global supply chains - served as a deterrent to bidders and investors alike.

Higher energy prices and supply chain bottlenecks translated into spiralling inflation, which central banks were only able to contain to a limited extent (despite hiking their key rates several times). Following the slump in share prices in February, stock exchange prices began to recover very sluggishly in the face of investor restraint in response to the global political crises. Starting in October 2022, however, climbing share prices saw the DAX40 bounce back to almost January levels by the end of the year.

Despite the recovery in prices at the end of the year, most investors remain sceptical. Potential strategic bidders appear to be focusing on the risk of paying too high a price for an investment in a competitor, or in a company that is attractive for other strategic reasons. As a result, the public takeover market was quiet in 2022, with private equity investors also adopting a cautious stance.

1.1. Trends on the public M&A market in 2022

1.1.1. Only a small number of WpÜG offers in 2022 and lower overall volume in a year-on-year comparison

Compared to the record previous year, the market for public takeovers as defined by the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz*, WpÜG) declined sharply in 2022 in terms of both the number of offers published and their volume. As was already the case in 2021, one dominant trend was that of listed companies sought delisting from the regulated market. In 2022, half of all WpÜG offer documents were published with the aim of withdrawing from the stock exchange's regulated market upon completion of a delisting offer. Many companies appears to feel that, given the extensive reporting requirements under capital market law, access to the capital market is becoming a less attractive option. Private equity investors, in particular, are increasingly pursuing the option of delisting (accepting their subsequent inclusion in the OTC market at the instigation of other market participants until a potential squeeze-out at a later date). One recent example from 2022 is that of the announcement of the planned delisting in connection with the voluntary takeover offer for Vantage Towers made by a bidding consortium comprising KKR and Vodafone. Another example dating back to 2021 involved Easy Software's delisting in a move initiated by Battery Ventures.

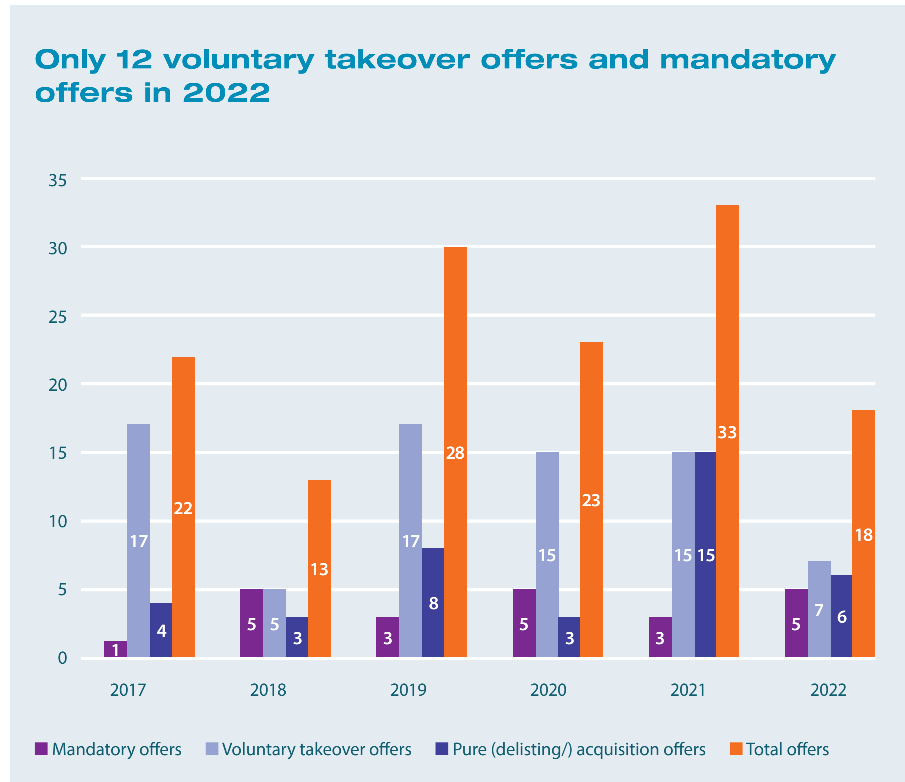


Figure 13: Number of WpÜG procedures in 2017-2021 (excluding prohibitions)

Out of the total of 18 WpÜG procedures initiated in 2022 (including one published prohibition), six were pure delisting offers; in two other cases, a mandatory offer was combined with a delisting offer; in another case, a voluntary takeover offer was combined with a delisting offer (see Figure 13). The number of delistings initiated accounted for nine, i.e. half, of all WpÜG procedures, making up a significant share of the public takeover market for the second year running. By way of comparison: only three delisting offers were published out of a total of 23 WpÜG procedures in 2020.

In 2022, only seven voluntary takeover offers were published, cutting the number of voluntary takeovers in half compared to the previous year. The number of mandatory offers remains very low at only two; another two mandatory offers were combined (in one of those cases, with a delisting offer – which was also not open to the inclusion of conditions – and in the other case with an acquisition offer made by a second bidder). This is evidence for the further consolidation of a trend that was already observed in 2021 towards avoiding mandatory offers if at all possible in scenarios where control is about to be acquired.

Moreover, the volume of takeover transactions in 2022 was down considerably in a year-on-year comparison. The offer for the mobile infrastructure operator Vantage Towers AG that was published on 13 December 2022 by a consortium comprising KKR and Vodafone increased the total volume of all offers in 2022 to EUR 21.4 billion – leaving this offer out of the equation, the total volume would have come to only EUR 5.3 billion. In 2021, the total transaction volume was more than EUR 67 billion.

1.1.2. Only three transactions running into the billions

In 2022 there were only three deals with a transaction volume in excess of the EUR 1 billion mark. Aside from the offer for Vantage Towers, there was only the takeover offer for Aareal Bank (transaction volume of EUR 1.9 billion), made after a second takeover attempt made by private equity investors Advent and Centerbridge with the involvement of the Canadian pension fund CPPIB had failed a year earlier because the minimum acceptance threshold was not reached, and Oaktree's offer, made via an offer vehicle, for Deutsche Euroshop (transaction volume of EUR 1.4 billion), i.e. just three cases in total. White & Case was involved in the last two transactions.

This made 2022 the weakest year since 2016 in terms of the transaction volume of public takeovers (see Figure 14).

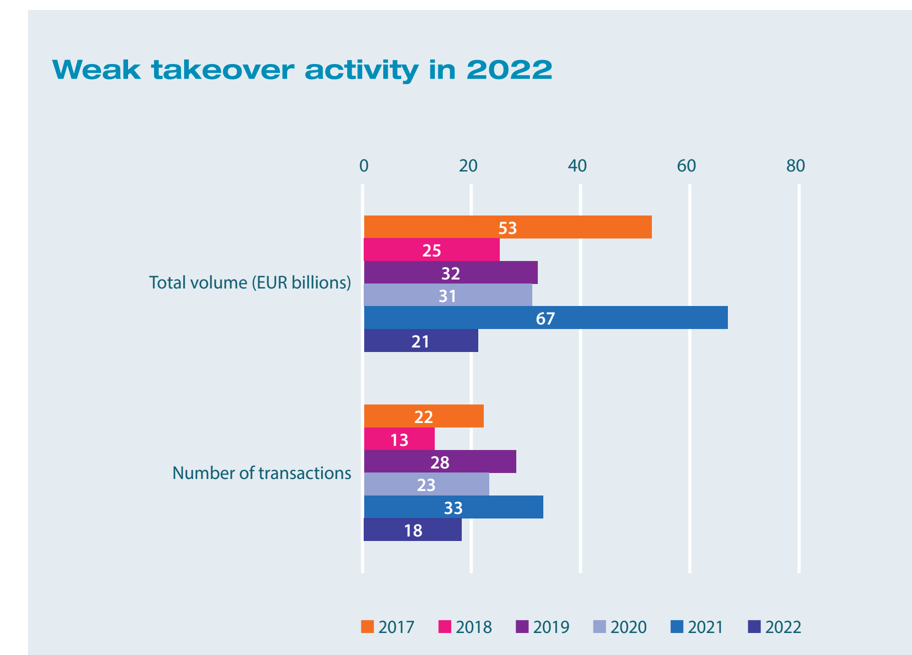


Figure 14: Volume and number of WpÜG transactions in 2017-2022

Additionally, the trend towards reducing the financing volume in WpÜG procedures by concluding non-tender agreements has become more established. If the shares blocked under these agreements are taken into account, the total transaction volume of all WpÜG procedures in 2022 is reduced further to only EUR 7.8 billion in total.

1.1.3. Only cash offers, mostly with no more than a small premium

The decision made by Frankfurt Higher Regional Court (Oberlandesgericht, OLG) on exchange offers (decision of 11 January 2021, WpÜG 1/20), and more especially in particular the further details it provides on the term "liquid share" and the associated considerable legal and practical hurdles for exchange offers (see *Are exchange offers experiencing a renaissance?*, page 52), mean that, when takeover procedures are being prepared, the use of shares as consideration is currently not regarded as an option when structuring an offer.

Shares were not offered as consideration in a single case – not even as an element of "mixed consideration" (see Figure 15).

Figure 15: Number of WpÜG transactions and the consideration offered

In the current market environment, dominated by rising interest rates and expectations of falling share prices, willingness on the part of investors to pay considerable premiums when taking over a listed company is the exception rather than the rule. In 14 out of the 18 WpÜG offers, the statutory minimum price within the meaning of sections 4 and 5 of the WpÜG Offer Regulation (*WpÜG-Angebotsverordnung*, WpÜG-AngebotsVO) was decisive when it came to defining the consideration offered. Genuine premiums that were not already predefined by the price paid for the earlier acquisition within the meaning of section 4 WpÜG-AngebotsVO were only paid in the takeover offers for Aareal Bank (1.5 percent on the price paid for the earlier acquisition and 16.6 percent premium on the average share price for the past three months) and in the takeover offer made to the shareholders of Deutsche Euroshop, who were offered a premium of 32.8 percent on the average share price for the past three months. In a number of cases, however, relevant premiums on the average share price for the past three months were paid due to high prices paid for the earlier acquisition within the meaning of section 4 WpÜG-AngebotsVO, for example the 19 percent premium recently paid for shares in Vantage Towers, the premium of between 25.4 percent and 141 percent for the Home24 shareholders (which varied from bidder to bidder) and the 82.8 percent premium featured in the offer that Nikon AM made to the shareholders of SLM Solutions Group AG.

1.1.4. No sectoral focus and active private equity bidders

Unlike the situation in 2021, a year characterised by a reshuffling of the cards within the real estate market, bidders did not focus on any specific sector in 2022. The voluntary takeover offers were made to the shareholders of a major provider of mobile infrastructure (Vantage Towers), an online furniture retailer (Home 24), a manufacturer of 3D metal printers (SLM Solutions Group), a pharmaceutical company (Biofrontera), a manufacturer of medical technology (Geratherm Medical), a shopping centre operator (Deutsche Euroshop) and shareholders of a bank (Aareal Bank).

All of the takeover transactions with transaction volumes of more than EUR 1 billion were executed by private equity firms in 2022. This confirms trends that had emerged in previous years and points towards a sustained high number of delisting offers.

1.1.5. Largely positive statements by the management and supervisory boards of the target company

It has since become the rule in the takeover market to prepare the way for positive support for the offer made to the shareholders of the listed company in advance by concluding corresponding business combination agreements or delisting agreements (see *New trends in business combination agreements, delisting agreements, etc.*, page 74). Consequently, it comes as little surprise to see that in 2022, in 14 out of the total of 18 WpÜG procedures, the management board and the supervisory board of the target company jointly recommended acceptance of the offer in the statements made pursuant to section 27 WpÜG, thus providing positive support for the WpÜG procedures – generally in line with the agreements that were concluded in advance.

1.1.6. Joint negative statements by the management and supervisory boards

The Management Board and Supervisory Board of artnet clearly rejected the offer made by Weng Fine Art AG. They levelled their criticism not only at the low price offered, in the absence of an attractive premium, but also at the objectives and intentions regarding the further development of the artnet Group that the bidder had presented in the offer document, which the boards felt were contrary to the interests of artnet and its stakeholders. Similarly, the Management Board and Supervisory Board of Biofrontera rejected the renewed offer made by Deutsche Balaton. Additionally, the employees of the various Biofrontera companies issued a negative statement.

1.2. What were the noteworthy special features of German takeovers in 2022?

1.2.1. New trends in how transactions are secured

As only voluntary takeover offers could be tied to closing conditions, the number of offers that included conditions was low, in line with the generally low level of takeover activity.

The first occasion when the current geopolitical situation was reflected in a condition was in Oaktree's offer for Deutsche Euroshop; the offer was subject to the condition of the collective defence clause in Article 5 of the North Atlantic Treaty of 4 April 1949 ("NATO Treaty") not being triggered by the North Atlantic Council pursuant to Article 9 of the NATO Treaty before the expiry of the acceptance period.

Both the takeover of Aareal Bank and the takeover of Vantage Towers (in each case by private equity investors) were tied to approval under foreign trade law. Nikon AM also required approval for the execution of the takeover to be issued by the competent investment control authorities in Germany, the United Kingdom, France, the United States and Canada (for information on the importance of investment control procedures in public takeovers, see *FDI screenings as showstopper?*, page 58).

1.2.2. Only one prohibition in 2022

The mandatory offer which the Swiss company Astutia Venture Capital AG made to the shareholders of ECHOS Holding AG, Frankfurt am Main, was prohibited by BaFin in a decision of 8 April 2022. The prohibition was based on section 15 (1) WpÜG, as at that time the Swiss bidder had not yet submitted an offer document meeting the WpÜG requirements to BaFin. Astutia Venture has not yet published any offer for ECHOS Holding AG, which is surprising given that the control threshold set out in section 35 WpÜG had evidently been exceeded, thus triggering the obligation to publish a mandatory offer.

1.3. No new court decisions in the field of takeover law (that would be relevant in the short term) in 2022

Neither Frankfurt Higher Regional Court (OLG) – the court responsible for WpÜG matters – nor the German Federal Court of Justice (*Bundesgerichtshof*, BGH) published any new court decisions in 2022 that would be of practical relevance in the short term.

The legal dispute surrounding the takeover of Postbank by Deutsche Bank AG, however, is moving into its next round, after already having been addressed by both Cologne Higher Regional Court and the German Federal Court of Justice on several occasions. In its judgment of 13 December 2022, the Federal Court of Justice referred the matter back to the court of appeal on the grounds that Postbank's shareholders might be entitled to higher consideration as part of Deutsche Bank AG's takeover offer, thus sending the legal dispute surrounding the takeover of Postbank into the next round. The court is now faced with the task of

clarifying, once again, whether Deutsche Bank exceeded the threshold of at least 30 percent of the voting rights in Postbank due to the attribution of voting rights associated with the shares that Deutsche Post AG already held at that time pursuant to section 30 WpÜG – considering investor protection clauses. According to the judgment, the attribution of voting rights is also possible in light of the fact that, based on the agreements, Deutsche Post AG already held the shares in Postbank for the account of the defendant – for the purposes of a dividend opportunity (section 30 (1) sentence 1 no. 2 WpÜG). In its ruling, the Federal Court of Justice explains that as the claim made is subject to the regular limitation period of three years (in accordance with sections 195, 199 of the German Civil Code (*Bürgerliches Gesetzbuch*, BGB)) it is not yet statute-barred (for details, see BGH, judgment of 13 December 2022, II ZR 9/21 and II ZR 14/21, full text available on the BGH homepage).

1.4. Conclusion

From a public takeover perspective, 2022 was a quiet year with no surprises and was dominated by global crises and uncertainty on the financial markets. At the beginning of 2023 there were no major changes to be noted. In particular, it is still the case that no major takeover transactions have emerged. It will be interesting to see whether more stable conditions on the financial markets, with stable interest rates and falling inflation, will encourage activity among potential bidders.

2 Communication with, and potential responses to, activist investors

Dr Alexander Kiefner
White & Case LLP

Dr Lutz Kraemer
White & Case LLP

Five to ten years ago, activist investors were seen in Germany primarily as a group that only pursued short-term interests that posed a threat to companies and their shareholders. This view has changed fundamentally over recent years, not just in terms of the significance of these investors and the likelihood of them taking action but also, in particular, in terms of how they are perceived by capital market participants and the media.

2.1. Successful rebranding of activist funds

The image that activists once had, namely that of "corporate raiders" or "short sellers" has undergone a fundamental change: By working together with conventional "long-only funds" major activist funds and hedge funds have managed to rebrand themselves as defenders of shareholder interests reacting directly to bad corporate governance and underperformance.

For listed companies, this means that the conventional "defence manuals" used to set out strategies designed to help defend against hostile takeovers now need to be modified to include reactions addressing what has become a more likely scenario: a campaign by activist funds. As a result, the defence advice found in the engagement letters used by leading investment banks includes provision for the full range of potential services, including both the reaction to campaigns by activist funds and support for genuine takeover scenarios.

Due to the increasing ties between "long-only funds" that are already invested and activist funds serving as their "mouthpiece", publicity campaigns are not only becoming more frequent, the accumulated voting power they can draw on at general meetings also makes them more dangerous for both the management board and the supervisory board. Recent trends, such as mandatory ESG components in (long-term) management board remuneration or – non-binding – Say on Climate resolutions at general meetings also provide activists with a welcome rostrum for showcasing their role as drivers of long-term shareholder interests, allowing them to bolster their public image in the media.

2.2. Actions to be taken by the management board and the supervisory board

The new patterns of activist behaviour, which can be observed across the globe, map out the challenges and the need for action by management and supervisory boards, in particular when it comes to achieving the right level of preparedness. First, companies need to make sure they familiarize themselves with what is now a highly differentiated landscape of international activist funds, including the ability to categorise them by looking at their past campaigns and the focus of their activities (see 2.3.). Second, consideration needs to be given to the typical areas activists utilize for an attack (corporate governance, group structure/spin-offs, capital allocation, underperformance in a peer group comparison and, most recently, lack of ESG resilience) – see 2.4 below.

Following a short description of the typical steps of escalation within an activist campaign (including the legal repertoire available to activist funds) (2.5.), the situations typically associated with special risks for companies are outlined in brief (2.6.) before examining in more detail how companies can prepare properly and adopt proactive defence strategies (2.7.).

Proper and timely preparation requires having a company culture which is self-critical and characterized by close involvement on the part of investor relations, legal, compliance/ESG and finance in order to ensure that any vulnerabilities within the company are identified on an ongoing basis as part of both an "inside-out" and an "outside-in" analysis.

2.3. The various types of activist shareholders – an attempt at categorisation

Activists can generally be split into categories depending on whether they behave aggressively and tend to favour publicity campaigns or are willing to be more "cooperative" and quieter in how they exert influence. There is also another group of activists specialising in arbitrage, especially merger arbitrage, which has more in common with hedge funds: sometimes referred to as agitators, they rely on confrontation that attracts publicity and tend to

be event-driven, meaning that their activities and investment horizons are generally geared towards the short term and aimed at maximising profits in particular situations, for example during a company takeover.

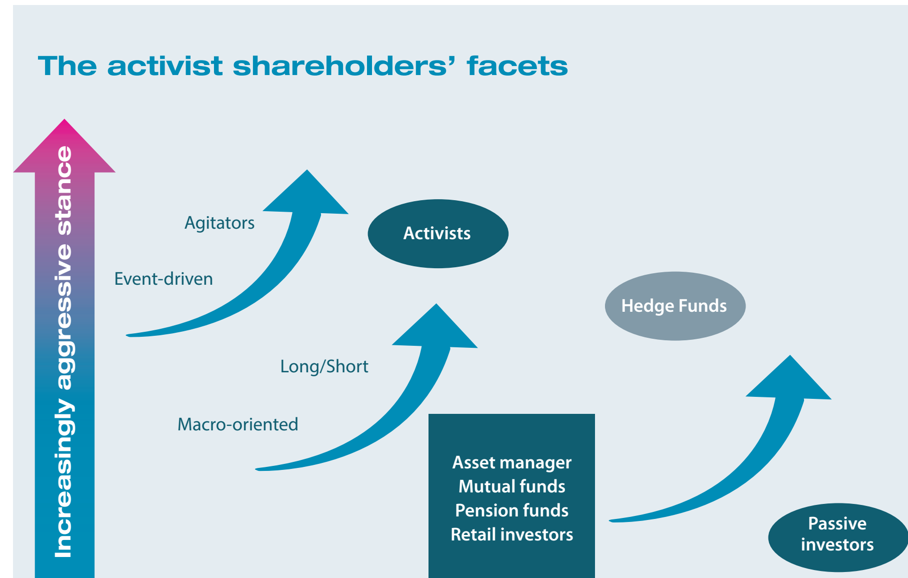


Figure 16: Spectrum of shareholder activism

Funds such as The Children's Investment Fund (TCI) or Wyser-Pratte typically begin exerting public pressure on management immediately after starting to invest. Their campaigns are typically aimed at selling specific divisions of the company, pointing towards genuine or alleged significant underperformance, as well as at collecting special dividends distributed due to alleged misallocation of capital. One example of a fund that takes a cooperative approach is Cevian Capital, which has invested in Bilfinger and Thyssen Krupp, acquiring significant stakes over many years. Such funds explicitly pursue the objective of being represented on the supervisory board and being able to discuss their expectations with management from their position on the board. Although hedge funds specialising in merger arbitrage, such as Elliott, have recently moved towards more long term and higher levels of investment, they often see takeover situation as an opportunity to exploit by pushing hard for an increase in the offer consideration due as part of the takeover process, or a higher compensation payment in the context of integration measures after a successful takeover.

The change in the investment approach pursued by long-term institutional investors such as pension funds or mutual funds like Blackrock, Fidelity, DWS, Union Investment or Allianz Global Investors has been a decisive factor in improving the prospects of success for activist campaigners. These investors have recently begun addressing similar clear requests to the management and supervisory boards of listed companies – in some cases publicly, for example in the context of the takeover of Osram by ams. It follows that the positioning adopted by the major mutual and pension funds has become a key criterion for the success of activist campaigns, and it is important to make sure that the analysis of their investment behaviour and current views on management performance are constantly monitored, reviewed and updated by the investor relations team. Interaction between activists and long-term institutional investors frequently results in a scenario where requests are first publicly raised by activists and then endorsed by (some of) the long-only funds. In order to ensure an appropriate reaction by the management and supervisory boards, good timing is essential – in particular if the next general meeting is scheduled to take place in the near future.

2.4. Typical areas of attack for shareholder activism

Figure 17: Wide range of possible touch points for attacks by activists

There are certainly geographical differences in this respect: in Germany, a significant number of campaigns launched by activist shareholders and hedge funds have been successful due to poor financial performance as represented by weak KPIs and/or alleged corporate governance deficits. For example, the Chairman of the Board of Managing Directors and the Chairman of the Supervisory Board of Commerzbank AG, the Chairman of the Supervisory Board and ultimately also the Chairman of the Executive Board of Thyssen Krupp AG, and most recently the CEO of Bayer AG, have all recently become the target of public campaigns due to alleged shortcomings in performance.

The table below presents an overview of the estimated capital employed by the five leading activist funds in Europe in 2022:

Investor	New investments	Volume
PERSHING SQUARE CAPITAL MANAGEMENT	1	$4.4 B
TRIAN FUND MANAGEMENT	1	$1.8 B
ELLIOTT MANAGEMENT	5	$982.8 M
THIRD POINT PARTNERS	3	$613.4 M
SARISSA CAPITAL MANAGEMENT	2	$412.2 M

Source: Insightia Shareholder Activism Report 2022

In the meantime, both Elliott and Cevian Capital have moved into single-digit billion USD territory, and Pershing Capital, which recently reported a switch from its previous strategy of attracting publicity through its campaigns to a more cooperative and longer-term approach, also accounts for a volume running between five and ten billion dollars.

The main areas which have come attack in the past - underperformance in a peer group comparison, misguided capital allocation with calls for special dividends, a focus on core competencies to avoid a conglomerate discount and corporate governance-driven attacks – have now been joined, in an increasing number of cases, by various ESG-driven demands. This new point of attack gives activists an opportunity to ride the wave of "green demands" and to hide their own interests (i.e. higher distributions and spin-offs) behind purportedly "green" concerns. This means that in the future even the more aggressive activists are likely to attempt to rebrand their activities by claiming them to be in the interests of society as a whole.

2.5. Covert and overt confrontation

The table below shows the typical stages, from acquiring a shareholding (usually only a small stake) through to approaching institutional investors and writing to the management, public campaigns and ultimately legal disputes. The key step is to contact and convince long-only funds that an improved capital allocation or a change in the makeup of the board will generate a higher enterprise value (through a sale of subsidiaries and a thorough sum-of-the-parts – analysis).

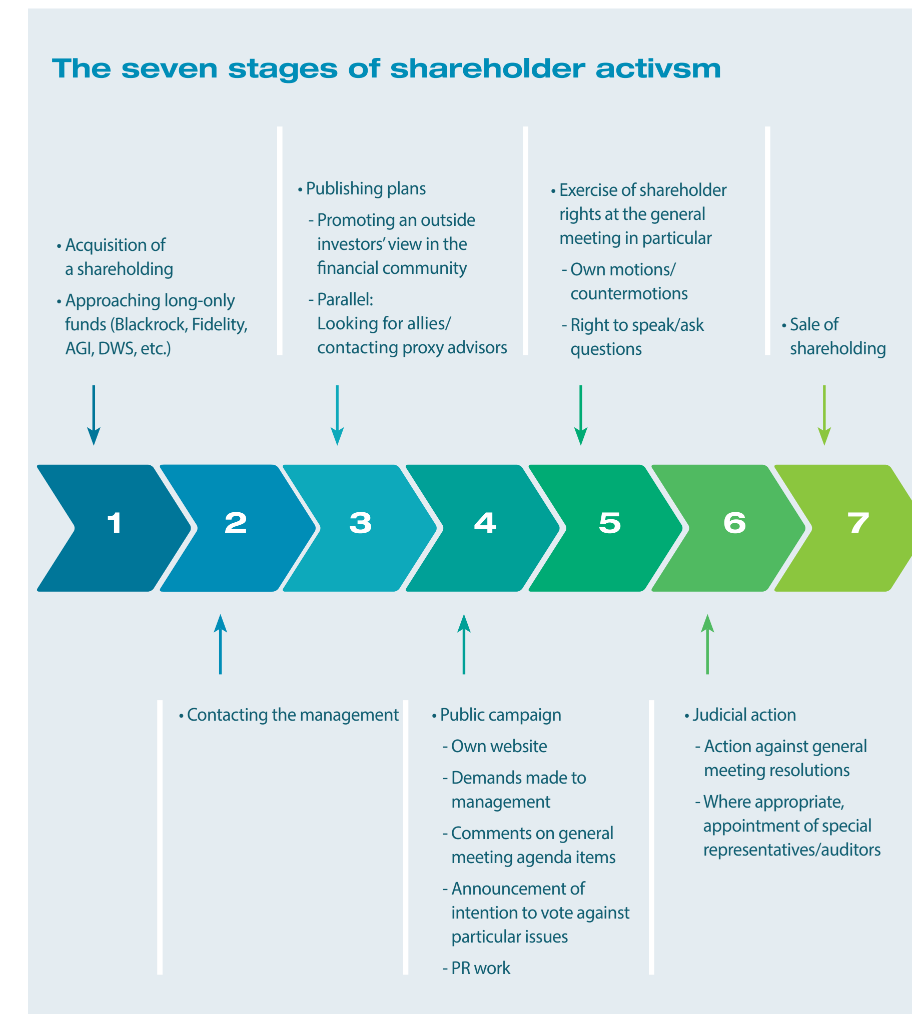


Figure 18: Typical steps of the activists

Regardless of the above, long-only funds are also adopting a much more critical stance than they did ten years ago, both before and during the general meeting. Particularly when it comes to addressing underperformance by management, a joint approach with activist funds is a likely scenario. While the first three months of the year used to be the key period for investor relations teams to liaise with institutional funds and proxy advisors, the preferred approach today should be one of permanent dialogue, especially where a company which has already identified weaknesses in its own strategy or where targets have been missed.

If and only if an unbiased analysis of investor opinion leads to the conclusion that activist shareholders would be unable to attract sufficient support can the activists' demands for talks be ignored and an imminent campaign countered by means of releasing appropriately aggressive counter-information. Activists will generally seek to make contact with the management board by sending a detailed letter requesting changes; if these are approved by the management board, they will generally move on to approach the chair of the supervisory board. These letters should be analysed meticulously and any response - where and to the extent appropriate – should be drafted with assistance from external legal and financial advisors.

The legal toolkit used by activist funds is typically limited to measures proposed at the general meeting as well as potential challenges to general meeting resolutions. The gateways used by activist campaigns to generate additional momentum include for example a refusal to grant discharge to the management board and/or the supervisory board, supervisory board elections with corresponding counter-proposals, alternative dividend resolutions, "Say-on-Pay" and, where applicable, "Say-on-Climate" resolutions. Proxy advisors play an extremely important role in this respect, as they usually form their opinions on management proposals early on – and often in a rather formulaic manner. It follows that management would be well advised to discuss any problematic or crucial items on the agenda with the proxy advisors in a timely manner, pointing out any special aspects that need to be taken into account and responding to objections in good time while adopting a highly sensitive approach. It is important to stress that discharge resolutions adopted with an approval rate of less than 80 percent are usually considered a defeat for the management and seen as evidence of a need to make improvements to investor communication. Regardless of their legally binding effect, defeats in "Say-on-Pay" or "Say-on-Climate" resolutions also have a negative impact on the professional image and the trust placed in both management and investor relations.

The paramount importance of proxy advisors in emerging activist campaigns becomes evident simply from considering the position of the market leader, Institutional Shareholder Services (ISS) - which has an estimated market share in excess of 50 percent among institutional investors, shaping the voting behaviour of these investors to a considerable degree (according to estimates, around 80 percent of foreign institutional investors in German companies follow the recommendations put forward by ISS and other advisors). The lesson from this has to be that companies should communicate proactively rather than simply waiting to react to voting recommendations.

Finally, the risk of negative recommendations being made by proxy advisors should be mentioned as it provides a – separate – gateway for activist campaigns; some activist shareholders deliberately rely on negative recommendations made by proxy advisors to justify a critical stance towards the company's management and take this as a basis for building a campaign. This sort of feedback loop between proxy advisors and activist shareholders can also develop particular momentum in takeover situations, as passive funds tend to wait to see whether a takeover offer succeeds in passing the critical 50 percent approval threshold. This means that a negative recommendation made by proxy advisors based on an activist campaign or, conversely, an activist campaign based on a negative assessment of a takeover offer by proxy advisors can both have an exponential impact on the risks associated with a transaction's success.

2.6. Situations associated with special risks for companies

The classic scenario where a company is performing less well than its peers or repeatedly fails to meet its own forecasts provide the fuel that drives conventional activist campaigns, which often succeed in getting members of the management board and/or supervisory board to resign due to the dissatisfaction that generally arises (also) among long-only funds. In contrast, campaigns relating to alleged misallocation of capital or "under-leveraged" balance sheets, often accompanied by demands for extensive share buybacks or special dividends, generally have fewer prospects for success. Complex group structures and the avoidance of conglomerate discounts have also had good prospects of success recently due to a trend towards focusing on core competences; although these "corporate clarity campaigns" have so far taken place primarily in the US and in London, lately they have been emerging in Germany as well (Bayer, Fresenius, etc.). After all, where a takeover scenario occurs and provides an occasion for the launch of a campaign, if the scenario involves a cash offer and not, as happens in exceptional cases, an exchange offer, the focus will usually be on arbitrage gains or "blackmail", rather than corporate clarity.

Over the next few years, corporate governance-led campaigns are likely to increase due to criticism levelled against the system of management board remuneration, the various scenarios where supervisory board members have shown themselves to be insufficiently impartial, as well as demands for an improved environmental policy focus ("green labelling"). Until such time as an industry standard has emerged, ESG reports that are allegedly lacking in transparency can be used by activists as another reason to refuse discharge or in support of their own proposals for the election of board members.

Due in particular to the volatility of the economy and developments in share prices in the wake of the COVID-19 pandemic as well as the disruption of old supply chains and the establishment of new ones, the corresponding reassessments of particular sectors provide fertile ground for activist campaigns. The EU's proposed Corporate Sustainability Due Diligence Directive, if transposed into national law, will put additional pressure on companies, as even where the greatest possible care is taken, problems in individual supply chains (especially those relating to complex products or larger product portfolios) cannot always be resolved adequately in a timely manner.

2.7. Proper preparedness and defence strategies

In today's world, index listed companies are constantly the focus of attention and criticism from activist funds. This makes it crucial for every management and supervisory board to have access to the latest information so that they can make sure they are prepared not only for potential hostile takeover offers, but also for public campaigns directed against their own corporate strategy. The key elements in this process of ensuring readiness are information, dialogue and organisation.

First, the company's own assessment of its financial performance and market capitalisation should be combined with a peer review as part of an unbiased, critical outside-in analysis, constant monitoring to check for any positive or negative deviations, identification of the underlying reasons for such deviations, and sounding them out critically with the help of external advisors.

Constant monitoring of trading volumes, voting rights announcements and changes in the investor base are just as essential as preparing a "heat map" of estimated purchase prices and average prices of major institutional investors. These provide a good indicator of willingness to support activist investors or, alternatively, to refrain from lending support to their campaigns due to satisfaction with the company's share price performance to date. Finally, all areas of the company must be reviewed to ensure sufficient synergies, a good strategic fit and compatibility with the core competences that the company has communicated.

Companies should ensure their capital structure is optimised on an ongoing basis using an appropriate mix of equity, debt and hybrid components, while also comparing the leverage they consider necessary against that of their peer group. Finally, companies should question their own corporate communications with regard to ambitious, less ambitious or missed targets, and regularly conduct a self-critical review of market response.

The second, and likely even more important, element involves constantly engaging in active investor relations work, encompassing transparent communications regarding performance, strategy and the use of funds, with equal attention being paid to all of the relevant target groups, i.e. investors, analysts and proxy advisors, as well as shareholder associations. Particularly during critical phases, companies should proactively seek dialogue rather than shying away from possible points of criticism or attack. Experience shows that some management boards prefer not to seek a timely process of dialogue with investors when targets have been missed, even in the face of strong recommendations to do so from their own investor relations team.

Finally, just as is the case when preparing for hostile takeovers, proper organisation and clearly defined roles are key: both the management board and the supervisory board ought to have a transparent system governing communications and clear channels of communication. It is advisable to make sure that the chair of the supervisory board is perceived as being there, willing and ready to stand alongside the CEO and, where appropriate, the CFO, and to engage in potential discussions with investors, and that he/she is well prepared and able to communicate accordingly. Investors can very quickly pick up on whether the supervisory board really is a true strategic sounding board for the management board and whether it supports the corporate strategy. The impact of any signs of strategic dissent between the management board and the supervisory board can be disastrous, especially during public campaigns

2.8. Recommendations for the management and supervisory boards' response to public activists' demands

In cases involving public campaigns, management and supervisory boards often disagree on whether and how to talk to activists or whether to reject their requests by referring to the company's own strategic considerations, or whether to simply ignore them.

There are two rules that have proven effective in practice (and which even representatives of activist funds have described as meaningful). If an activist's enquiry is still of a confidential nature, i.e. all that has happened so far is that the CEO has been contacted or confronted with strategic considerations set out in a letter from an activist (often a new shareholder holding a very small stake), then a – very well prepared – meeting with the activist is certainly to be recommended. First, every shareholder, regardless of how large or small their stake is, ought to be taken seriously and their ideas should be heard. Second, the management board can use the meeting with the activist shareholder as an opportunity to review its own assessment of the company's strategy, its corporate governance, its capital allocation, etc. in the face of especially critical objections. Even if the activist's letter or demands are going to be made public at a later date, the company will then be prepared for them and in a much better position to react.

If, on the other hand, activist funds go public right away or aggressively seek to go public following on from what they see as a fruitless meeting, further discussions are generally not to be recommended. At this stage, continuing to engage in discussions aimed at reaching a consensus will no longer be meaningful effective and tend to be seen as a sign of weakness. This view is shared by most activist representatives. In such cases, companies should focus on convincing their other shareholders and involving proxy advisors early on, so as to be able to win the proxy fight that is often inevitable in such cases.

Additionally, both of the forms of contact with activists referred to above should be taken as an opportunity for a further review of the impartiality and professionalism of the supervisory board members in view of an upcoming proxy fight. It is not uncommon for latent conflicts of interest to become apparent during the course of campaigns when the glare of publicity can mean that the assumed impartiality of the board members is forced to undergo a stress test. Companies can make sure that their reaction on the capital market is as prompt and professional as required in these situations by involving competent investment bankers, lawyers and PR advisors at an early stage.

3 Are exchange offers experiencing a renaissance?

Thilo Diehl
White & Case LLP

Dr Tobias Heinrich
White & Case LLP

In 2022, the significant increase in interest rates, high rates of inflation and a large number of geopolitical challenges changed the sentiment on the capital markets. This also had an impact on the momentum for public takeovers and bidders' strategic considerations regarding a potential public M&A transaction (see also *A snapshot of the German takeover market in 2022*, page 34). In terms of structure, exchange offers have re-entered the spotlight as an alternative to conventional cash offers, despite having played a relatively minor role in the past (see study, page 19 f.). Amidst current uncertainty in the capital markets, exchange offers could offer decisive advantages over conventional cash offers.

3.1. Pros and cons of exchange offers

One of the advantages of exchange offers is, firstly, that they preserve the bidder's liquidity. The bidder is only obliged to deliver liquid shares, rather than cash, to the target's shareholders. A takeover in the form of an exchange offer could therefore be feasible even in a difficult financing environment characterised by a drastic rise in borrowing rates; a comparable cash offer, by contrast, could be difficult or impossible to finance. Exchange offers can also be more economically attractive for the target's shareholders (particularly in times of very high inflation) who get to retain a long-term investment that offers protection against inflation. Due to the exchange of shares, moreover, the target's shareholders can continue to participate in the success of the combined companies without having to make a new investment decision.

One major disadvantage of exchange offers compared to their cash equivalents – apart from a much more extensive offer document – is the requirement to prepare a (listing) prospectus to admit the offer shares to trading on a regulated market in the European Union. The interaction between takeover and prospectus law often poses a challenge for exchange offers. For this reason, market participants generally consider leveraged cash offers to be the more practicable and attractive option. In addition, the implementation of a capital increase against contributions of the target's shares in kind and exclusion of pre-emptive rights always dilutes the bidder's existing shareholders. The exclusion of pre-emptive rights – at least in cases involving German bidders – also has to be justified in detail in order to meet the requirements under the German Stock Corporation Act (*Aktiengesetz*). Depending on the specific structure of the authorised capital (the utilisation of authorised capital excluding shareholders' pre-emptive rights at German companies is often limited to 10 percent of the bidder's registered share capital), a general meeting may need to be convened by the bidder to authorize the issuance of new shares. These challenges mean that executing an exchange offer requires more time than a cash offer would. It is important to remember, however, that cash offers are often financed using a short-term bridge facility, which is refinanced using debt and equity issues once the cash offer has been completed. If the bridge facility is refinanced using a rights issue, a prospectus also has be prepared – at least afterwards – as part of the refinancing of the cash offer.

This means that an exchange offer might be more attractive than a cash offer. Current developments with regard to exchange offers are summarised below.

3.2. Consideration in the form of shares

In an exchange offer, consideration is paid in the form of new, liquid shares of the bidder. German bidders generally use their authorised capital to issue the new shares against contributions in kind (while excluding pre-emptive rights), provided that the volume of the authorised capital is sufficient and the requirements for excluding pre-emptive rights are satisfied. By comparison, convening a general meeting to resolve on a capital increase is less flexible, particularly due to the extensive preparatory work and the notice period for convocation. Furthermore, a resolution of the general meeting is associated with considerable procedural and legal risks due to shareholders' ability to raise objections and file actions for annulment (*Anfechtungsklage*).

The authorised capital can only be created in a maximum amount of 50 percent of the registered share capital (section 202 para. 3 of the German Stock Corporation Act). However, the use of authorised capital by way of a capital increase against contributions in kind, with shareholders' pre-emptive rights being excluded, is often limited to 20 percent (or, in some cases, only 10 percent) of the registered share capital. Such restrictions are consistent with the recommendations of proxy voting advisors Glass Lewis and ISS.

If the amount of authorised capital is insufficient, then one option bidders have (short of convening a general meeting) is offering mixed consideration comprising shares and cash. If new shares corresponding to less than 20 percent of the bidder's registered share capital are created, then such shares may be admitted to trading on a regulated market without publishing a prospectus.

3.3. Share liquidity

If the bidder is seeking to achieve a takeover using an exchange offer, the German Securities Acquisition and Takeover Act ("Takeover Act") requires the consideration to be paid in "liquid shares". The German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, "BaFin") can prohibit the publication of the offer document if the shares offered are insufficiently liquid (section 15 para. 1 no. 2 of the Takeover Act). As there is no legal definition of liquidity in the Takeover Act, the interpretation of this term was controversial for some time.

3.3.1. BaFin's previous administrative practice

In previous decisions, BaFin focused, in particular, on whether the target's shareholders could sell the shares under reasonable conditions and in a timely manner in return for payment of cash consideration in euros.

3.3.2. New definition of liquidity

In the Biofrontera case, the Frankfurt Higher Regional Court sought to define the term "liquid shares" in greater detail in its judgment of 11 January 2021. Unlike in BaFin's previous decisions, which were always made on a case-by-case basis, the Frankfurt Higher Regional Court based this decision primarily on Article 22 (para. 1) of the MiFID Regulation (Regulation (EC) No 1287/2006). This means that the shares of a bidder must be traded daily and have a free float of at least EUR 500 million. Furthermore, there must either be at least 500 trades per day on average or at least EUR 2 million in average daily turnover. This has increased the requirements for classifying the shares offered as "liquid" significantly. BaFin's recent administrative practice suggests that it is following the approach taken by the Frankfurt Higher Regional Court and applying the liquidity criteria stringently.

3.3.3. Evaluation of the new definition of liquidity and practical consequences

The Frankfurt Higher Regional Court's decision and BaFin's subsequent administrative practice represents a significant blow to the public exchange offer market. Unless the recent court decisions on the definition of liquid shares are overturned soon or the (EU) legislator takes action, only a few bidders will be able to make exchange offers in the future. Applying the liquidity conditions, BaFin would have been forced to prohibit 40 percent of the pure exchange offers executed successfully over the past decade. In the future, the significantly more stringent requirements imposed by the Frankfurt Higher Regional Court are likely to result in exchange offers only being an option for bidders in the large-cap or upper mid-cap segments with sufficiently high levels of free float.

3.4. Prospectus Regulation and Delegated Regulation 2021/528

Exchange offers also have to take into account the requirements of prospectus law in addition to those of the Takeover Act. Prospectus law requirements have to be met with regard to both the further information in the offer document and the admission of the shares offered to trading on the regulated market (see section 11 para. 4 of the Takeover Act in conjunction with section 2 no. 2a of the Offer Regulation under the Takeover Act).

3.4.1. Previous legal situation based on Prospectus Directive

Before the Prospectus Regulation came into force on 21 June 2019, the content requirements imposed on bidders making exchange offers under prospectus law were characterised by what was known as the equivalence requirement. This meant that bidders had to prepare an annex to the offer document that contained information "equivalent" to that provided in a securities prospectus (cf. also Article 4 paras. 1b and 2c of Directive 2003/71/EC (Prospectus Directive)). As a result, the annex to the offer document and the listing prospectus for the offer shares were largely identical.

3.4.2. Current legal situation

With the Prospectus Regulation (Regulation (EU) 2017/1129), the European legislator moved away from the equivalence requirement for exchange offers. Bidders are now only required to publish an "exemption document" for the public offer and admission of securities to a regulated market (see Article 1 paras. 4f and 5e of the Prospectus Regulation), instead of having to prepare a prospectus (pursuant to Article 3 para. 1 of the Prospectus Regulation). As the exact form of the exemption document was unclear for some time, the German legislator continued to require inclusion of the minimum prospectus information in the offer document until the adoption of the relevant Delegated Regulation (see section 2 no. 2 1st half sentence of the Offer Regulation under the Takeover Act (old version)). As a consequence, the equivalence requirement continued to apply.

In determining the content of the exemption document, Delegated Regulation 2021/528 (which entered into force in 2021) distinguishes between three scenarios, in which the shares offered as consideration constitute (1) a primary issuance, (2) a secondary issuance or (3) a secondary issuance where the offer shares do not represent more than 10 percent of the bidder's shares that are already admitted to trading on the regulated market.

3.4.2.1. Primary issuance

Primary issuances are transactions in which the bidder's shares have not previously been admitted to trading on the regulated market. The shares are to be offered to the public and admitted to trading on a regulated market as part of the exchange offer for the first time (i.e., the bidder is not yet listed prior to the offer).

As the offer shares have not yet been admitted to the regulated market, stringent prospectus law requirements apply to a primary issuance (Article 2 para. 1 (4) of Delegated Regulation 2021/528 in conjunction with Annex 2). The requirements correspond to those that apply in the context of an IPO. In effect, the legislator has maintained the equivalence requirement for primary issuances in order to counteract the risk of a backdoor listing.

3.4.2.2. Secondary issuance

Exchange offers are more likely to involve secondary issuances in the future (as was the case in the past). Secondary issuances are transactions in which the bidder's shares were already admitted to trading on the regulated market prior to the exchange offer (i.e. the bidder is already a listed company). Simplified prospectus law requirements apply to the exemption document in such cases (Article 2 para. 1 (3) of Delegated Regulation 2021/528 in conjunction with Annex 1).

Since a bidder's shares are not required to have been admitted to trading on a regulated market for a minimum period to use an exemption document, issuers can submit an exchange offer using the exemption document immediately after their shares are admitted to trading for the first time. Consequently, the minimum information that an exemption document has to contain (see Annex 1 of Delegated Regulation 2021/528) is also significantly less extensive than the minimum information to be provided in a simplified prospectus for rights issues (Annexes 3 and 12 of Delegated Regulation 2019/980).

3.5. Summary

This overview of key structuring considerations under takeover and prospectus law illustrates the recent changes in the requirements that apply to exchange offers. From a takeover law perspective, the Frankfurt Higher Regional Court has sharpened the definition of liquidity. Because BaFin has apparently applied this decision in its subsequent administrative practice and there are no indications that the national legislator intends to amend the Takeover Act (in particular, by defining "liquidity"), the liquidity requirement will have the effect of making exchange offers less common. This largely counteracts the relief provided under prospectus law and the abandonment of the equivalence requirement on the European level.

A new (national) statutory definition of liquidity would be a welcome development to reconcile these opposing regulatory developments. Otherwise, European initiatives to make exchange offers more attractive by providing relief under prospectus law will be to no avail. Until then, there is a risk that the stringent liquidity requirements will be the deciding factor for or against the submission of an exchange offer, despite all of the relief provided under prospectus law. As a result, exchange offers will only be viable for a very small group of bidders in the large-cap and upper mid-cap segments, even in an environment that is favourable for such transactions.

4 FDI screenings as showstopper?

Dr Tobias Heinrich
White & Case LLP

Dr Tilman Kuhn
White & Case LLP

Foreign direct investment (FDI) reviews have recently become an increasingly relevant factor for acquisitions of (listed and unlisted) companies. In 2022, at least 20 takeovers across the globe effectively failed due to FDI concerns, i.e. they were either formally blocked by an FDI regulator or abandoned by the parties due to the regulators' FDI objections.

The most prominent recent example of a transaction in Germany that failed on FDI grounds is the attempted acquisition of a majority stake in Munich-based wafer manufacturer Siltronic AG by rival Taiwanese chip supplier GlobalWafers by way of a public tender offer. The German Federal Ministry for Economic Affairs and Climate Action (*Bundesministerium für Wirtschaft und Klimaschutz*, BMWK) did not approve the acquisition within 13 months of it having been notified, i.e. prior to the long stop date of January 31, 2022, which was the maximum long stop date under German takeover rules. Therefore, a key closing condition was not met. The BMWK's inability to approve the transaction despite the long review was largely interpreted as an alternative way of blocking the deal (instead of issuing a formal prohibition).

The number of FDI prohibitions or approvals subject to material mitigation requirements in Germany increased significantly last year. Up until the takeover of AIXTRON by a Chinese investor was ultimately blocked back in May 2016, FDI proceedings were considered a mere formality, at least in Germany, outside of the defence industry. By the end of 2019, only two further prohibitions (50Hertz and Leifeld, in both cases attempted acquisitions by Chinese investors) had been issued.

In 2022 alone, five prohibitions, or approvals subject to conditions, of planned investments by non-EU/EFTA investors became public in Germany. GlobalWafers/Siltronic came to light in January 2022. In May 2022, the BMWK prohibited the takeover of ventilator manufacturer Heyer by the Chinese investor Aeonmed, justifying its decision by pointing to the COVID-19 pandemic, in which the government had determined that the availability of critical healthcare products needed to be specifically protected under foreign trade law.

In October 2022, the German government approved the acquisition of a stake in HHLA Container Terminal Tollerort GmbH ("CTT") by the Chinese company CSPL, but only subject to material changes. CTT operates a container terminal in the Port of Hamburg. Press reports suggest that the German Federal Chancellery and several ministries had different opinions on the planned acquisition to begin with. Just before Olaf Scholz's first visit to China as Chancellor, the German government approved the transaction subject to conditions. This allowed CSPL to acquire a stake of only 24.9 percent, instead of the originally planned 35 percent. The BMWK also prohibited CSPL from acquiring atypical options for exerting influence over CTT extending beyond the typical influence that a 24.9 percent shareholder can exert in a quest to ensure that CSPL could not influence strategic matters. Meanwhile, the German Federal Office for Information Security has determined the container terminal to be part of Germany's critical infrastructure, so the BMWK re-assessed whether this has an impact on its clearance, but finally approved the acquisition of a stake of 24.9 percent in May 2023.

In November 2022, the prohibition of the acquisition of Elmos Semiconductor SE ("Elmos") based in Dortmund by the Swedish company Silex Microsystems, a subsidiary of the Chinese Sai Microelectronics, became public. The BMWK explained that the planned acquisition of Elmos, which develops, produces and distributes semiconductors for use in the automotive industry in particular, would pose a threat to public order and security in Germany. In the BMWK's view, there were no alternatives, such as approval of the acquisition subject to conditions or a mitigation agreement, that would be suitable to address these concerns. A second case was kept strictly confidential by the BMWK around the same time. According to press reports, this concerned the proposed takeover of the semiconductor firm ERS Electronic GmbH in Bavaria, which has made a name for itself as a pioneer for thermal wafer testing, by a Chinese investor.

In around 80 percent of the blocked transactions, the bidders originated from China, Hong Kong, or were European subsidiaries of Chinese companies. The more interventionist approach to FDI reviews is because the competent authorities view certain sectors as more sensitive from a national security and industrial policy perspective, and because accordingly, the regime's scope has been expanded and legal framework has been tightened considerably in recent years.

In other countries, too, FDI interventions have become more common (see table 1).

Prohibited deal	Sector	Location of the target company	Location of the buyer	Location of the authority issuing the prohibition notice	Date of prohibition
Faber Industrie/Rosatom	Energy	Italy	Russia	Italy	1 June 2022
Robox/Chinese Efort Intelligent Equipment	Robotics	Italy	China	Italy	1 June 2022
University of Manchester vision sensing technology/ Beijing Infinite Vision Technology Company	Optics	United Kingdom	China	United Kingdom	20 July 2022
Pulsic/Suer Orange HK Holding	Software	United Kingdom	China	United Kingdom	17 August 2022
HiLight/SiLight Semiconductor	Semicon-ductors	United Kingdom	China	United Kingdom	19 December 2022

Tab. 1: Examples of prohibited transactions in 2022 (excluding Germany)

At EU level, EU Regulation 2019/452 establishing a framework for the screening of foreign direct investments into the Union (EU Screening Regulation), which entered into force in October 2020, provides for better coordination of FDI reviews among the 27 EU member states. The amendments to the German Foreign Trade and Payments Act (*Außenwirtschaftsgesetz*, AWG) (1st AWG Amendment) and the German Foreign Trade and Payments Regulation (*Außenwirtschaftsverordnung*, AWV) (15th - 17th AWV Amendments) since 2020 adjusted German investment screening to reflect new EU legal requirements and at the same time strengthened it in areas where, in the view of lawmakers, individual investments by non-EU/EFTA bidders might harbour particular risks in terms of German security concerns. In the United States, the first Presidential Executive Order EO 14083 directed at the *Committee on Foreign Investment in the United States* (CFIUS) defined additional security factors in September 2022 that the Committee must take into account when assessing transactions. Complementing this, the Enforcement and Penalty Guidelines were published in October 2022, tightening up the US regime further.

The main changes in the overall legal framework in Germany, the US and Europe, as well as their effects on transaction practice, are presented below.

4.1. The German FDI regime

In political terms, Germany is still aiming to ensure a liberal investment climate. Nevertheless, the country's FDI regime has become consistently broader and stricter since 2016 to ensure protection of technologies that are considered essential, certain industries and key expertise in the interest of public security and order. Several transactions involving investments in critical infrastructure, telecommunications networks or other technologies were only approved after lengthy screening processes and/or only subject to stringent conditions. The FDI regime's extended scope of protection also focuses on the potential use of key technologies, for example in the semiconductor industry or in military applications, as well as in healthcare.

4.1.1. Overall legal framework

The German FDI rules still distinguish between the sector-specific and the cross-sector review. All investments made by a foreign (i.e. non-German) investor in the sectors listed in section 60 AWV, such as war weapons, transmissions and engines intended for military vehicles, products featuring IT security functions, as well as weapons and armaments, trigger a mandatory filing requirement and are subject to sector-specific screening. Pursuant to the latest AWV amendments, an FDI filing and review is also if the target company's German activities are classified as critical within the meaning of section 55 para. 1 sentence 2 AWV (Cross-sector review) if the investor is a non-EU/EFTA investor.

The reporting threshold for sector-specific screening, i.e. all foreign direct investments into a German target that is active in areas related to "defence", is 10 percent of the voting rights, which will then trigger a mandatory filing. Consequently, this 10 percent threshold also applies to all activities classified as conventional critical infrastructure or otherwise more traditionally viewed as particularly critical in cross-sector screening (section 55a para. 1 nos. 1 to 7 AWV). The reporting threshold for all other activities (more recently) classified as critical, as listed in the AWV, in cross-sector screening is 20 percent of the voting rights. All of these trigger filing requirements if made by non-EU/EFTA investors and feature a standstill obligation until approval (i.e. they must not be consummated), breaches of which can result in sanctions being imposed), meaning that they have to be subject to a condition subsequent. For all other foreign direct investments, the investment threshold above which the BMWK may call in the deal is 25 percent; in such cases, there is no mandatory filing or statutory standstill obligation. The AWV sets out further thresholds for additional notification obligations if stakes corresponding to 20 percent (if the original threshold was 10 percent), 25 percent, 40 percent, 50 percent and 75 percent of the voting rights are exceeded. As soon as the next threshold is reached, an additional notification must be submitted. This would then again involve a standstill obligation and the threat of criminal sanctions if this obligation is not complied with.

The competent authority in Germany is the BMWK, which involves other ministries and authorities depending on the scope of its review. The primary criterion for the BMWK's review is whether the foreign direct investment is expected to have a negative impact on public order or security in the Federal Republic of Germany, another EU member state or in connection with projects and programmes of Union interest (in cases involving defence-related transactions, the criterion is whether the transaction is likely to impair key security interests of the Federal Republic of Germany).

4.1.2. Procedure

All transactions subject to mandatory screening must be filed with the BMWK. In cases involving a takeover of a listed company, notification must be submitted immediately after publication of the decision to make an offer (section 10 WpÜG). All WpÜG offers subject to a notification requirement under German foreign trade law are subject to a standstill obligation (breaches of which will be penalised) subject to the conditions set out above and are provisionally ineffective until the transaction is approved. This must be reflected by a corresponding closing condition in the offer document. In particular, the buyer cannot be allowed to exercise voting rights either directly or indirectly and must not be granted access to certain forms of sensitive data before the transaction has been approved.

Breaches of the statutory standstill obligation or of individual standstill orders issued by the BMWK are subject to penalties under criminal law, including imprisonment of up to five years or fines. Negligent violations are considered administrative offences that may result in fines of up to EUR 500,000.

All BMWK decisions can be challenged before a German court. Judicial proceedings are often not, however, a practical option for the parties involved due to the time or publicity involved, and the government has considerable leeway when it comes to assessing which transactions are likely to be detrimental to public order or security.

4.1.3. Timeline

The review period available to the BMWK is two months for the initial review, at which point a decision is made on whether to initiate the second review phase. A period of four months is provided for the second review phase by law, with this period commencing upon receipt of all the necessary documentation. The BMWK does, however, have a generous margin of discretion when it comes to defining this point in time and, as a result, marking the commencement of the statutory time periods. In particularly complex cases, the BMWK generally has the right to extend the formal review period by a further three months, and by four months in cases involving defence transactions. In addition, the review period for the implementation of the formal review measures is suspended if additional information is requested and for as long as negotiations on a mitigation agreement are under way between the BMWK and the parties involved. As a result, measures like these taken by the BMWK in an ongoing FDI procedure outside of the official review period can have a significant impact on the transaction timeline. The BMWK can also decide in a shorter period than the four months provided for the second review phase as a matter of principle.

Even if the transaction does not trigger any notification requirement, foreign investors often choose to initiate a review process by submitting a voluntary application for a clearance certificate to the BMWK to give them legal certainty. Once the full application has been submitted, the BMWK has two months to decide whether to issue the clearance certificate or initiate a formal review. Once this period is expired, the clearance certificate is deemed to have been granted if no review has been initiated.

4.1.4. The GlobalWafers/Siltronic case

Where an FDI filing is necessary or a review is otherwise expected, granting of approval under foreign trade law by a certain date (the "long stop date") is included in the offer documents as a closing condition for public takeovers. In January 2022, Taiwanese silicon wafer manufacturer GlobalWafers failed in its attempted public takeover of its Munich-based rival Siltronic AG, a case that illustrates the impact of an FDI clearance closing condition in connection with a long stop date for a public takeover. To close the deal, the takeover offer published in December 2020 by a German subsidiary of GlobalWafers stipulated that various conditions had to be met by 31 January 2022. This also included the issuance of a clearance certificate, which had been applied for in December 2020, by the BMWK. With the date of 31 January 2022 for screening by the ministry rapidly approaching and with BaFin having rejected any postponement of the long stop date as an option, GlobalWafers attempted to establish in court through an emergency petition that a BMWK clearance certificate was deemed to have been issued ("Genehmigungsfiktion"), arguing, in technical terms, that the BMWK's deadline extension was invalid and the statutory review time limit had hence been exceeded. With the dismissal of the emergency petition by the competent Berlin administrative court and the appeal filed against it, the takeover failed due to lack of FDI clearance by the specified long stop date. The BMWK said that it was not possible to complete all the screening steps by this date. In particular, the BMWK argued that it had not had sufficient time to examine the Chinese merger control clearance. Upon expiry of the long stop date, however, the regulatory condition of the takeover offer had not been met and, as a result, completion of the offer was barred. According to the publication by the court, failure to meet the condition also triggered a termination fee of EUR 50 million. However, in the court's view, it was to be noted that ultimately, both the long stop date set as a condition of acquisition and the termination fee were voluntary, self-imposed risks on the merits which the bidder had apparently been willing to assume.

4.2. EU Screening Regulation

Because the EU Screening Regulation does not afford the EU the right to screen and decide on foreign direct investments on a standalone basis, FDI reviews and enforcement are still within the sole power of the EU member states. The Regulation serves primarily to harmonise and coordinate what are very different screening mechanisms between EU member states, and to ensure that each country concerned, as well as the EU as a whole is provided with information on, and is involved in, ongoing screening procedures.

4.2.1. Cooperation mechanism

In particular, the Regulation introduced a cooperation mechanism based on which the European Commission can issue non-binding opinions on FDI screening proceedings under way in member states. FDI reviews are still conducted in the member state concerned and based on its national rules. The member states not screening themselves can also opt, alongside the European Commission, to issue opinions to the screening member states. The member states and the European Commission can also issue opinions on a transaction that is not undergoing screening because it is being executed in a member state where there is no FDI review mechanism in place, or where the transaction does not meet the statutory criteria for FDI screening, or because the member state with jurisdiction for screening has decided not to review a particular investment. In the latter case, the member state that could but does

not screen must provide the other member states concerned and/or the European Commission with a minimum level of information on a confidential basis without delay.

The cooperation mechanism can also apply to an investment that has already been completed and is being assessed under a member state's ex post rules, or to an investment that has not undergone screening within 15 months of completion of the investment. Most member states, however, have only passed ex ante FDI regulations, meaning that transactions are only screened before they are completed.

The member states have exclusive responsibility for screening decisions under their domestic FDI mechanism, including to block or clear subject to mitigating conditions. It is, however, impossible to rule out a scenario in which smaller EU member states (in particular) will come under considerable pressure to take the opinions or comments issued by the European Commission or other member states into account in their decisions to a more determinative extent, even if they are not legally obliged to do so.

4.2.2. Requirements for member states

While the EU Screening Regulation does not oblige EU member states to introduce a national FDI screening process, most member states have implemented one in recent years. With the exception of Bulgaria and Cyprus, all EU member states now have foreign trade legislation that provides for an FDI review process or have expressed their intention to introduce one in the near future.

National FDI authorities pursue different approaches. Some FDI authorities have systematically reported every transaction involving non-EU investors as part of the EU cooperation mechanism, while others only do so subject to specific conditions.

4.2.3. European Commission report on FDI screening for 2021

The European Commission published a report on FDI screening in 2021 in September 2022. In 2021, the European Commission had analysed more than 400 foreign direct investments within the European Union to ensure that these investments would not pose any threat to security or public order within the EU. The main findings of the report reveal the following:

- The vast majority of procedures are approved swiftly, both at member state level and under the EU Screening Regulation.
- 86 percent of the FDI transactions reported by the member states were closed by the European Commission within a period of 15 days.
- Less than 3 percent of the transaction procedures were concluded by the European Commission issuing an opinion.
- Germany, France, Italy, Spain and Austria accounted for more than 85 percent of the notifications to the European Commission.

- The top 5 countries of investor origin for the transactions notified are the United States, the United Kingdom, China, the Cayman Islands and Canada. Russia accounted for less than 1.5 percent of the cases screened.
- FDI reviews related to a wide range of sectors. Most of the cases notified, however, were in the manufacturing sector, including defence, aerospace, energy, health and semiconductors, at 44 percent, and in ICT, at 32 percent.

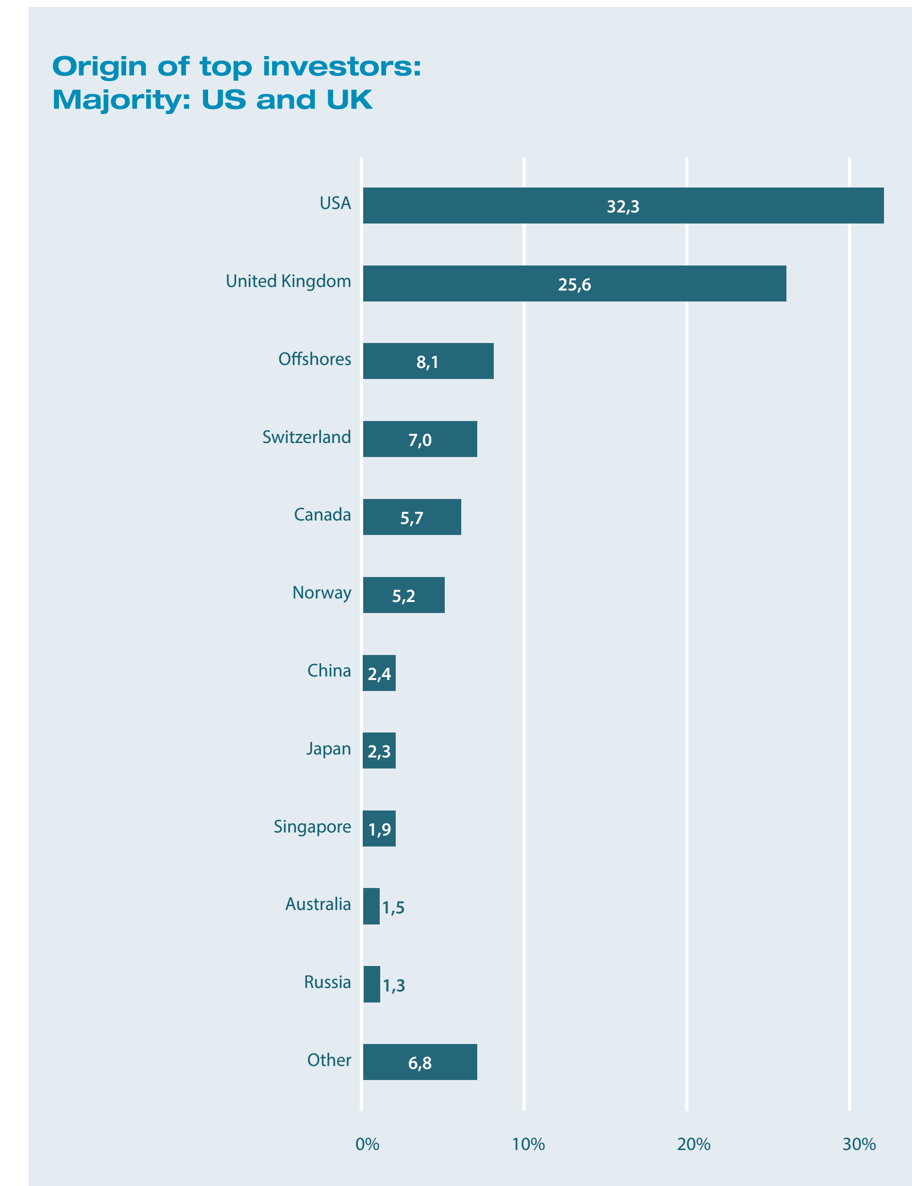


Figure 19: Origin of top investors (more than 10 percent) in the EU

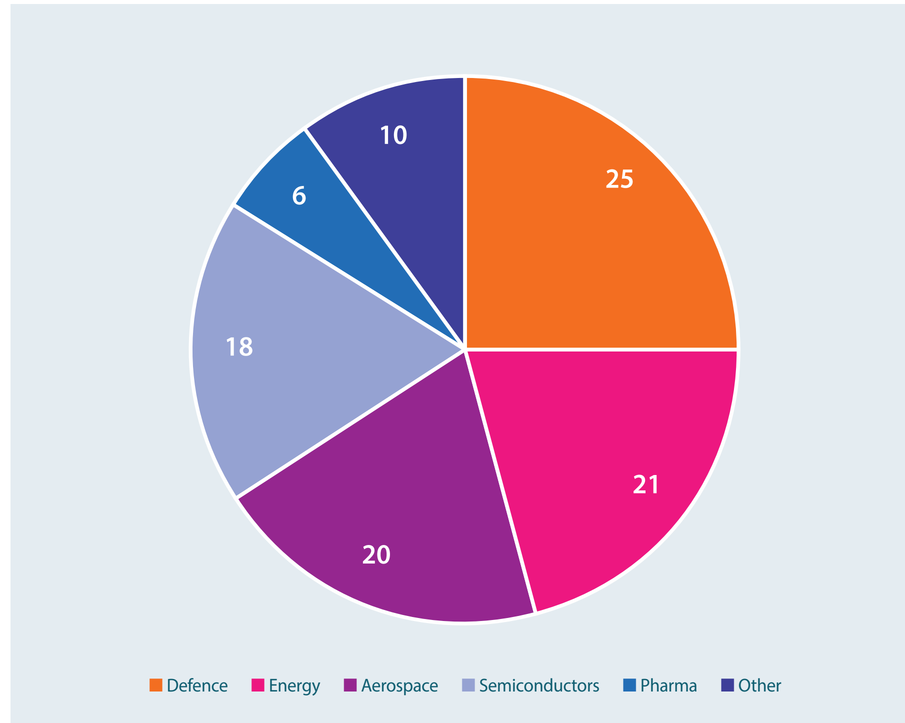


Figure 20: Manufacturing sub-sectors in Phase 2 in 2021 cases

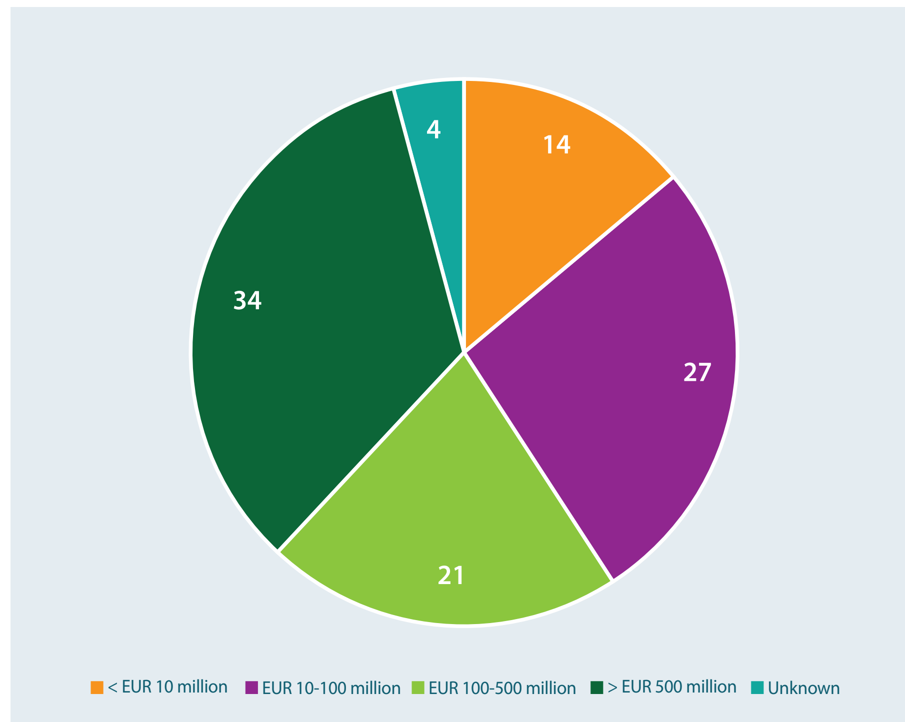


Figure 21: Volume per FDI transaction notified

4.2.4. Timeline

The question as to how long the procedure under the EU Screening Regulation takes depends on a large number of factors. While most transactions will be screened by the European Commission within 15 days in what is known as Phase 1, in-depth screening for the remaining transactions was initiated in Phase 2. This Phase 2 can span a period of several months, partly because member states have to provide the information requested as part of the consultation process. There are no binding requirements or restrictions on how long member states can take to respond. In 2021, member states took between only a few days and 101 days to respond in Phase 2 of the consultation process. Any other provisions governing deadlines set out in the EU Screening Regulation are suspended during this consultation process.

4.3. CFIUS (USA)

The historical development of procedures before the *Committee on Foreign Investment in the United States* (CFIUS) shows that reform efforts have always been linked to an actual or perceived threat to US security interests associated with foreign investment. The latest major reform came in the form of the *Foreign Investment Risk Review Modernization Act* (FIRRMA), passed in August 2018, which entailed considerable reforms to the CFIUS procedure. Investment control laws in the US were then also clarified further and tightened up by Executive Order EO 14083 of 15 September 2022. The five areas of focus are:

- Supply chain resilience
- Impact on United States technological leadership
- Assessment of aggregate investment trends in industries
- Cybersecurity risks
- Sensitive data

The US Department of the Treasury, which serves as the CFIUS chair, takes the lead in each case, supported by a co-lead—the federal agency with the most appropriate expertise to review a particular case. While the five areas identified by the recent EO have also been screened in the past, they are now indisputable codified areas of focus by CFIUS.

The CFIUS Enforcement and Penalty Guidelines were also published on 20 October 2022. These describe, for the first time, how CFIUS identifies, processes and assesses National Security Agreement (NSA) violations and imposes penalties.

A scenario in which outbound investments would also fall under the CFIUS regime in the future cannot be ruled out. The proposed National Critical Capability Defense Act (NCCDA) published in December 2021 provides for an administrative procedure applying to certain outbound activities of US or third-country companies with significant US business (in particular with regard to US subsidiaries of non-US companies). Global investors should keep an eye on these developments – particularly with regard to transactions related to China – when assessing investment control law risks.

4.3.1. Procedure

In the past, formal CFIUS procedures tended to be initiated by a voluntary application, in the vast majority of cases this was submitted jointly by the parties involved (joint voluntary notice). Since FIRRMA, a transaction filing requirement has applied in cases where an investment would result in the direct or indirect acquisition of a substantial interest in a US company related to critical technology, critical infrastructure or sensitive personal data, where the buyer is a foreign person.

FIRRMA has introduced a new procedure for a short-form declaration, generally allowing transactions to be approved in a much shorter period of time. Violations come to the attention of CFIUS in a myriad of ways, including through information provided by the parties themselves (via voluntary disclosures/applications or in response to CFIUS inquiries), in notices or declarations, via monitors and auditors for CFIUS Mitigation Agreements, as a result of CFIUS on-site visits, reports from the general public, other government agencies and publicly available information.

In light of this enhanced monitoring and enforcement environment, it is now more important than ever for parties to carefully consider whether contemplated transactions might trigger a mandatory CFIUS filing as well as for companies operating under mitigation requirements to prioritize compliance. Companies that are subject to conditions, and for which a Mitigation Agreement may therefore be an option, should implement compliance mechanisms, develop a strong and collaborative relationship with CFIUS monitoring agencies and make sure they disclose any violations or suspected violations promptly.

4.3.2. Timeline

For transactions subject to a mandatory notification requirement, the application must be filed with CFIUS at least 30 days before the transaction is completed. The submitted declarations, i.e. the short-form applications, will be examined by CFIUS within a period of 30 days. Based on previous experience of the cases covered by a pilot project starting in 2019, approximately 70 percent of applications were submitted as short-form declarations. CFIUS only required the filing of full application documents in 28 percent of these cases. This means that legal certainty for the transaction concerned was achieved in more than 70 percent of all cases using the short-form declaration procedure.

CFIUS is required to complete its review of a notice within 45 days, a period that can be extended by an additional 45 days if CFIUS considers this necessary to conduct further investigations. CFIUS must respond to a declaration within 30 days, after which CFIUS has the right to request a written notice. If CFIUS identifies national security concerns and the transaction is not terminated voluntarily, CFIUS can impose mitigation measures or refer the transaction to the President of the United States, who can approve or block the transaction within 15 days. In 2016, for example, President Barack Obama blocked the takeover of the German chip equipment maker AIXTRON by the Chinese investor Fujian Grand Chip Investment citing security concerns.

4.3.3. 2021 CFIUS Report

The key role which CFIUS plays in investment control is evident from its activity reports. CFIUS published its most recent Annual Report on 2 August 2022, providing statistics on transactions filed with CFIUS in 2021 and details of measures taken to address national security risks arising from the notified transactions.

- CFIUS reviewed 272 notices and 164 declarations.
- CFIUS cleared 60 percent of the notified transactions – within 45 days in the case of notices and 30 days in the case of declarations.
- Mitigation measures were only taken for 10 percent of the cleared transactions.
- There were no presidential measures in 2021

Year	Number of notices	Number of notices withdrawn during review phase	Number of investigations	Number of notices withdrawn after commencement of investigations	Presidential decisions
2012	114	2	45	20	1
2013	97	3	49	5	0
2014	147	3	52	9	0
2015	143	3	67	10	0
2016	172	6	79	21	1
2017	237	4	172	70	1
2018	229	2	158	64	1
2019	231	0	113	30	1
2020	187	1	88	28	1
2021	272	2	130	72	0
Gesamt	**1829**	**26**	**953**	**329**	**6**

Tab. 2: CFIUS statistics for 2012-2021

4.4. Impact of investment control procedures on transaction practice

The extensive obligations to conduct investment control reviews that apply worldwide have a considerable impact on the selection of the target company, the analysis of the strategic further development options and the structuring and actual implementation of the takeover proceedings, as well as on the design of the transaction documents.

4.4.1. Selection criteria for the target company and bidder

From a bidder's perspective, the possible obligation to conduct an investment control procedure is an extremely important criterion when it comes to selecting a target company. Knowing for sure that a transaction can be executed successfully can be a decisive factor in selecting a target. This is why, in cases involving major M&A projects, it makes sense to conduct a feasibility study when the project is launched to determine how likely the transaction is to be approved not only from an antitrust perspective, but also from an investment control perspective. The product portfolio and geographical coverage are key factors to be taken into account.

From the perspective of the target company, it makes sense to conduct a preventative risk analysis that looks at the impact of relevant investment control rights and the composition of the economic network and the company's shareholders. This can be conducted as a separate feasibility study in order to identify risks to future development and expansion by potential investors early on.

4.4.2. Due diligence

If investment control law intervention cannot be ruled out from the outset, the potential bidder should, in particular, make sure that the material scope and level of detail of its expert investigation into the target company (due diligence) reflects the investment control procedures that may come into play, and use the knowledge derived from this process when preparing the corresponding applications. The due diligence activities conducted by prospective buyers should include the following:

- Reviewing whether notification is mandatory and, if not, reviewing whether voluntary notification to secure the transaction would be a sensible approach
- Security clearance by government authorities
- Geographical scope of economic activities
- Product and service portfolio and (where appropriate already broken down into military and dual-use goods, critical infrastructure and critical technologies) further developments that are already planned, as well as those that are merely possible
- Economic network of the target company, in particular current suppliers, customers and joint venture partners, as well as planned and possible changes to the network

- Utilisation of subsidies, cooperation with state bodies or bodies (such as universities) which themselves receive state or supranational support
- Key staff members and their security clearance as well as the security screening system in general

4.4.3. Reverse Break Fees

In the context of investment control procedures, target companies sometimes require an agreement on financial compensation to be paid by the buyer in the form of what are known as reverse break fees, set out in a business combination agreement that is concluded prior to the transaction, so as to cover the risk of the transaction failing because regulatory approval is not granted, or because one or more regulatory conditions are not met (see *New trends in business combination agreements, delisting agreements, etc.,* page 74). In addition to providing a safeguard against the collapse of the deal, they are also intended inter alia to incentivise buyers to do their utmost to obtain the requisite approval under investment control law.

The considerations regarding permissibility that have to be taken into account in cases involving conventional break fees – in particular with regard to their amount – are precisely not relevant in cases involving reverse break fees, because they do not place undue limits on the corporate bodies of the target company with regard to their management discretion or with regard to capital protection rules.

In order to ensure that a reverse break fee is actually paid, escrow agreements are frequently put in place whereby part or (more usually) all of the fee is deposited in an escrow account for the benefit of the target. Depending on the buyer's home country and the location of the funds, payment of the reverse break fee may itself be subject to capital controls.

The importance of hedging regulatory risks, especially in relation to non-approval by the CFIUS, is shown not least by the steadily maturing market

4.4.4. Offer document

Where notification of the transaction is not mandatory, the decision whether to include regulatory closing conditions relating to successful completion of the investment control procedure in the offer documents is left to the parties' discretion. In practice, however, investment control approval is usually included as a closing condition. The closing condition is met if and when written confirmation has been received from the competent authority. The aim of such a condition is to avoid the consequences of having to unwind the transaction if it is blocked, particularly since those consequences are difficult to estimate. The regulatory condition in the offer document also has to include a long stop date. The length of the time limit will depend to a key extent on a well-informed assessment of how long the investment control procedure will take. The Global Wafers/Siltronic case described above shows that even a period of 13 months can be too short.

4.5. Conclusion

There is an emerging international trend towards more stringent FDI screening in M&A transactions involving foreign bidders, which is reflected in the large number of new FDI regimes and rules. Particularly given the ongoing global political tension, this trend is not expected to reverse over the next few years.

Having to undergo one or more FDI reviews in parallel increases the complexity of the transaction as a whole. Parties to an M&A transaction should give careful consideration to the risk of FDI reviews, which are usually conducted at the start of the due diligence process, and factor screening procedures into the transaction timetable. In view of the potentially significant risks associated with FDI reviews, it may make sense for the parties to initiate talks with the national FDI authorities as early on as possible before a binding agreement is signed and announced. This can help to minimise the risk of FDI reviews proving to be showstoppers.

5 New trends in business combination agreements, delisting agreements, etc.

Investment agreements or business combination agreements (BCAs) are often concluded by bidders and target companies in connection with public takeovers. Such agreements have become a key component of public takeovers and also of any subsequent integration of the target company. They give the bidder and the target company a certain degree of transaction security, which is of decisive importance not least given an increasingly uncertain market environment – only to mention the current geopolitical situation, ongoing supply chain issues following the COVID-19 pandemic, rising interest rates and inflation. As a result, investment agreements and BCAs have become an indispensable component of day-to-day takeover activity, and have by now established themselves as standard market practice. Whereas back in 2018, an investment agreement or BCAs was (only) concluded in around 30 percent of public takeovers, this figure had risen to around 90 percent by 2021. In 2022, agreements like these were concluded in approximately 55 percent of public takeovers.

The last edition of this study, published in 2018, already explored the typical aspects covered by investment agreements and BCAs, as well as the interests of bidders and target companies. Interested readers are therefore referred to the last study for further information in this regard. The information below is based on an evaluation of selected [2] offer documents and statements from the 2018 – 2022 period and focuses on current developments in the content of BCAs, emerging market standards and special features of individual public takeovers. Given the increasing number of delistings in the German takeover market, this section also includes an overview of the key contents of delisting agreements and their implementation.

[2] For each respective year in the 2018 – 2022 period, the three largest takeover offers based on transaction volume have been considered.

Dr Stefan Bressler
White & Case LLP

Dr Thyl Hassler
White & Case LLP

Dr Alexander Kiefner
White & Case LLP

5.1. Current developments, typical content of BCAs and investment agreements

5.1.1. Offer conditions

Takeover bids are typically subject to a large number of conditions (unlike mandatory offers and delisting acquisition offers, where conditions, in principle, cannot be imposed). Offer conditions can be structured in a variety of ways; ultimately, they depend on the factors motivating the parties in the specific case. Commonly, offer conditions relate to a specific minimum acceptance threshold, the achievement of regulatory approvals and a commitment not to implement structural measures under company law or corporate actions.[3] The latter prevents a scenario in which the bidder's stake is diluted, for example due to the use of authorised capital. Material adverse change (MAC) clauses are also becoming increasingly common. These can be structured either as independent business MAC[4] relating to the target company, independent market MAC[5] relating to sector-specific indices or as combined business-market MAC.[6] In 2022 the current geopolitical situation was reflected in an offer condition for the first time: the offer for Deutsche EuroShop AG was subject to the condition that the NATO collective defence clause had not been triggered in Europe upon expiry of the acceptance period. As a general rule, the parties agree on duties of cooperation so that regulatory conditions, in particular, can be met.

[3] See Grammer AG (2018), Stada Arzneimittel AG (2018), Axel Springer SE (2019), Scout 24 AG (2019), Qiagen N.V. (2020), alstria office REIT-AG (2021), Deutsche Euroshop AG (2022), Aareal Bank AG (2022).

[4] See Grammer AG (2018), Siltronic AG (2020), Deutsche Wohnen SE (2021).

[5] See Axel Springer SE (2019), Scout 24 AG (2019), Siltronic AG (2020), Deutsche Wohnen SE (2021), Aareal Bank AG (2022).

[6] See Qiagen N.B. (2020).

5.1.2. Statements by the management and supervisory boards of the target company

One confirmed trend is that parties use corresponding provisions in the investment agreement or the BCA to secure a positive statement by the management and supervisory board of the target company, often subject to a fiduciary out clause. The statements evaluated for the 2018 – 2022 period, for example, were exclusively positive and were issued as joint statements by the management and supervisory board.[7] After conclusion of an investment agreement or BCA separate statements were only issued in two cases in the 2018 – 2022 period.[8]

5.1.3. No shop / no talk

Commitments by the target company going beyond the duty to support the offer, to refrain from looking for a competing offer (*white knight*) during the course of the takeover proceedings (*no shop*) or from entertaining such discussions (*no talk*) can be found in less than half of the offer documents analysed.[9]

5.1.4. Strategic focus / business policy of the target company

Each investment agreement or BCA sets out the bidder's intentions with regard to the strategic focus and business policy of the target company, which are also reflected in the offer document. This commonly includes provisions on the target company's dividend policy,[10] provisions on financial support for the target company provided by the bidder as part of a growth strategy[11] or if refinancing is necessary due to change-of-control clauses triggered by the takeover.[12] Otherwise, the provisions vary considerably on a case-by-case basis.

5.1.5. Safeguarding locations and jobs

It is also common practice to include provisions on safeguarding locations and jobs; these can be found in all investment agreements and BCAs.

[7] RIB Software SE (2020): managing directors and Administrative Board, Hella GmbH & Co. KGaA (2021): personally liable partner and Supervisory Board.

[8] Akasol AG (2021), Osram Licht AG (2019). In another case (Rhön-Klinikum AG (2020)), a separate statement was also issued following the conclusion of a joint venture agreement between the main shareholders.

[9] Axel Springer SE (2019), Qiagen N.V. (2020), Deutsche Wohnen SE (2021), Hella GmbH & Co. KGaA (2021), Aareal Bank AG (2022).

[10] Grammer AG (2018), Siltronic AG (2020), Deutsche Wohnen SE (2021), Deutsche Euroshop AG (2022), Aareal Bank AG (2022).

[11] Stada Arzneimittel AG (2018), Scout 24 AG (2019), Qiagen N.V. (2020), alstria office REIT-AG (2021), Vantage Towers AG (2022), Aareal Bank AG (2022).

[12] Scout 24 AG (2019), Osram Licht AG (2019), Qiagen N.V. (2020), Vantage Towers AG (2022), Aareal Bank AG (2022).

5.1.6. Know-how

Other more common provisions serve to protect research and development (no reduction in or relocation of research and development activities),[13] or to protect trademarks[14] and intellectual property. This trend had already emerged when the last edition of the study was prepared and has been confirmed.

5.1.7. Corporate governance

Provisions on the future composition of the bidder's corporate bodies, such as the appointment of members of the target company's corporate bodies to the bidder's management or supervisory board, are only found in isolated cases.[15] This is particularly the case when the BCA reflects a partnership of equals. By contrast, provisions regarding the future composition of the target company's corporate bodies are very common. These generally focus on the composition of the supervisory board or the appointment of non-executive directors and, in this respect, strive to ensure that the bidder is represented in a manner that is commensurate with its stake after the takeover offer is completed.[16] Requirements of the German Corporate Governance Code regarding independent supervisory board members are explicitly complied with,[17] whereas provisions on a specific gender quota are a rare occurrence.[18] Changes in the management board in connection with the public takeover, however, are generally not covered by the BCA.[19]

5.1.8. Structural measures

Every investment agreement or BCA also contains agreements between the parties regarding structural company law measures aimed at integrating the target company once the takeover is complete. These measures focus on domination and profit and loss transfer agreements, as well as squeeze-outs under stock corporation, transformation or takeover law. Sometimes, the bidder makes a commitment *vis-à-vis* the target company not to implement such measures within a defined period of time.[20] From the bidder's perspective, this helps to increase the acceptance rate, as it sends out the message to the target company's shareholders that a speculation on a higher compensation payment under a domination and profit and loss transfer agreement or a squeeze-out is not worthwhile. In 2019, Bain & Carlyle had also reached an agreement in their offer, which had been secured by an investment agreement with Osram but ultimately failed due to a competing offer made by ams, that they would not waive the minimum acceptance threshold so as to avoid speculation by activist shareholders. By and large, however, agreements on structural measures are limited to mere declarations of intent by the bidder, which are also reflected in the offer document.

[13] Siltronic AG (2020).

[14] Grammer AG (2018), Stada Arzneimittel AG (2018), Axel Springer SE (2019), Osram Licht AG (2019), Deutsche Wohnen SE (2021), Hella GmbH & Co. KGaA (2021), Aareal Bank AG (2022).

[15] Siltronic AG (2020), Deutsche Wohnen SE (2021), Hella GmbH & Co. KGaA (2021).

[16] Stada Arzneimittel AG (2018), Axel Springer SE (2019), Scout 24 AG (2019), Osram Licht AG (2019), Siltronic AG (2020), RIB Software SE (2020), Qiagen N.V. (2020), Deutsche Wohnen SE (2021), Vantage Towers AG (2022), Deutsche Euroshop AG (2022), Aareal Bank AG (2022).

[17] Stada Arzneimittel AG (2018), Scout 24 AG (2019). Osram Licht AG (2019), alstria office REIT-AG (2021), Aareal Bank AG (2022).

[18] Alstria office REIT-AG (2021).

[19] Grammer AG (2018), Axel Springer SE (2018), Scout 24 AG (2019), Osram Licht AG (2019), Siltronic AG (2020), alstria office REIT-AG (2021), Aareal Bank AG (2022).

[20] Siltronic AG (2020), Deutsche Wohnen SE (2021), Hella GmbH & Co. KGaA (2021), alstria office REIT-AG (2021).

5.1.9. Future listing

Provisions on the target company's future listing are also typical. The vast majority of cases either refer specifically to a planned future delisting[21] or at least express this intention on the part of the bidder.[22]

5.1.10. Break Up Fee, Reverse Break Up Fee

Provisions governing break-up fees due by the target company, or reverse break-up fees due by the bidder, in the event that the transaction fails for reasons for which the other party is not responsible, can only be found in individual cases.[23]

5.1.11. Term

Standard terms of two to five years are commonplace.[24] Longer terms, however, are also agreed upon for individual provisions, for example those aimed at safeguarding locations and jobs.[25] By contrast, shorter terms were also increasingly common in 2022.[26] Terms in excess of five years are absolute exceptions.[27]

5.2. Special features of delisting[28] agreements

Since November 2015, shareholders of issuers seeking the delisting from the regulated market have to be offered compensation pursuant to the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz,* WpÜG) as a matter of principle. Section 39 para. 2 of the German Stock Exchange Act (*Börsengesetz*, BörsG) sets out the provisions governing voluntary delisting. The delisting is implemented by the stock exchange admissions office upon application by the issuer. This also applies to issuers that have their registered office abroad but are listed on a German stock exchange in the regulated market (section 39 para. 4 BörsG), which means that compensation also has to be offered to outside shareholders of foreign issuers if these issuers are seeking delisting from the regulated market in Germany.

Pursuant to section 39 para. 2 sentence 3 BörsG, delistings are only permissible if, at the time the application is submitted, an offer document for the acquisition of all of the securities that are subject of the application is published (no. 1)[29] or if the securities continue

[21] Axel Springer SE (2019), Osram Licht AG (2019), Qiagen N.V. (2020).

[22] Stada Arzneimittel AG (2018), Siltronic AG (2020), RIB Software SE (2020), Hella GmbH & Co. KGaA (2021), alstria office REIT-AG (2021), Vantage Towers AG (2022), Aareal Bank AG (2022).

[23] Siltronic AG (2020), Qiagen N.V. (2021).

[24] Stada Arzneimittel AG (2018), Scout 24 AG (2019), Osram Licht AG (2019), Siltronic AG (2020), RIB Software SE (2020), Deutsche Wohnen SE (2021), Hella GmbH & Co. KGaA (2021), alstria office REIT-AG (2021), Aareal Bank AG (2022).

[25] Stada Arzneimittel AG (2018), Osram Licht AG (2019), Hella GmbH & Co. KGaA, Deutsche EuroShop AG (2022).

[26] Vantage Towers AG (2022), Deutsche EuroShop AG (2022).

[27] Grammer AG (2018), Axel Springer SE (2019).

[28] For the purposes of this study, the term "delisting" refers to the (voluntary) revocation by an issuer of shares' admission to trading on a regulated market. Once the shares have been delisted – provided that there is no squeeze-out – many issuers are included in OTC trading at the instigation of other market participants; this means that the shares can still be traded.

[29] The offer is then to be described as a compensation offer under the BörsG.

to be admitted to trading on an organised market of another domestic stock exchange or foreign stock exchange within the EU or EEA, provided that the requirements for delisting on this market match the German regulations (no. 2 lit. b). The issuer's management board is obliged to take any delisting decision only with due consideration of the interests of all shareholders in the company concerned. The legislator is of the opinion that the submission of the aforementioned acquisition offer constitutes sufficient protection for (minority) shareholders. There is no need for a resolution to be passed by the issuer's general meeting.

In practice, delisting offers are made either by a major shareholder (often with the (long-term) objective of carrying out a subsequent squeeze-out), a bidder or, in individual cases, by the company itself.[30] A takeover or mandatory offer can also be structured as a delisting offer at the same time.[31] Although a compensation offer has to be made to the outside shareholders as part of a delisting since the BörsG amendment, delistings are currently en vogue and account for – either as pure delisting offers or in combination with takeover or mandatory offers – a significant share of all offers. In 2021 and 2022, for example, around half of all offers were delisting offers (partly combined with a takeover or mandatory offer).

Due to the special features of the delisting process, in which, while the bidder has to make the delisting offer while the company's management board submits the application to the stock exchange and can only do so if there actually is a delisting offer, the bidder and the company rely on mutual cooperation if they want to carry out the delisting. In practice, concluding a delisting agreement setting out these mutual obligations has become common practice in this respect. The principles of takeover law related investment agreements can generally be applied to delisting agreements, although there are some special features and the starting position for a delisting is different to that for conventional takeover proceedings.

5.2.1. Interests of the bidder

As a general rule, a bidder will only make a delisting offer to shareholders if it is sufficiently certain, with regard to the transaction, that the company will cooperate with the bidder and will actually submit the delisting application. The cooperation obligations that have to be met in this regard and the planned timeline for the delisting process are set out in the delisting agreement. Alternatively, once a domination agreement has been concluded with the company, the bidder can issue an instruction that the delisting application be submitted.[32] The decision to make the delisting offer typically coincides with the conclusion of the delisting agreement and has to be published in accordance with sections 10 para. 1 sentence 1 / 35 para. 1 sentence 1 WpÜG.

5.2.2. Interests of the company

Concluding delisting agreements is generally permissible under the German Stock Corporation Act (German Stock Corporation Act, AktG). They essentially set out obligations incumbent upon the management board to submit the delisting application and to support the

[30] Delisting offer made by Rocket Internet SE to its shareholders on 30 September 2020 and by a.a.a aktiengesellschaft allgemeine anlageverwaltung to its shareholders on 18 November 2022.

[31] See, *inter alia*, ERWE Immobilien AG (2022), Geratherm Medical AG (2022), SMT Scharf AG (2021), DEAG Deutsche Entertainment AG (2021), Godewind Immobilien AG (2020), Westgrund AG (2020).

[32] See Easy Software AG (2020).

bidder's delisting offer by issuing a positive reasoned statement by the company's corporate bodies (section 27 WpÜG). The company's management board can also make support of the delisting offer subject to the fulfilment of certain conditions, e.g., a specific offer price, commitments regarding the company's future business activities, employment conditions or specific financing commitments.

5.3. Typical content of delisting agreements

5.3.1. Obligations incumbent upon the parties

The focus for the company is on the obligation to submit the delisting application and support the offer, e.g., in the form of a positive statement issued by the management and supervisory board (see above). Delisting agreements also typically include the company's obligation not to list (any further) shares or other securities on a regulated market and to take action to also arrange for delisting from the OTC or another MTF/OTF as defined by the Market Abuse Regulation to the extent the company has initiated their inclusion. If members of corporate bodies hold shares in the issuer, commitments to tender these shares in the delisting offer are also often included in a delisting agreement.[33] From the bidder's perspective, the main obligations naturally include the execution of the offer subject to specific conditions, such as payment of a defined minimum price, commitments regarding the company's business activities or employees, employment terms, corporate body composition or future dividend policy.

5.3.2. Fiduciary out

Delisting agreements and the associated support provided by the company's management and supervisory board, are also subject to compliance with the duties of the company's corporate bodies, in particular the general duties of care and loyalty ("fiduciary out") and the assessment of the offer document. In this respect, the principles familiar from takeover law related BCAs apply, namely that the offer is only supported to the extent that the duties incumbent upon the management or supervisory board under the AktG do not require different action on the part of these bodies.

5.3.3. Consideration

Although some of the principles that are familiar from conventional takeover/acquisition offer transactions also apply to delistings, there are a number of major differences with delisting offers, particularly with regard to consideration.

Section 31 WpÜG applies accordingly to delisting offers, subject to the proviso that the consideration must consist of a cash payment in euros. This means that, unlike with takeover or acquisition offers, (liquid) shares cannot be offered as consideration. In addition, the cash consideration (subject to earlier acquisitions) has to correspond at the very least to the weighted average domestic stock exchange price of the securities in the last six months

[33] See Constantin Media AG (2019), HolidayCheck Group AG (2021), Hornbach Baumarkt AG (2022).

(as opposed to only three months for takeover offers) prior to publication pursuant to section 10 para. 1 sentence 1 or section 35 para. 1 sentence 1 WpÜG.[34] If, however, the company has violated *ad hoc* obligations or the prohibition of market manipulation during this period, the bidder is obliged to pay the difference between the consideration set out in the offer document and the consideration corresponding to the value calculated on the basis of a company valuation of the issuer (section 39 para. 3 sentence 3 BörsG). Consequently, bidders should consider also requiring the company to provide assurance in the delisting agreement that it will comply with the obligations set out in the Market Abuse Regulation. However, there may also be special cases, other than the aforementioned legal violations, in which a company valuation is required. In the case of Deutsche Wohnen's delisting offer for GSW in 2022, both a voluntary takeover offer had previously been published and a domination agreement had been concluded, meaning that a company valuation was performed because no six-month average price could be ascertained.

The issuer's corporate bodies have, for the most part, also obtained a fairness opinion to check the adequacy of the consideration in delisting offers.[35]

5.3.4. Conditions

Section 39 para. 3 sentence 1 BörsG states that delisting acquisition offers cannot be subject to conditions. According to the explanatory memorandum to this Act, sections 18 and 25 WpÜG are explicitly not applicable. This means that the regulations governing delisting offers are more stringent than for takeover offers, but also more stringent than for mandatory offers, as the latter, according to unanimous practice, can be subject to the condition of granting of regulatory approvals. There is some controversy amongst scholars whether the ban on the formulation of conditions in delisting offers also applies in cases involving the fulfilment of regulatory conditions, or whether this regulatory approval already has to have been obtained before the offer. In practice, delisting offer documents do not provide for any (regulatory) closing conditions; any merger control approval is obtained in advance.[36]

5.3.5. Term

Delisting agreements typically have shorter terms than BCAs or investment agreements, with standard practice being terms of up to two years. This is because delisting agreements are designed to ensure cooperation between the bidder and the company with a view to a specific event – the implementation of the delisting – whereas in an investment agreement or BCA, the target company is aiming to safeguard its medium and long-term interests.

[34] In cases involving combined takeover bids/mandatory offers and delisting offers, the consideration must correspond, at the very least, to the stock exchange price over the last 6 months, as well as the last 3 months prior to the decision to make the offer / obtain control.

[35] See Constantin Media AG (2019), HolidayCheck Group AG (2021), Hornbach Baumarkt AG (2022), but not Axel Springer SE (2020), GSW Immobilien AG (2022).

[36] For example, STS Group AG (2021), Centrotec SE (2020), Godewind Immobilien AG (2020), Westgrund AG (2020).

5.3.6. Ensuring financing

The principle of ensuring financing also applies to delisting offers. This means that, before the delisting offer document is published, the bidder has to take the necessary measures to finance the offer and ensure that all financial resources required to complete the delisting offer are available in a timely manner (section 13 para. 1 sentence 1 WpÜG). The financing confirmation required pursuant to section 13 para. 1 sentence 2 WpÜG has to be enclosed with the delisting offer document.

5.3.7. Management board duties in the event of delisting

The submission of the delisting application is an entrepreneurial decision made by the management board to which the business judgement rule applies. The question as to whether the supervisory board's consent is required depends on whether a right to reserve approval is provided for, *e.g.*, in the issuer's articles. The management board has to base the delisting decision on the company's interests and weigh up the advantages and disadvantages of listing (also for outside shareholders). Advantages of listing on the stock exchange include, for example, increased availability of financial resources via the capital market, access to (institutional) investor groups, as well as possible reputation advantages associated with the listing. The disadvantages of listing include more extensive reporting obligations and the associated time and resources required for capital market compliance, as well as the costs associated with the listing. Due to the links between the delisting agreement, the delisting offer and the submission of the delisting application, the management board's decision regarding the delisting has to be made and documented before/when the delisting agreement is concluded.

5.4. Conclusion

The findings of the last edition of this study with regard to investment agreements and business combination agreements have been confirmed. They have become integral components of day-to-day takeover activity and key instruments for boosting transaction security and determining future cooperation between the parties. The trend towards concluding these agreements in connection with public takeovers, which had already started to emerge a few years ago, is set to continue. With this in mind, and particularly in times dominated by an uncertain market environment, bidders and target companies are advised to familiarise themselves with the market standards and to explore the various contractual arrangements available in individual cases early on.

Given the trend that has emerged, and indeed is expected to continue, towards further delistings, the conclusion of delisting agreements to provide transaction security for both parties will continue to become more common. From the perspective of the target company's corporate bodies, particular attention has to be paid to the entrepreneurial decision regarding the delisting, which has to have been made before the delisting agreement is concluded. From the bidder's perspective, care should be taken to ensure a sufficient level of transaction security, as well as to secure the cooperation of the target company in the context of the delisting as extensively as possible.

6 Financing public takeover offers with debt

Andreas Lischka
White & Case LLP

In the case of public takeover offers, financing for the purchase price must be secured by the bidder before publishing the offer document. The following article examines the legal requirements applying to the financing of an offer under the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz*, WpÜG) with debt.

6.1. Legal requirements for financing public takeovers in Germany

Before publishing a takeover offer where the consideration is to be paid at least partly in cash the bidder must submit a cash confirmation that complies with section 13 para. 1 WpÜG. The cash confirmation must be provided by an investment services company independent of the bidder. To this end a debt financing agreement that complies with takeover law requirements has to be agreed before the commitment letter is issued, except if the bidder is able and willing to pay the maximum amount of cash consideration from already available cash reserves. Additionally, takeover financing is required to be described in the offer document published by the bidder.

The cash confirmation must not be subject to any conditions. It will only be subject – indirectly – to the conditions of the takeover offer. These are usually few in number. Therefore, the investment services company will be bound by its commitment letter until the offer completes. It will consequently require a high degree of certainty with regard to the takeover financing (known as "certainty of funds"). This makes it crucial for the conditions precedent set out in the takeover financing agreement to be very limited and to be within the bidder's control. In addition, the availability period and the conditions precedent must be aligned with the steps envisaged for the offer so that the committed financing is actually available when the offer consideration is due.

6.2. Key differences from financing private transactions

What sets the financing of public takeovers apart from that of private acquisitions is the acquirer's lack of access, at least initially, to the target company's own financial resources. Due to restrictions under the German Stock Corporation Act (*Aktiengesetz*, AktG), a target company may not provide financial assistance for the acquisition of its own shares. Since German stock corporations (*Aktiengesellschaften*) are subject to very strict equity protection rules and can therefore only provide security for the liabilities of their majority shareholders in exceptional circumstances, even providing financing for the takeover at a later stage appears difficult. All standard structures require, among other steps, the approval of the target company's general meeting with a qualified majority. This makes securing and refinancing public takeovers far more time-consuming and complex than private transactions.

Another key difference from other types of financing is that, even after a successful takeover, the bidder does not have unrestricted control over the target company – at least during a transitional period. Under the German Stock Corporation Act the target company's management board remains solely responsible for managing the company, even if the bidder has acquired the majority of the registered share capital. The right to issue instructions to the target company's management board can only be obtained through a domination agreement with the target company or a squeeze-out that includes converting the target company into a German private limited company (*Gesellschaft mit beschränkter Haftung*, GmbH). Again, all these measures require, among other things, the approval of the target company's general meeting with a qualified majority. Implementing the measures is time-consuming, and the details and tax consequences can often only be worked out after the takeover has been completed. Therefore, takeover financings often include obligations regarding conduct that differ from those in private transactions.

Lastly, takeover financings often provide for certain covenants and thresholds to be adjusted after the takeover has been successfully completed, if (after consulting the target company's management) this proves necessary. The reason is that, in a public takeover, it is much more difficult for the bidder and its lenders to obtain private information about developments in the target company or its group companies. This is because the bidder usually has only limited access to the target company's staff before announcing its takeover offer. In addition, any provision of information must comply with the requirements of the Market

Abuse Regulation (MAR) regarding ad hoc publicity and insider dealing. It is therefore more difficult, when concluding the takeover financing, to tailor rules that will also affect the target company than it would be in a private transaction.

6.3. Preparing for the cash confirmation and the takeover financing

6.3.1. Structuring the financing

Usually, bidders approach one or more potential lenders at an early stage of structuring public takeovers, if they intend to pay the takeover consideration at least partly in cash because they cannot, or do not intend to, pay it entirely from already available cash reserves. They will generally first approach large investment banks that can provide both the cash confirmation and the takeover financing on their own. However, especially in the case of takeover offers by private equity investors, approaches to alternative lenders known as "debt funds" are becoming increasingly common. If the takeover financing is to be provided by a debt fund, the bidder will ask a separate investment services company to provide the cash confirmation required by section 13 WpÜG in reliance on the takeover financing provided by the debt fund.

6.3.2. Confidentiality and multi-tracks (known as "trees")

The preparation of public takeovers is subject to strict confidentiality requirements. A leak of information can quickly wreck a transaction. In addition, the MAR requirements regarding ad hoc publicity and insider dealing must be adhered to as the targets are listed companies. Therefore, in contrast to private transactions, bidders often approach only a small number of banks or debt funds as potential lenders – or even just one. Strategic investors in particular often approach a single bank with which they already have a good relationship, not only to advise them from an M&A perspective but also to provide the cash confirmation and the takeover financing behind it. Private equity investors, on the other hand, tend increasingly to approach one or more debt funds with which they already have relationships. Due to the strict confidentiality requirements, lenders – once engaged – usually only act for one bidder in public takeovers. Unlike in private transactions, it is unusual for the same lender to provide different bidders (using Chinese walls) with support in connection with their public (and in this case competing) offers for the same target company. Internally as well, lenders usually try to involve as few people as possible before the offer is announced. For this reason, lenders are also usually subject to strict confidentiality requirements.

6.3.3. Negotiation of the term sheet and documentation before the offer is announced

The first step is to negotiate a term sheet containing the key provisions of the takeover financing. This will specify, among other things, the maximum nominal amount of the takeover financing, the interest rate, the term and the minimum ratio of debt to equity (i.e. the leverage).

Ideally, the loan agreement will be negotiated and concluded on the basis of the term sheet before the bidder makes its announcement pursuant to section 10 WpÜG. However, there is often insufficient time to finalise the loan agreement before the announcement has to be made. In such cases, before the bidder makes its announcement pursuant to section 10 WpÜG, the lender will issue a commitment letter in which it irrevocably undertakes to provide takeover financing on the basis of the conditions that were agreed in the term sheet. The lender will only issue this commitment letter to the bidder (or its acquisition vehicle), and the commitment letter should not be confused with the cash confirmation that an independent investment services company must provide to the shareholders pursuant to section 13 WpÜG (see section 6.4 below regarding the cash confirmation). Even – or perhaps especially – in the case of a mere commitment letter, it is crucial that it confirms the "certainty of funds". Accordingly, the commitment letter must be structured in such a way that the lender's obligation to execute the loan agreement and provide the takeover financing depends only on conditions that are within the bidder's control. The intention behind this is to give the bidder – and the issuer of the cash confirmation – sufficient certainty that a loan agreement that meets the requirements will be executed before the end of the offer period. Particular care should be taken to ensure that the commitment letter is not subject to internal approvals on the lender's side or to conditions that are outside the bidder's control, such as Material Adverse Change (MAC) clauses not being triggered or the accuracy of representations and warranties.

6.4. Issuance of the cash confirmation pursuant to the WpÜG

In the case of a cash offer, the bidder must provide a cash confirmation before publishing its offer document. The cash confirmation must be attached to the offer document and published together with it.

The cash confirmation must be issued by an investment services company independent of the bidder. In this context, 'independent' means that there is no connection under German company law between the bidder and the issuer of the cash confirmation. The requirement for independent review and confirmation is intended to prevent the publication of dubious or inadequately financed offers.

The investment services company must confirm in its cash confirmation that the bidder has taken the necessary measures to ensure that the funds required to perform its offer in full will be available when it is required to make the cash payment (see section 13 para. 1 WpÜG). The German Federal Financial Supervisory Authority (BaFin) will not take any steps to verify this itself but will instead rely on the cash confirmation. Where the measures taken by the bidder are insufficient to ensure the financing of its offer and where the funds required to pay the consideration are thus unavailable, shareholders who accepted the offer will be entitled to compensation for damages from the investment services company that issued the cash confirmation. The investment services company will only avoid liability if it can prove that it was unaware of the inaccuracy or incompleteness of the information in the cash confirmation about the bidder securing the funds required to make the cash payment and that its lack of awareness was not due to gross negligence on its part.

Before issuing the cash confirmation, the investment services company will therefore generally check whether the bidder has actually taken the necessary measures to secure the funds required to finance its offer. For this purpose, staff and lawyers not already involved in the takeover financing itself will typically check the bidder's financial status, the documentation for the takeover financing, and the lender's solvency. Their review will focus in particular on the certainty of funds. For the issuer of the cash confirmation, it is also crucial that the conditions precedent align with the intended steps in the takeover and with the offer conditions provided for in the offer document, and that all outstanding conditions are within the bidder's control. For this reason, the issuer of the cash confirmation, and therefore also the bidder, will usually insist that the documentation for the takeover financing be completed and that any necessary conditions precedent have been satisfied, so far as possible, by the time the cash confirmation is issued.

6.5. Loan agreement

For the above reasons, the loan agreement underlying the takeover financing should ideally be executed before the cash confirmation is issued and the offer document is published. However, if – as is often the case – there is not enough time to achieve this, a commitment letter will be signed initially, and the loan agreement will then be executed in the period between the publication of the offer document and the expiry of the offer period.

The detailed terms of the loan agreement will depend above all on the bidder's solvency and potential plans to refinance the takeover financing. Usually, the loan agreement will be governed by German or English law, depending on the size of the transaction and any plans to syndicate the loan subsequently. There are no statutory requirements in this respect.

The loan agreement will specify not only the financial terms of the acquisition financing (including the maximum nominal amount, the interest rate and the maximum term), but also the conditions precedent and the availability period. Moreover, the loan agreement will also contain a number of covenants and other obligations regarding conduct that require a number of special features of public takeovers to be observed.

6.5.1. Conditions precedent – certain funds

In order to protect the public and existing shareholders from inadequately financed public takeover offers, the WpÜG – as already explained – sets a high standard for the certainty of funds. The immediate reference here is to the cash confirmation. However, the requirement for certainty of funds also affects the actual takeover financing indirectly. The loan agreement therefore usually contains a certainty of funds concept. This concept only permits conditions precedent that are within the bidder's control. The occurrence of a financial or legal adverse change at the target company or the market in general will not usually entitle the lender to refuse to disburse the takeover funds. The only exception is for conditions that also feature in the offer document.

6.5.2. Availability period

For lenders, it is crucial for their disbursement obligation to be limited in time, as it represents a risk that they must mitigate as much as possible – and must reserve against with their own funds. On the other hand, the financing must be guaranteed for the entire duration of the offer, which cannot be predicted with absolute certainty from the outset. The offer period may, for example, be extended by amendments to the offer, the convening of an extraordinary general meeting of the target company, competing offers or a prolonged merger control procedure. This may well extend the offer period – and therefore the necessary drawdown period – to as long as 12 months. This often appears challenging for lenders. Due to these conflicting interests, availability periods are often heavily negotiated. Since most of the reasons for delay are outside the bidder's control, lenders usually accept that the period during which the acquisition financing can be drawn down can be as long as nine to 12 months.

6.5.3. Compulsory unscheduled repayments

If the takeover financing is only to be made available for a short term of 12 to 36 months, i.e. for a transitional period, the loan agreement will usually include provisions as to when and to what extent the bidder must repay the takeover financing early if it receives funds from another financing, a bond issue, a capital increase or a distribution from the target company.

6.5.4. Security

Lenders will usually provide takeover financing on an unsecured basis to strategic investors that have investment grade ratings and can prove that their ratings will remain unchanged after acquiring the target companies and raising the takeover funds.

In cases involving other types of investors, lenders will usually require them to provide security. The initial security package will usually consist of pledges on the shares in the target company that the bidder acquires and on the bidder's bank and custody accounts. The bidder can provide this security package before drawing down the takeover financing. If – as is often the case in takeovers by private equity funds – the bidder is a special purpose vehicle, it will be key for the lenders to know when and under what conditions they can expect to obtain security for the target company's assets and earnings.

It is very difficult, if not impossible, for lenders to take security from this source at the beginning of a takeover. This is because a German *Aktiengesellschaft* is not allowed to use its own funds to help third parties acquire its shares (see section 71a AktG) nor to directly or indirectly reimburse shareholders for their contributions (see section 57 AktG). These restrictions prevent a target company from providing any part of the financing and prevent it and its subsidiaries from providing guarantees or security at the beginning of a takeover. The law does allow these restrictions to be lifted, but only if an inter-company agreement (e.g. a domination and profit transfer agreement) is concluded between the bidder and the target company or as a result of a squeeze-out under the German Transformation Act (*Umwandlungsgesetz*, UmwG) or the AktG. However, the conclusion of an inter-company agreement requires approval by the general meeting of the target company in the form of a resolution adopted by at least 75 percent of the votes cast at the meeting. A quorum of 90 percent is required for a squeeze-out under the UmwG, and a quorum of 95 percent is required for a

squeeze-out under the AktG. For this reason, the loan agreement often requires the bidder to include a minimum acceptance level in its offer document and, if certain thresholds are reached, to take all necessary steps to conclude an inter-company agreement or implement a squeeze-out within a certain period of time. Recently, however, bidders have increasingly resisted hard obligations of this sort because they increase their risk of defaulting under their loan agreements, and opportunistic investors could take advantage of this to put pressure on the bidders following takeovers (see *Some suggestions from the advisory practice for amending the WpÜG*, page 100).

6.5.5. Obligations regarding conduct

All loan agreements contain a number of covenants and other requirements regarding the conduct of the bidder and – to the extent that the bidder has any relevant influence – the conduct of the target company and its group companies. Since the bidder must comply with these obligations regarding conduct during the entire term of the loan, they must cover a great variety of contingencies and financial targets. The detailed terms will depend above all on the bidder's solvency, the structure of the takeover and the maximum term of the takeover financing.

It should be noted with regard to the target company that, even after a successful takeover, the bidder will not have unrestricted control over the company – at least during a transitional period. This is because the target company's management board remains solely responsible for managing the company, even if the bidder has acquired the majority of the registered share capital. The bidder will only gain the right to issue instructions to the target company's management board if and when it enters into a domination agreement with the target company or implements a squeeze-out of the minority shareholders that includes converting the target company into a *GmbH*. All of these measures will require, as already mentioned, the approval of the target company's general meeting with a qualified majority. Implementing these measures will take several months at least – and sometimes over a year. Additionally, compensation payments to the minority shareholders will be required, and the loan agreement will generally include provisions on the financing of these payments for a specified availability period. The loan agreement should address all of these circumstances as well as the resulting uncertainties.

The questions of whether the bidder is to be obliged, following a successful takeover, to take specific measures to increase its control over the target company within a certain period of time is often the subject of extensive negotiations before the takeover financing is concluded. This is because such obligations may prompt opportunistic investors to acquire a blocking minority in the target company and use it to exert pressure on the bidder. This will result in a tension between the lender's wish to gain sound collateral to secure the takeover financing and the risk that such obligations could expose the bidder to increased pressure and that could be exploited by investors to force the bidder to make further payments or other concessions. There is no standard solution to this tension, and the negotiations on this issue will very much depend on the specific circumstances of each transaction.

7 Cash confirmations – practical aspects

Dr Matthias Kiesewetter
White & Case LLP

Dr Stefan Bressler
White & Case LLP

7.1. General overview

Prior to the publication of a takeover offer, the bidder shall have the necessary arrangements in place to ensure that it has at its disposal the necessary resources for the complete fulfilment of the offer at the time when the claim for consideration falls due. With regard to total funding requirements and sources, these measures need to be summarized in general terms in the offer document. The primary obligation to have available sufficient cash to satisfy all offers in case of a full acceptance of the offer in accordance with the offer and the German Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz – WpÜG*) solely rests with the bidder and the offer must not be subject to any financing condition.

The offer document needs to include a confirmation by a European financial services enterprise ("**Cash Confirmation Bank**") that the bidder has the necessary arrangements in place to ensure that it has at its disposal the necessary resources to perform the offer in full at the time at which the claim for cash payment falls due ("**Cash Confirmation**"). Deviating from the scenario of a squeeze-out under the German Stock Corporation Act (*Aktiengesetz*) or under the German Transformation Act (*Umwandlungsgesetz*), the Cash Confirmation in accordance with the German Takeover Act is not a guarantee.

The German Federal Financial Supervisory Authority ("**BaFin**") requires the Cash Confirmation to be issued in a standard form repeating the relevant text of Section 13 of the German Takeover Act, i.e. additions or explanations in the Cash Confirmation that would limit the scope of the Cash Confirmation are not permissible.

7.2. Potential liability of the cash confirmation bank

7.2.1. Required standard of care

For the purpose of issuing the Cash Confirmation and the avoidance of any liability under the German Takeover Act, the Cash Confirmation Bank needs to demonstrate that it has acted without gross negligence, but responsibly and has taken all reasonable steps to assure itself that the bidder has sufficient resources available to satisfy full acceptance of the takeover offer in accordance with its terms when due.

Whether or not the Cash Confirmation is correct, or the bank has at least acted responsibly and taken all reasonable steps, would ultimately be a question of fact for the competent court to decide on. However, since the German Takeover Act entered into effect in 2002 and insofar as we are aware, there have been no court decisions dealing with the liability of a Cash Confirmation Bank for an incorrect Cash Confirmation.

The issuance of the Cash Confirmation inevitably requires a subjective commercial judgement, which can only be made by the Cash Confirmation Bank. In the first instance, any aspects of the transaction itself such as size and solvency of the bidder, a funding transaction entered into in the course of the takeover offer and the expected time until settlement are taken into account. However, the Cash Confirmation Bank's judgement may also take into account matters, which are not deal-specific at all, such as the Cash Confirmation Bank's knowledge of its client and affairs.

To get comfortable, the Cash Confirmation Bank will typically take the following into account:

- In a first step, the Cash Confirmation Bank would look at the **maximum financing requirement**, assuming 100 percent acceptance of the offer and taking into account the number of (i) all outstanding target shares (i.e. shares not already held directly by the bidder) and (ii) any new shares of the target (e.g. from

convertible bonds) that may be issued until the expiry of the additional acceptance period as well as all transaction costs which the bidder will incur for the preparation and implementation of the offer and in connection therewith. Subject to certain requirements, arrangements with shareholders to not accept the takeover offer (no-tender agreements) may be considered for the determination of the otherwise required financing amount.

- In a second step, the Cash Confirmation Bank would look at the envisaged **financing sources** (i.e. debt and/or equity) and measures put in place by the bidder. Depending on the envisaged arrangement, the Cash Confirmation Bank will request corresponding information, warranties in the cash confirmation agreement and underlying documents from the bidder (due diligence request list).
- **Time frame:** The Cash Confirmation Bank further needs to get comfortable that the funds are available when due, i.e. at the anticipated settlement date. To the extent that this is within the control of the bidder, the cash confirmation agreement concluded with the bidder typically reflects this via appropriate covenants in the cash confirmation agreement (e.g. regarding term of regular acceptance period and measures that might lead to its extension such as amendment of the offer terms). To the extent that certain events outside the control of the bidder would cause an extension of the acceptance period and delay settlement, the Cash Confirmation Bank takes a reasonably conservative view on the timeline and builds in some "buffer" in terms of availability (i.e. assumed time-frame in case of a competing offer).

7.2.2. Scope of liability

In case the Cash Confirmation Bank is in breach of its obligations under Section 13 of the German Takeover Act, it would be liable for losses incurred by the shareholders who have tendered their shares into the offer resulting from the non-fulfillment or incomplete fulfillment.

The claim of the respective accepting shareholder against the Cash Confirmation Bank corresponds to the claim of the shareholder against the bidder that is not able to pay the offer consideration at settlement. Thus, shareholders may (i) withdraw from the acceptance of the offer (i.e. not transfer their shares) and claim the difference between the value of their shares and the consideration offered or (ii) transfer their shares and claim damages in the full amount of the consideration.

7.3. Potential financing measures

7.3.1. Debt

With regard to the debt financing, the Cash Confirmation Bank has to verify that the relevant agreements are effective and that no termination options have been agreed which conflict with the bidder's financing responsibility under the offer. In practice, the lender often also assumes the role of the Cash Confirmation Bank, allowing on the one hand a seamless procedure while on the other hand requiring the Cash Confirmation Bank to wear two hats and to ensure compliance with the standards of the German Takeover Act with regard to its roles as cash confirmation bank.

7.3.2. Equity

To the extent that the bidder finances its offer with its existing funds, the Cash Confirmation Bank must gain clarity that these funds exist at the time of the publication of the offer and are still available to a sufficient extent at the time of settlement. The Cash Confirmation Bank's due diligence procedures contain inherently a forecast and commercial assessment on the suitability of the measures taken to ensure the ability to fulfill the offer, taking into account foreseeable variables.

If the bidder is, as typically the case, a shelf company acquired solely for the purpose of the takeover and funded by its parent company, the Cash Confirmation Bank must in particular verify the financial situation of the parent company as well as the source of the funds on the level of such parent company and review the underlying documentation in connection thereto. In addition, the Cash Confirmation Bank would request a guarantee and covenants from the parent company with regard to the financing of the bidder by way of a separate agreement (e.g. equity commitment letter or keep well agreement).

7.3.3. Exchange rate risk

In the event that the available cash is in a currency other than Euro (e.g. USD), the bidder must ensure that it has sufficient funds in Euro at the time the offer consideration is due, also against the background of possible exchange rate risks (e.g. via exchange rate hedge or by requesting a "buffer" to be taken into consideration when calculating the funds held in a foreign currency). In its assessment, the Cash Confirmation Bank will consider the duration of the exchange rate risk, such as time until settlement and amounts in question relative to the overall funds.

8 Exemption from the obligation to launch a mandatory offer in connection with the restructuring of the target company

Dr Matthias Kiesewetter
White & Case LLP

Dr Nico Frehse
White & Case LLP

8.1. A report on BaFin's administrative practice over the last ten years

Restructuring a target company is the most frequently applied exemption from the obligation to launch a mandatory offer under German takeover law. This exemption is likely to become even more important as a result of the expected increase in restructurings due to the recent economic turbulences.

We have examined the administrative practice of the German Federal Financial Supervisory Authority (BaFin) over the last ten years to identify typical scenarios and points to consider when applying for this exemption.

8.1.1. Lead time

It is key to prepare well and to coordinate with BaFin to minimise the lead time between applying for an exemption and BaFin deciding. BaFin's administrative practice in Figure 1 shows that the lead time between applying and BaFin deciding varied widely – from eight days to almost 19 months (average: about four months).

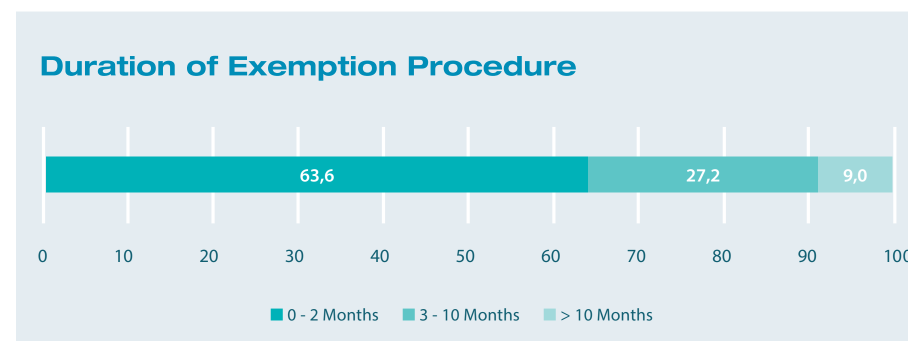


Figure 22: Lead time between applying for an exemption and BaFin deciding (in months)

8.1.2. Restructuring need

First, the bidder must prove that the target company has a need for restructuring that meets the exemption requirements of German takeover law.

In this context, BaFin most frequently accepted risks that threaten a company's existence within the meaning of the German Commercial Code (*Handelsgesetzbuch*, HGB) as a reason under takeover law for restructuring the company (80 percent of the restructuring cases). Another frequently accepted reason was imminent illiquidity of the company (48 percent) – see Figure 2. In contrast, neither illiquidity nor over-indebtedness was a significant factor in the decisions that BaFin has published.

The bidder must submit an expert opinion to BaFin to establish the need for a restructuring. Auditors generally prepare such expert opinions in accordance with the applicable standards of the German Institute of Auditors (*Institut der Wirtschaftsprüfer*, IDW). In an exceptional case, BaFin accepted an expert opinion from an investment bank.

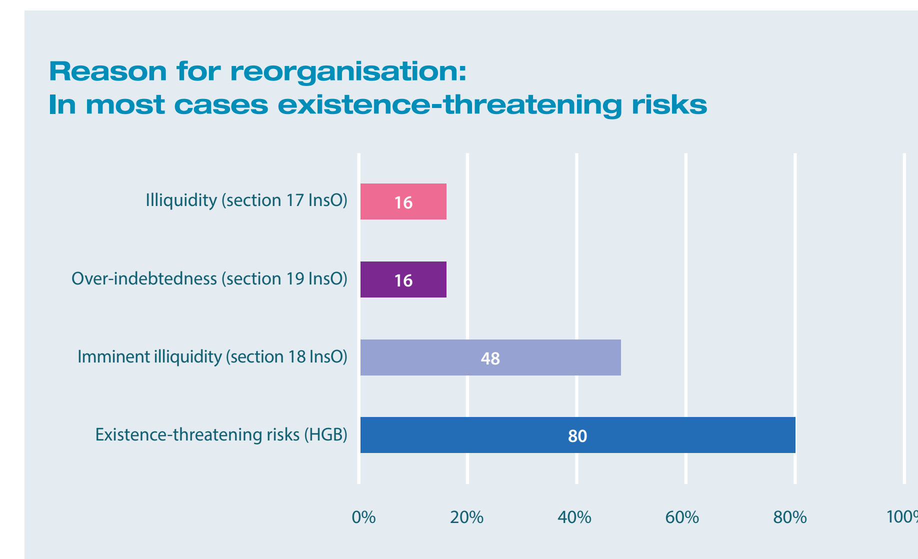


Figure 23: Reasons for needing a financial restructuring (several reasons were relevant in some cases)

8.1.3. Financial restructuring capability and concept

The bidder must demonstrate that it has a suitable restructuring concept with specific measures to overcome the crisis that the target company is facing. In other words, the company must have a realistic prospect of successfully continuing as a going concern.

96 percent of the proposed restructuring measures were capital increases of all kind – see Figure 3. In most cases, fresh capital was injected into the target company by way of a cash capital increase against the issue of new shares. In some cases, it was injected by way of an in-kind capital increase. In rare cases, it was injected by way of a mixed cash and in-kind capital increase. The restructurings were frequently combined with capital reductions (44 percent) or loans (36 percent). In their disclosed restructuring concepts, the applicants estimated an average lead time of about six months for the implementation of their concepts.

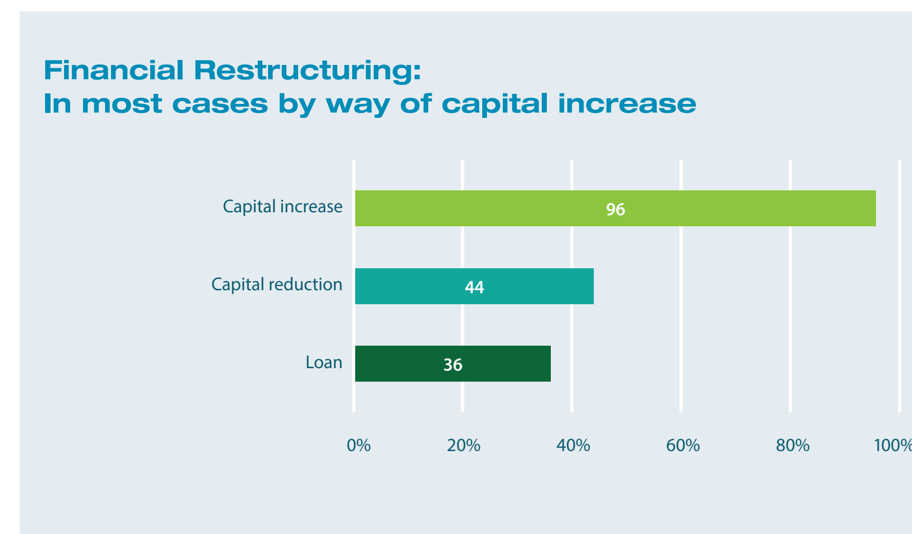


Figure 24: Financial restructuring measures

8.1.4. Contribution to the financial restructuring

In order to benefit from the exemption, the bidder must make an own contribution to the target company's restructuring and prove that its contribution will constitute the vast majority of the financial resources required for the restructuring. Most of the bidders (82 percent) were existing shareholders of the target companies, while bidders who had not previously been shareholders of the target companies made contributions to only 18 percent of the restructurings (see Figure 4). In most cases, the restructuring concepts and the exemptions were based on measures that involved contributions by the bidders and third parties (e.g., bondholders and lenders) to the restructurings.

Bidders often guarantee implementation of the capital increases by assuring BaFin – via backstop agreements – that they will acquire any new shares in the target companies that are not subscribed by other investors. Some third-party contributions were made in the form of waivers of claims or participation in a capital increase.

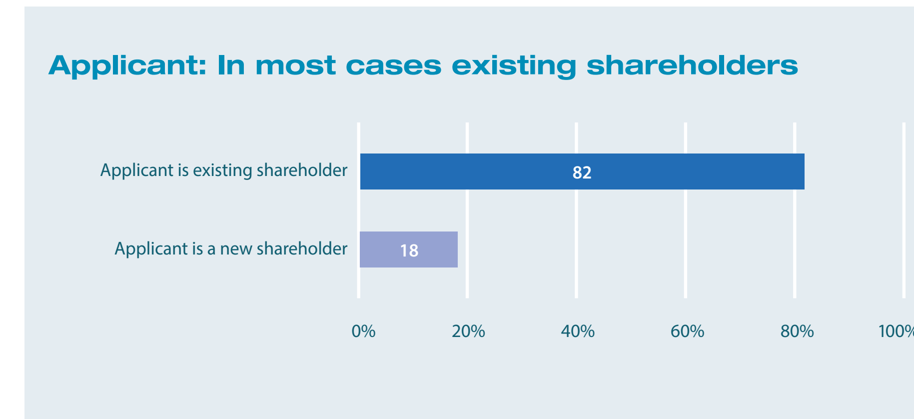


Figure 25: Status of the applicant

8.1.5. Ancillary provisions

BaFin has so far almost always attached ancillary provisions to its exemption decisions, such as conditions or reservations of the right to revoke. Typical conditions or reservations included (i) the implementation and registration of the capital increase as part of the restructuring or (ii) proof of the acquisition of new shares in the target company.

The bidders were generally granted an average of about two months to satisfy the conditions. In individual cases the bidder had to provide such proof without delay or only after 21 months. Depending on the type of ancillary provision, BaFin accepted extracts from the commercial register, subscription certificates and extracts from securities accounts as proof that the ancillary provisions had been satisfied.

8.2. Conclusion

The restructuring exemption has proven in numerous cases in recent years to be an important means to enable investments to be made in listed companies that are in a state of crisis. The very different lead times for the exemption procedure show, on the one hand, that BaFin has adopted a pragmatic approach that takes account of the circumstances of individual cases and, on the other hand, that it is important to prepare one's application well if one wants a swift and positive decision from BaFin.

9 Some suggestions from the advisory practice for amending the WpÜG

Dr Matthias Kiesewetter
White & Case LLP

Dr Alexander Kiefner
White & Case LLP

„Striving to better, oft we mar what's well." The first thing to say is that German takeover law has generally proven itself in practice during the more than 20 years since the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz*, WpÜG) came into force. The number of bids that have been executed successfully under the WpÜG in consultation with the Takeover Unit of the German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin) are clear evidence of this. True to the spirit of the aphorism cited above, the following article aims to provide some suggestions as to how the legislator and BaFin, through its administrative practice, could respond to some of the challenges that have recently emerged.

9.1. Exchange offers

Section 31 para. 2 sentence 1 WpÜG requires the exchange shares offered as consideration in public exchange offers to be "liquid". The shares offered in exchange for shares in the target company will not constitute valid consideration within the meaning of the WpÜG unless they meet this requirement. Since the WpÜG does not yet define when shares qualify as liquid, this is a matter of interpretation.

BaFin's previous administrative practice in this regard was both appropriate and practicable. Unfortunately, when Frankfurt Higher Regional Court confirmed BaFin's prohibition of the offer in the *Biofrontera* case in early 2021, it significantly tightened the requirement for liquidity and thereby caused BaFin to revise its previous practice on exchange offers. The liquidity criterion now requires bidders to plausibly demonstrate that the offered shares will have a free float in the regulated market of at least EUR 500 million after completion of the offer. Had this criterion applied in the past, it would have required the prohibition of a large number of public exchange offers – which are already rare. We are critical of the privileged position that this gives large stock corporations in exchange offers and the further complication of exchange offers that this produces.

We therefore argue that the determination under section 5 para. 4 of the German WpÜG Offer Regulation (*WpÜG-Angebotsverordnung*), namely the point at which the weighted average stock exchange price within a three-month period can no longer be used to determine the minimum price, should also be applied as a negative criterion to the assessment of the liquidity of the exchange shares. The WpÜG should now be amended to expressly require this.

9.2. Regulatory conditions, minimum acceptance threshold

Takeover bids may be made subject to conditions that comply with section 18 WpÜG. BaFin's administrative practice normally requires the conditions to be satisfied by the end of the regular acceptance period, failing which the bid fails.

An exception applies with regard to regulatory conditions, in respect of which BaFin has so far regularly accepted long-stop periods of up to 12 months from the end of the acceptance period. We are only aware of one case to date in which BaFin has allowed a longer long-stop period – 15.5 months from the end of the acceptance period in the 2018 *E.ON/innogy* bid proceeding, because it was expected to be subject to the sort of complex antitrust review that is normal in the energy industry.

Section 21 para. 1 sentence 1 nos. 3 and 4 WpÜG permit the bidder to lower the minimum acceptance threshold or waive conditions up to one working day before the expiry of the acceptance period. Both of these provisions go in the right direction.

A drop-dead or long-stop date 12 months after the expiry of the acceptance period is likely to prove less and less adequate to allow for regulatory conditions to be satisfied. When BaFin established its administrative practice, no one could have predicted that foreign trade regulation would be tightened up still further over recent years, causing a great deal of uncertainty regarding the lead time required to obtain a clearance decision. As long as shareholders who have accepted the offer can sell their shares via trading in the tendered shares (or can withdraw their acceptances) during the period of uncertainty, there will be no conflicting and overriding reason for the bid to terminate early or for the transaction to fail. We hope that BaFin will react to this development by adjusting its administrative practice and accepting longer long-stop periods as a new standard – also for non-energy targets.

The bidder's right to reduce the minimum acceptance threshold until the end of the acceptance period (but no longer during the two-week extension to the regular acceptance period provided for takeover bids – the so-called "fence-sitting rule" (*Zaunkönigregelung*) is closely related to the obligation under section 23 WpÜG requiring it to announce how its bid is progressing at specified intervals by means of so-called "water-level notifications" (*Wasserstandsmeldungen*). This includes the bidder's obligation to publish – initially on a weekly basis and during the last week of the acceptance period on a daily basis – the number of acceptance declarations it has received. It is generally accepted that these progress reports are not very meaningful in practice and do not achieve their intended purpose of providing market transparency. This is because a large proportion of institutional investors typically tender their shares just before the acceptance period expires. This often deprives bidders of the opportunity to react if the number of tendered shares proves to be insufficient at the end of the acceptance period. This seems inappropriate in its generality, and it often leads to undesirable, suboptimal results. On the other hand, it is also clear that, in a bid situation, neither the shareholders nor the target company should be left in the dark for too long about the satisfaction of conditions and the consequent success (or failure) of the bid.

We would therefore welcome it if the legislator decided to allow bidders to lower the minimum acceptance threshold after the expiry of the acceptance period at the same time as publishing – pursuant to section 23 para. 1 sentence 1 no. 2 WpÜG – the number of acceptance declarations they have received.

9.3. Settlement of the offer

We would welcome more flexibility in supervisory practice, if not necessarily a change in the law, with regard to the following point. BaFin typically allows a maximum period of eight to ten banking days for the bidder to settle its bid after it publishes – pursuant to section 23 para. 1 sentence 1 no. 3 WpÜG – the number of acceptance declarations it has received by the end of the additional acceptance period. This is sometimes difficult to reconcile with the fund-raising requirements of individual financial investors. Since the *WpÜG-Angebotsverordnung* does not specify a timeframe for the settlement, but only requires that the bidder specify the "time at which those who have accepted the offer will receive the consideration" in the offer document, there is nothing to prevent BaFin from exercising slightly more flexibility without losing sight of the justified concern that WpÜG-offers should be settled without delay.

9.4. The "white elephant" in the room – the overall legal environment for a "public to private"

Many bidders feel that a public takeover has not been "really" completed until all of the shares in the target company are in their hands and there is no longer any need for a stock exchange listing. However, it often takes more time to implement a squeeze-out in Germany than in other jurisdictions. Combining a takeover bid and a squeeze-out and achieving a correspondingly high offer acceptance rate is quite it is common in other countries, but virtually unheard of in Germany. Although a squeeze-out under takeover law pursuant to section 39a WpÜG would appear to be one obvious solution, this is irrelevant in practice since the obstacles (reaching a 95 percent participation rate in the course of the offer and a 90 percent irrevocable acceptance rate for the adequacy of the takeover price as compensation for the squeeze-out) are hardly ever cleared. Some market participants bet on receiving higher compensation if the bidder – often after a further increase in its shareholding – initiates a squeeze-out under the German Transformation Act (*Umwandlungsgesetz*, UmwG), which requires a 90 percent minimum shareholding, or under the Stock Corporation Act (*Aktiengesetz*, AktG), which requires a 95 percent minimum shareholding, or concludes a domination agreement permitting extensive control, which requires a 75 percent majority in the target company's general meeting, as a preliminary step.

This practice results from the use of different price-setting yardsticks. In the case of a domination agreement or a squeeze-out under the UmwG or the AktG, even a highly liquid stock exchange price only represents the lower price limit (at least according to the current practice, which is increasingly being called into question by the courts) – and a higher compensation amount may well result from a capitalised earnings value assessment. Since the stock exchange price usually rises automatically following the announcement of a takeover bid and will in any case reflect the premium that the bidder is offering, investors will expect an upside in the form of a higher compensation price if they wait a bit longer – assuming the takeover bid succeeds. An additional factor is that, where there is a control agreement or a squeeze-out under the UmwG or the AktG, the shareholders can subsequently have the amount of the compensation reviewed in relatively inexpensive court appraisal proceedings (*Spruchverfahren*).

The factors we have described above explain why, even in the case of a takeover bid with an attractive price reflecting a high premium, it may prove difficult to reach the minimum acceptance threshold and take control at the first attempt, and why the transaction may fail. It is generally unrealistic to expect to acquire 95 percent of the shares in the course of a takeover. In the interest of the competitiveness of the German takeover market, the legislator should work on improving the coordination between public takeover law on the one hand and the provisions on domination agreements and squeeze-outs under the UmwG or the AktG on the other. One suggestion is that an offer price that includes a substantial minimum premium over the share price should – conclusively – be deemed to be an appropriate compensation price for any control agreement or squeeze-out for a period of two years from the expiry of the offer period. This would remove most of the incentive to bet on expectations of higher compensation prices becoming self-fulfilling prophecies in the event of subsequent integration measures.

In recent years, there has been an increasing tendency to delist the target companies, and further legal clarification could help simplify the process. Currently, a bidder who acquires shares off-market at a price higher than the consideration set in the WpÜG offer within one year of publishing the results of the offer following the expiry of the acceptance period will in principle be obliged to pay the difference in arrears to the shareholders. However, section 31 para. 5 sentence 2 WpÜG provides that this does not apply where shares are acquired in connection with a statutory obligation to pay compensation – e.g., pursuant to a subsequent squeeze-out or on conclusion of a domination agreement. We suggest that the legislator should clarify that delisting offers which are statutorily required to precede delistings should also qualify as statutory obligations in this sense – so that no claim to a payment in arrears would arise if a delisting offer is initiated at a higher price within one year.

Authors

Dr Norbert Kuhn
Head of Corporate Financing
Deutsches Aktieninstitut e.V.
Telephone +49 69 92915-20
kuhn@dai.de

Dr Claudia Royé
Head of Capital Markets Law
Deutsches Aktieninstitut e.V.
Telephone +49 69 92915-40
roye@dai.de

Frankfurt
Deutsches Aktieninstitut e.V.
Senckenberganlage 28
D-60325 Frankfurt am Main
Tel. +49 69 92915-0
Fax +49 69 92915-12
dai@dai.de
@Aktieninstitut
LinkedIn Aktieninstitut

Brüssel
Deutsches Aktieninstitut e.V.
Rue Marie de Bourgogne 58
B-1000 Brüssel
Tel. +32 2 7894-100
Fax +32 2 7894-109
europa@dai.de

Berlin
Deutsches Aktieninstitut e.V.
Haus Huth
Alte Potsdamer Str. 5
D-10785 Berlin
Tel. +49 30 25899-774
Fax +49 30 25899-651
berlin@dai.de

Dr Alexander Kiefner
Partner
White & Case LLP
Telephone +49 69 29994 1132
alexander.kiefner@whitecase.com

Sabine Kueper
Attorney/
Professional Support Counsel
White & Case LLP
Telephone +49 69 29994 1343
sabine.kueper@whitecase.com

Berlin
White & Case LLP
John F. Kennedy-Haus
Rahel Hirsch-Straße 10
D-10557 Berlin
Tel. +49 30 880911 0
Fax +49 30 880911 297
www.whitecase.com
LinkedIn White & Case

Frankfurt
White & Case LLP
Bockenheimer Landstraße 20
D-60323 Frankfurt am Main
Tel. +49 69 29994 0
Fax +49 69 29994 1444

Düsseldorf
White & Case LLP
Graf-Adolf-Platz 15
D-40213 Düsseldorf
Tel. +49 211 49195 0
Fax +49 211 49195 100

Hamburg
White & Case LLP
Valentinskamp 70 / EMPORIO
D-20355 Hamburg
Tel. +49 40 35005 0
Fax +49 40 35005 111

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