



INSTYTUT ALLERHANDA

# Takeover Bids

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# Course overview



- i. Corporate consolidations – basic conceptualisations
- ii. Takeovers in context
  - i. Corporate governance
  - ii. Ownership patterns
  - iii. Political economy of takeovers
  - iv. Law and economics of takeovers
  - v. Regulatory strategies and legislative approaches
- iii. Hostile takeovers and takeover defenses
- iv. The EU Architecture for takeovers
  - i. Mandatory bid rule
  - ii. Price/Consideration offered
  - iii. No-frustration rule
  - iv. Break-through rule
  - v. Reciprocity
  - vi. Squeeze-outs and sell-outs
  - vii. The competent supervisory authorities and conflict of law rules
- v. The US approach to hostile takeovers
- vi. Creeping acquisitions
  - i. Case study: building a secret toehold & the use of CSD



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# Corporate consolidations – basic conceptualisations



## Consolidations – a typology

### forms of business consolidations

share deals

mergers

asset  
deals

SPA

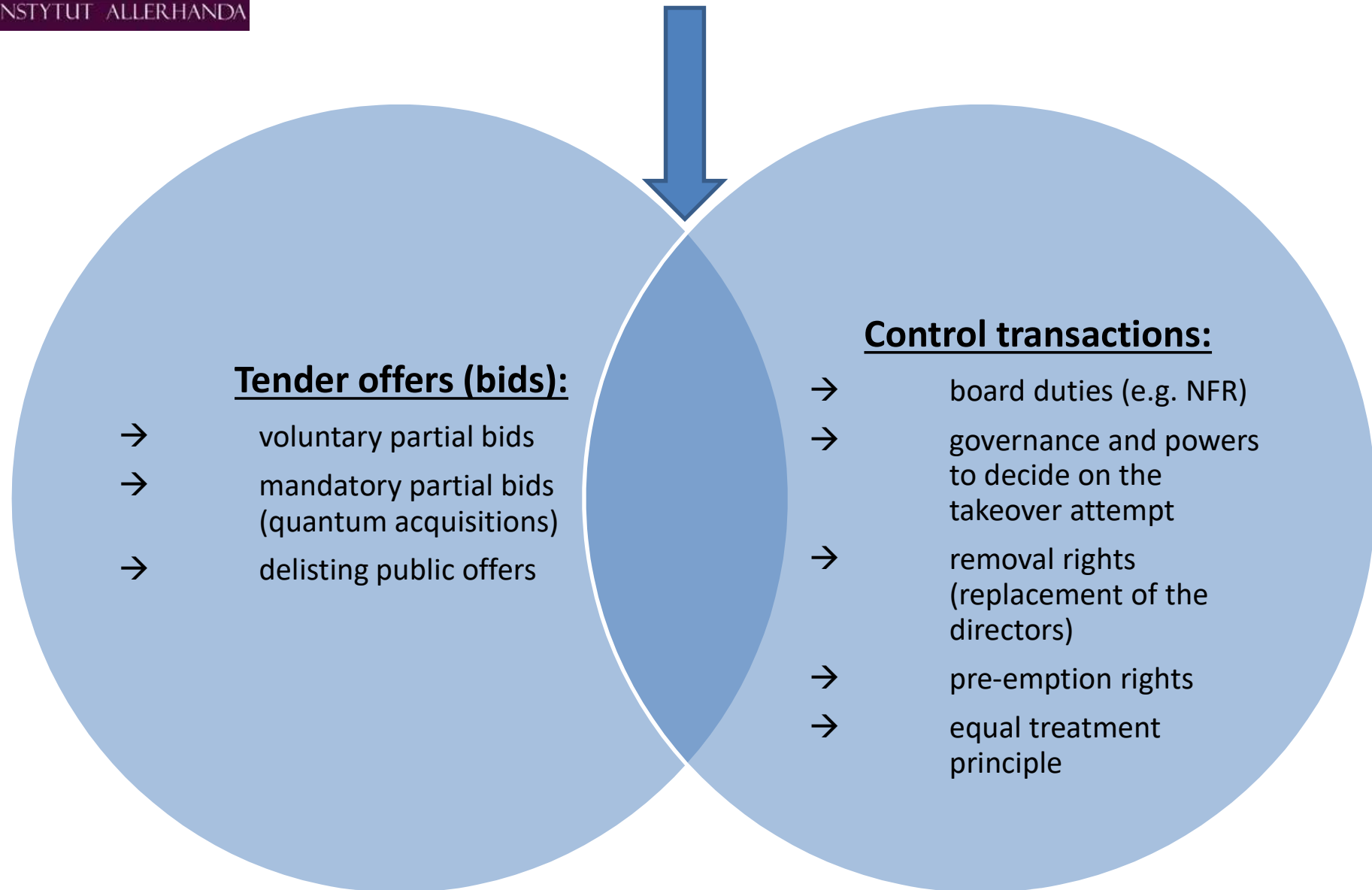
schemes of  
arrangement  
(share  
exchanges)

**takeovers**

friendly

hostile

# (mandatory/voluntary) takeover bids





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# Takeovers in context



corporate  
governance

ownership  
patterns

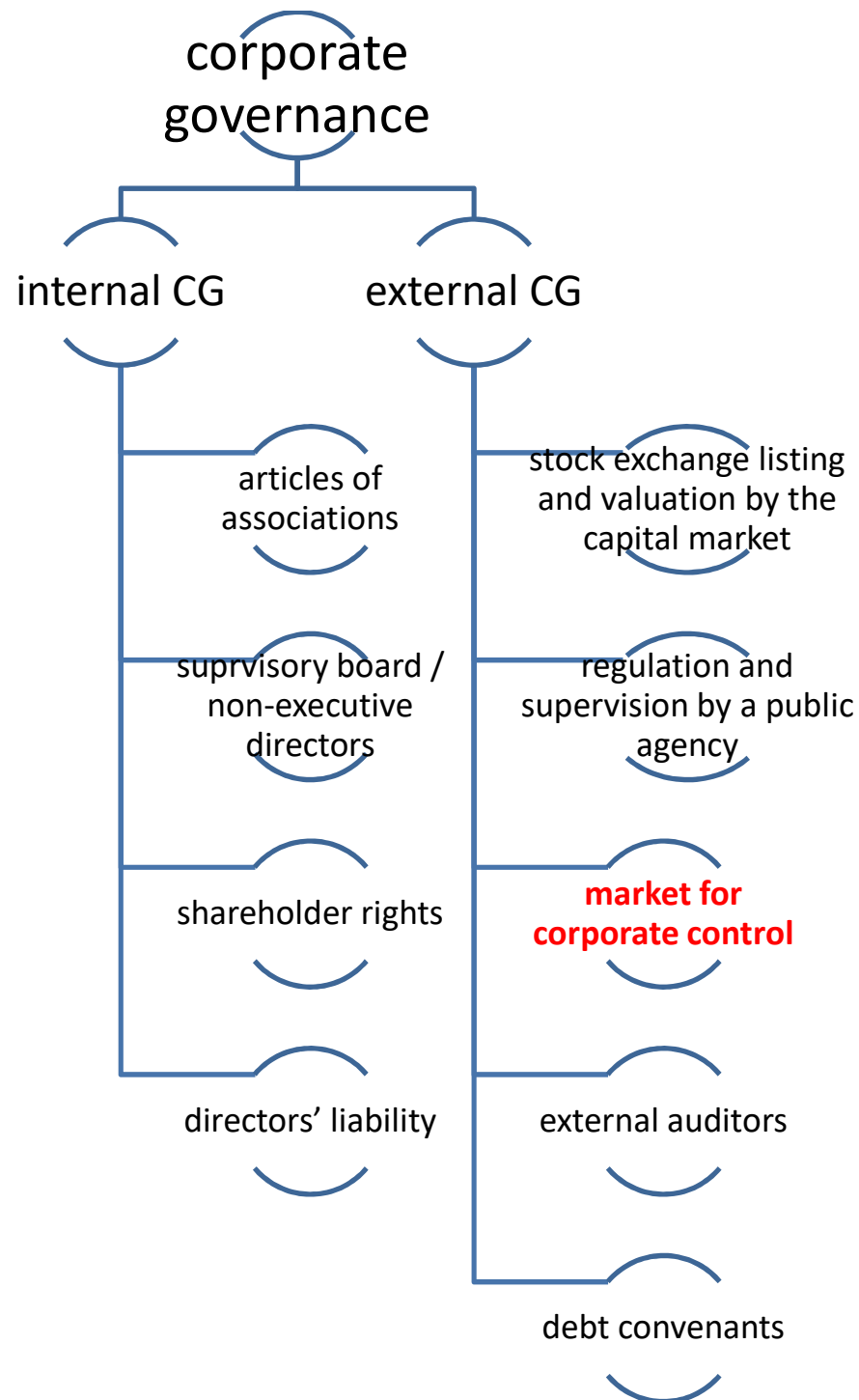
takeovers  
in context

political  
economy

law and  
economics

→ regulatory strategies



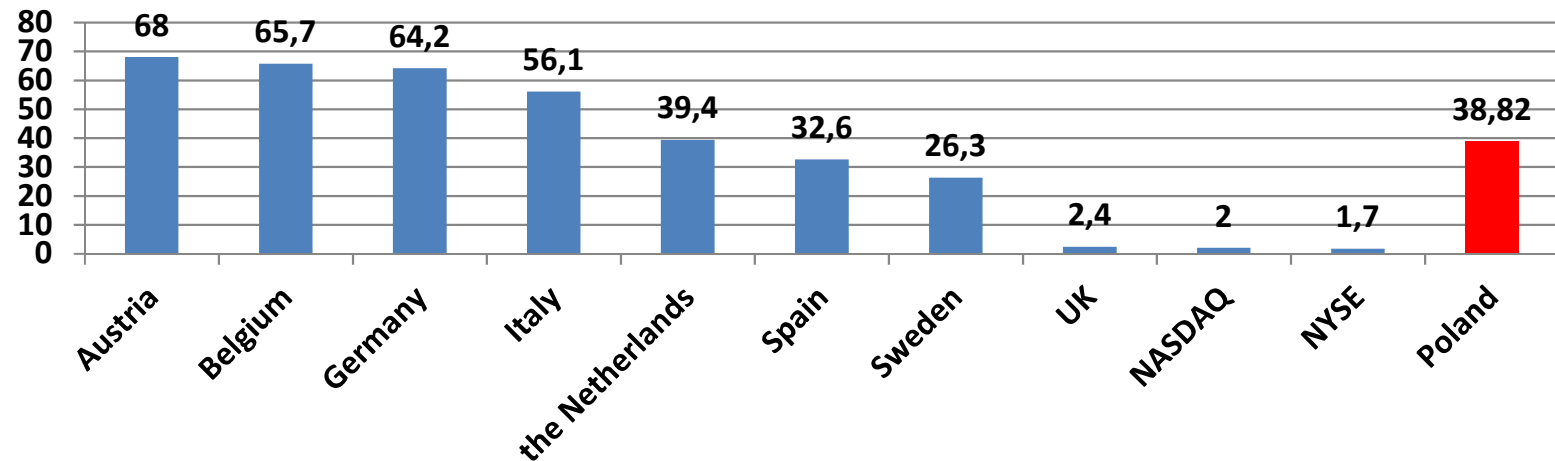




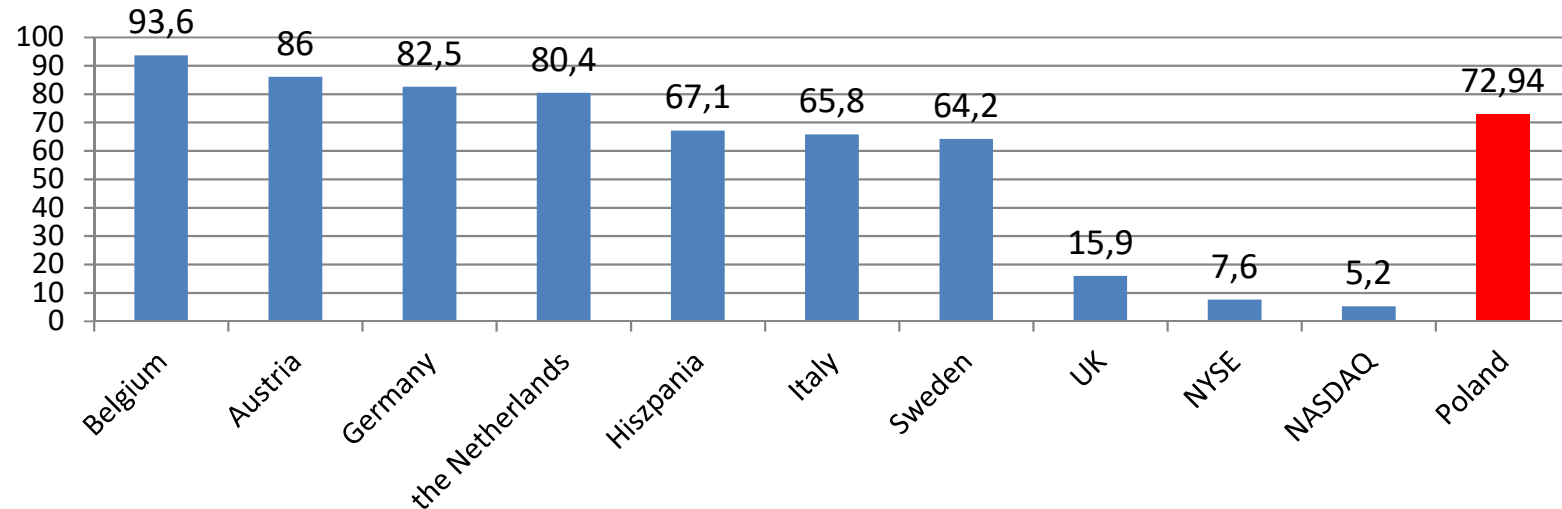
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## Ownership structures in a comparative perspective

Percentage of companies with a controlling blockholder

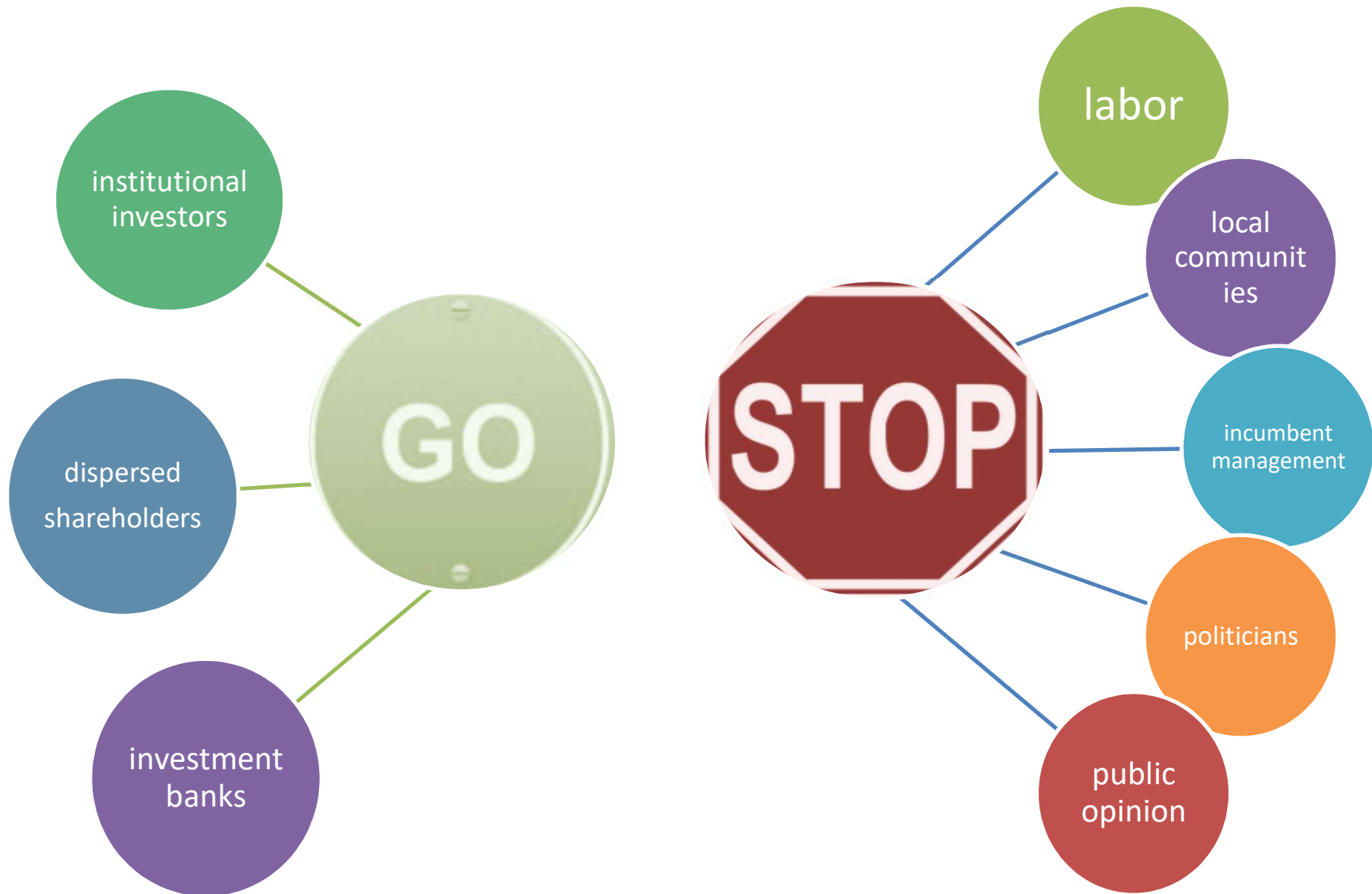


Percentage of companies with a shareholder owning at least 25 % of voting shares



Source: Barca & Becht (2001), *The Control of Corporate Europe*, OUP  
For Poland: T. Regucki, Allerhand Institute, own research (as of 28.11.2011)

# Political economy of takeover statutes

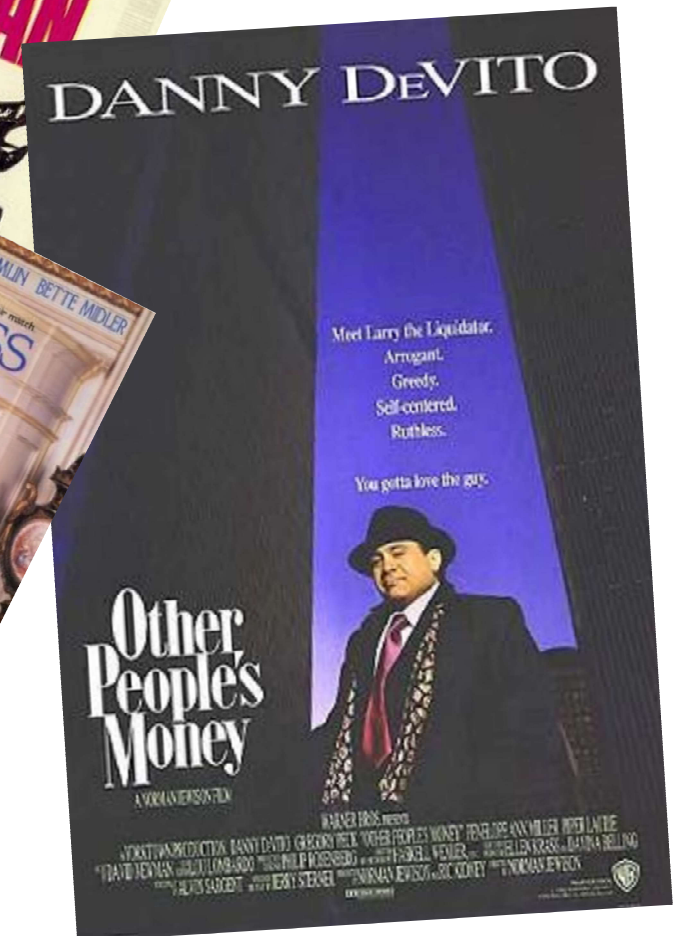




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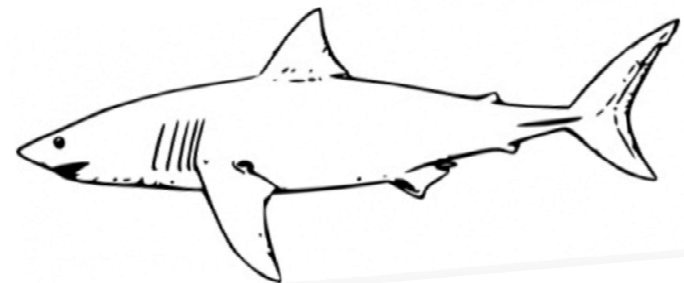
# Political economy of takeovers

Widespread popular scepticism  
influenced  
by mass culture





# Shark vs Raven



VISTULA VS W. KRUK  
1840





# law and economics of takeovers

*are hostile takeovers a good or a bad thing?*

- **the „shareholder value“-paradigm:**
  - under efficient markets hypothesis (**EMH**) stock prices reflect the intrinsic value of the corporation
  - tender offer at a premium over the market price reflects a value-enhancing proposal by a bidder who, if rational, must be fitter to manage the corporation in such a way that will increase the value of the company and generate better cash-flows in the future (better managerial performance, synergies, reorganisations)
  - hostile takeovers discipline the incumbent managers to perform at their best, and allow their replacement if they fail to deliver
- **the „corporation as a whole“-paradigm:**
  - corporation is a social institution authorised by law to promote wealth creation for the benefit of shareholders and managers, but also of the society at large
  - interests other than those of shareholders need to be taken account of (stakeholder perspective)

## L&E: facilitation of hostile takeovers through regulation?

### cons

- **hampering firm-specific investments**
- risk of loss of the **company's strategic agenda**
- encouragement of **short terminism**
- conflicts with the interests of **labor** and **local communities**
- **sustainability** considerations

### ???

- shareholder value
- (+) EMH
- (-) Takeover defences as a tool to
  - promoting **long-termism** over short-termism
  - improving **bargaining position** vis-a-vis the bidder

### pros

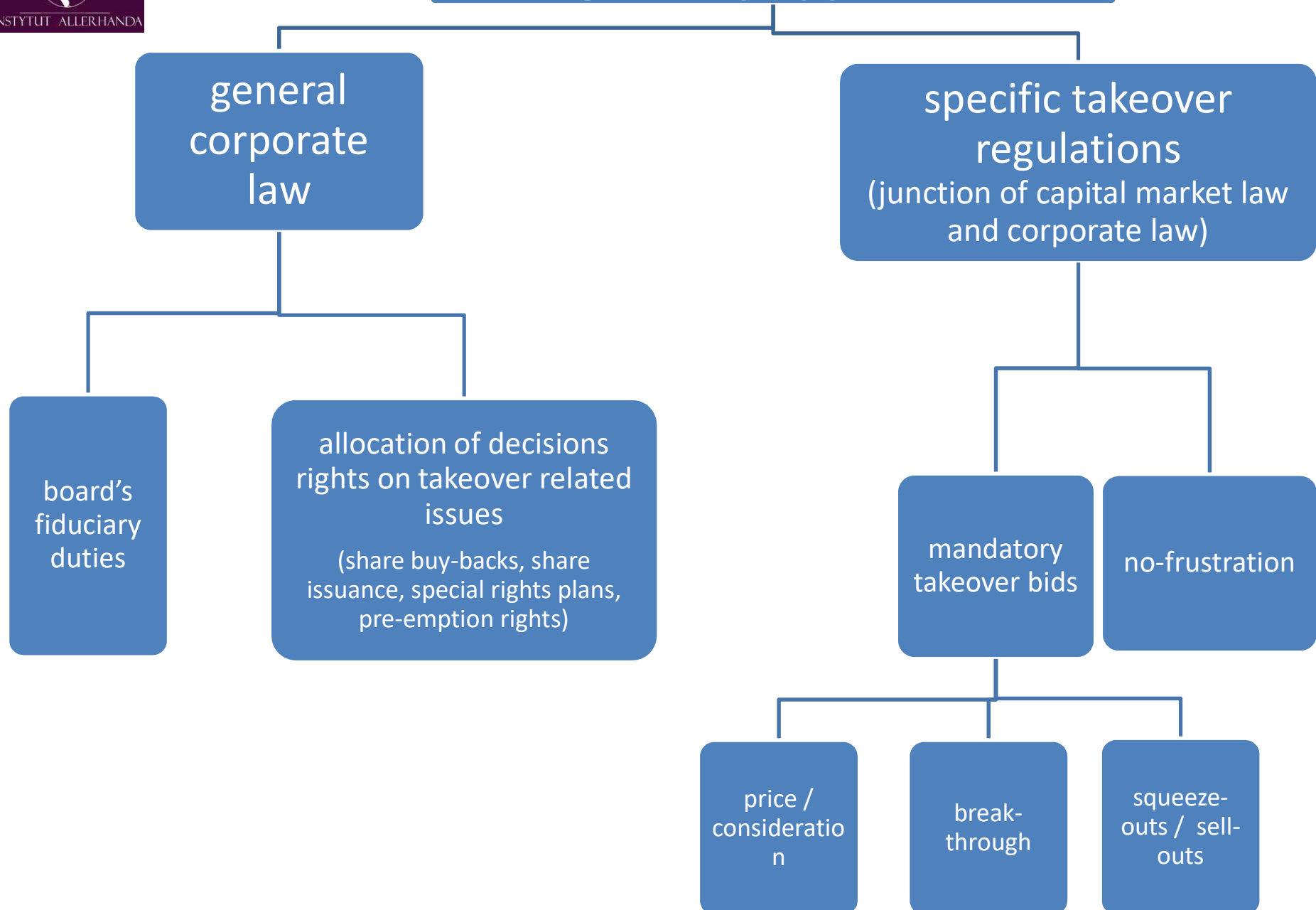
- **disciplining** effect on managers
- efficient **allocation** of productive **resources**

## L&E: legislative approaches

- How to regulate:
  - takeovers **promoting** regime/rules
  - takeovers **hindering** regime/rules
  - **neutral** (unbiased) approach
- Where to regulate? – choices with regard to legislative intervention:
  - **federal/EU** level
  - **state/MS** level
  - **company's** level (**articles** of associations)



# Regulatory approaches





## L&E: various agency conflicts

# Basic takeover scenarios

Where there is  
no controlling  
shareholder  
(control  
building)

Where there is  
a controlling  
shareholder  
(control  
transfer)



## L&E: agency conflicts and other problems where there is no controlling shareholder (**control building**)

- Agency conflict between the **target's management and shareholders as a class**:
  - the transaction may be **value-enhancing** for the target's shareholders **but** may **threaten the jobs of the incumbent management**
  - the transaction may **not be value-enhancing** for the target's shareholders **but** the **managers** may be **self-interested** in promoting the deal either by the fact of receiving attractive **termination payments** or being themselves **linked to the bidder**
- Other problems:
  - **control premium**: **equally shared** or captured by the acquirer?
  - **change in governance and risk profile** following the successful acquisition of a controlling block (**stand-alone → dependent company**), increased risk of extraction of private benefits of control by the majority shareholder



## **L&E: agency conflicts where there is a controlling shareholder (**control transfer**)**

- Agency conflict **between the target's controlling blockholder and dispersed shareholders**:
  - the problem of obtaining the **control premium** solely by the controlling blockholder
  - „exemption” (shielding) from the market for corporate control by the unwillingness of the controlling shareholder to tender shares
- Other problems:
  - **change in the risk exposure for the minorities** (part of the control premium may be in the acquirer's intention to expropriate the minority or loot the company)



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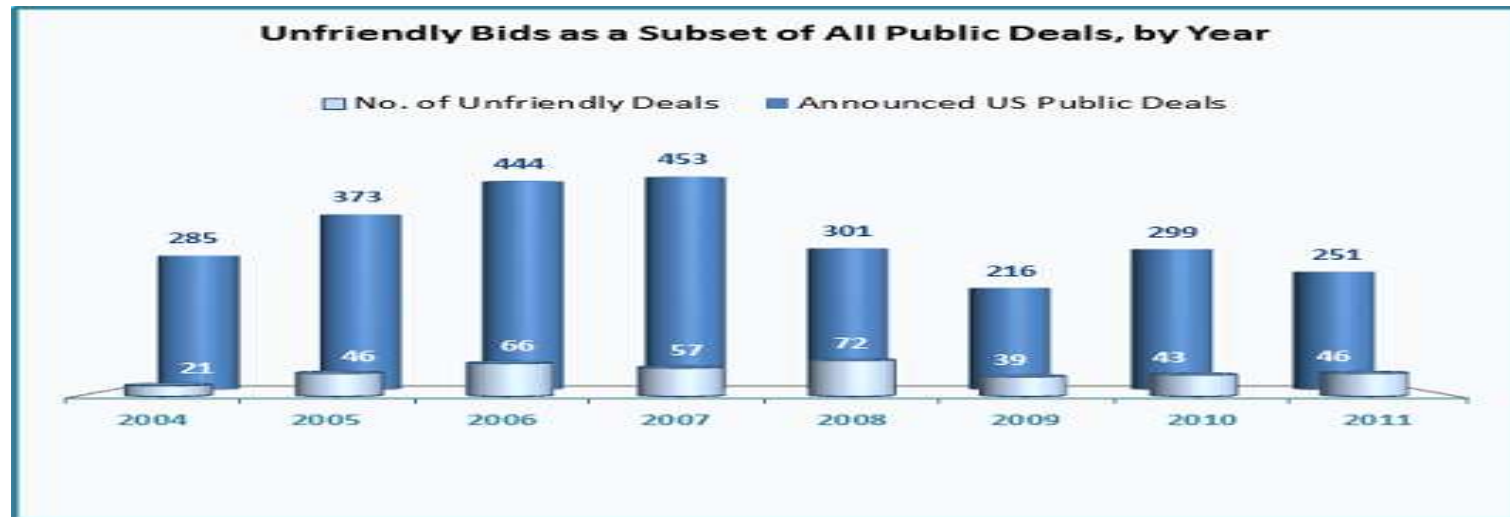
# Hostile takeovers and takeover defences



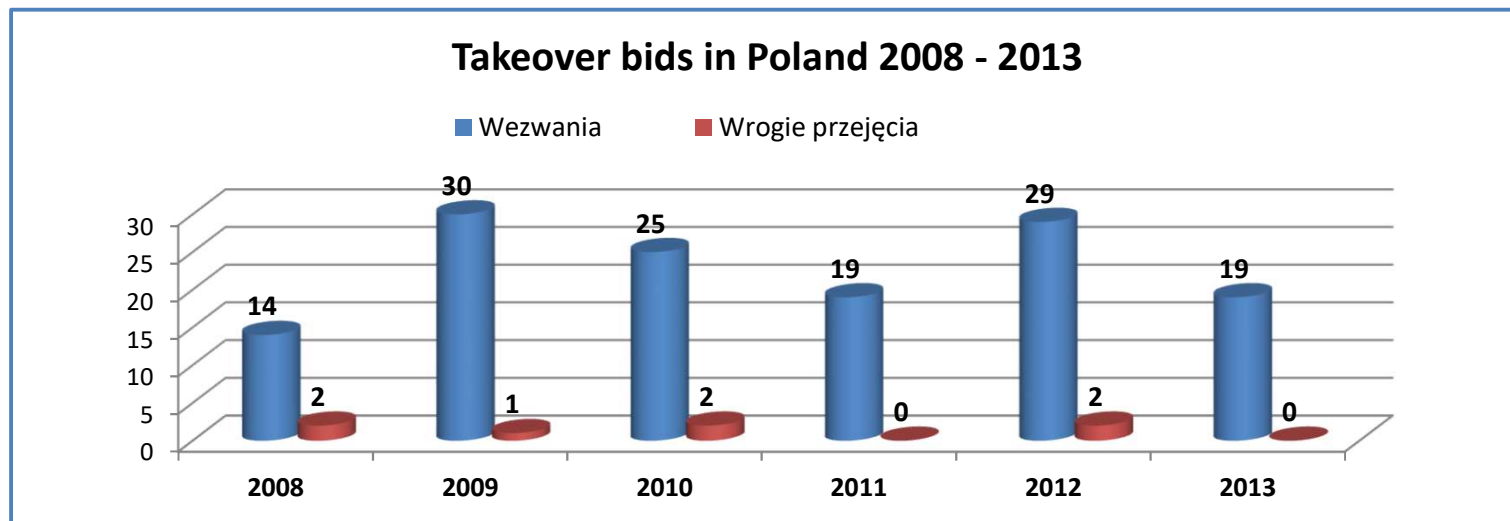
## Hostile takeovers and takeover strategies

- Point of departure: in **M&A** transactions
  - **shareholders** are the **ultimate decision-makers (as a group)**,
  - **Management Board** is... the **gatekeeper** or **self-interested** agent?
- **Hostile takeover bids**
  - „**circumvention**” of the **Management Board** via unsolicited offers
  - shareholders decide individually (coordination problems)
- **Takeover defences**
  - restoring **Management Board’s „say on deal”**

# Takeover activity US and Poland



Source: [www.factsetmergers.com](http://www.factsetmergers.com)



Source: Tomasz Regucki, Allerhand Institute, own research



# takeover defence categories

pre-bid  
(preventive –  
„shark  
repellents”)

- structural defences
- CEMs

post-bid  
(reactive)





# takeover defence methods

price-  
increasing  
defences

reduction  
of rights  
attached  
to shares

frustration  
of the  
commercial  
purpose of  
the  
acquisition

# pre-bid defences

structural defences and  
control enhancing mechanisms (see Article 10 sec. 1 TBD)

golden shares

supermajorities

staggered board

poison pills

multiple voting shares

ESOPs

voting caps

ownership ceilings

contractual sell-out rights

golden parachutes

change of control clauses  
(financial, non-financial)

# post-bid defences

## response by the target's board

soft  
parking

slim  
down:  
capital  
changes  
to keep  
the  
company  
lean, e.g.  
share  
buy-back,  
debt  
raising,  
extra  
dividends

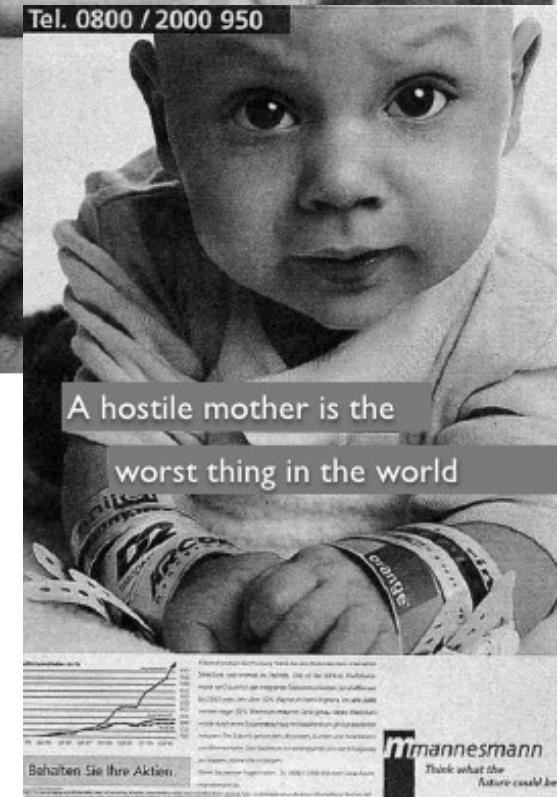
search  
for  
alternativ  
e bidder  
(White  
Knight,  
White  
Squire  
defence)

counter-  
bid  
(Pacman  
defence)

acquisitio  
n of the  
bidders  
interest  
in the  
target at  
premium  
(Greenm  
ail  
defence)

litigation

scorched-  
earth,  
crown  
jewel





# Poison pill

- **Idea:** to dilute the acquirer's block in the target so as to frustrate the bid and fend off takeover attempts
- **Triggers:** **flip-in** – launching of the offer or passing a certain threshold ; **flip-over** – merger
- **Entitlement:** **flip-in** – for every share held, a right to subscribe for or acquire one new share at a highly preferential (discounted) price (for every shareholder except the bidder); **flip-over** – preferred stock convertible into acquirer stock at a favourable ratio in case of post-acquisition merger
- **Governance and legal problems:**
  - board's power
  - equal treatment
  - pre-emption rights



**ALL AMERICAN**

**[2000] All American Semiconductor:**  
poison pill adopted by the board to be activated when a pursuer announces a tender offer that would result in purchasing 15% of the common stock.



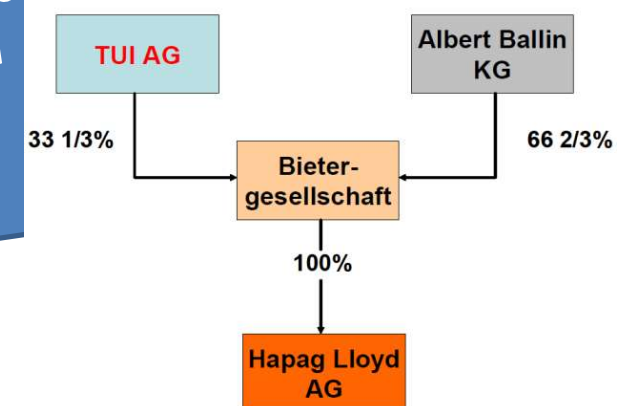
## Keeping assets away of the acquirer

- Change of control clauses (e.g. by financial investors)
- Lock-up of corporate assets



### [2008] TUI AG:

- TUI AG of Germany - the largest European travel company and number 5 in container shipping worldwide.
- TUI's container shipping business run via its subsidiary the Hapag-Lloyd AG
- Mr John Fredriksen – Norwegian shipping magnate and the largest shareholder of TUI AG.
  - Mr Fredriksen is interested in taking over Hapag-Lloyd,
    - either indirectly through increasing his stake in TUI or
    - directly by forcing TUI to spin off Hapag-Lloyd to TUI's shareholders
- TUI „exports“ Hapag-Lloyd to a subsidiary established with friendly investors and so keeps Mr Fredriksen away of Hapag-Lloyd





# Keeping assets away of the acquirer

- Stock lending / Soft parking



VS



## [2007] MOL Group:

- attempt of a hostile takeover of MOL (HU) by OMV (AT)
- MOL keeps buying own shares
- The limit on share buy-backs circumvented by stock lending to two friendly Hungarian banks. The banks were free to exercise voting rights but were contractually obliged not to sell shares



MITTAL

VS

arcelor

- Setting the stage – Parties
  - **Arcelor** was incorporated under Luxembourg law. Listed on SE in Luxembourg, Brussels, Paris, and on four Spanish stock exchanges
  - **Mittal Steel** was incorporated under Dutch law. Listed in New York and Amsterdam. Controlled by Mr. Lakshmi Mittal
  - **Ugitech** was Arcelor's French subsidiary
  - **Dofasco** was a large North American steel company
  - **Severstal** was the largest Russian steel producer controlled by Mr. Alexei Mordashov
  - **ThyssenKrupp** was the German steel and technology company





MITTAL

VS

arcelor

- Prologue
  - **Arcelor vs Dofasco.** On 30 December 2005, Arcelor made a successful bid for Dofasco. During March and April 2006, Arcelor acquired 100% of the shares of Dofasco.
  - **Mittal Steel & ThyssenKrupp.** On 26 January 2006 Mittal and ThyssenKrupp concluded an agreement whereby if Mittal were to be successful in its tender offer for Arcelor, Mittal would force Arcelor to sell Dofasco to ThyssenKrupp.
- Episode I: Mittal vs Arcelor – Let the battle begin
  - On 27 January 2006, Mittal Steel made an **unsolicited offer** of **€18.6 billion** in cash and shares for Arcelor.
  - On 29 January 2006, **Arcelor's board rejects** the offer (quote: *"150% hostile"; "no industrial logic"*)



MITTAL

VS

arcelor

- Episode II: Arcelor's defence
  - [**Crown Jewels**]: **sale of Ugitech** (Arcelor's French subsidiary)
  - [**Crown Jewels**]: **transfer of Dofasco to** an independent Dutch foundation "**Strategic Steel Stichting**" („S3"). Arcelor would retain full control over Dofasco, including all decision-making power and all economic interest relating to Dofasco, with the exception of any decision to sell Dofasco. The S3 Board members would have independent control over any decision to sell Dofasco.
  - [**slim down**] **raising debt € 4 billion Term Loan Facility** with a 3 year maturity.
  - [**slim down**] proposal to **increase dividends** from € 1.20 to € 1.85 per share.
  - [**slim down**] **further distribution of € 5 billion** to be later decided by the board (could take the form of a **share buyback**, an **extraordinary dividend payment**, or a **self tender offer** in-between the dates of the AGM)
  - [**White Squire**]: On 26 May 2006, **Arcelor and Severstal announced that they had agreed to merge**. In the proposed deal Arcelor would buy a 90% stake in Severstal. Following the subsequent merger, Mr. Mordashov would end up with a 32% block of shares in the new Arcelor.



MITTAL

VS

arcelor

- Episode III: Testing the limits

- on 11 June 2006, Arcelor's board:
  - **rejects** Mittal Steel's **revised offer**
  - **recommends** that shareholders support the proposed **merger with Severstal**
- **shareholders** and the **media increasingly critical about the governance** of Arcelor.

- Episode IV: Takeover's happy end

- **Pressure results in change of the attitude:** on 25 June 2006, Arcelor's MB eventually decided to recommend Mittal's improved offer to shareholders
- In September 2006, **93.7% of Arcelor shareholders tendered their shares to Mittal Steel**
- Sell-out and squeeze-out followed the bid
- (2007) a merger between Mittal and Arcelor

- Epilogue

- After the takeover, the boards of Mittal and Arcelor requested that the Stichting (S3) dissolve and **return the Dofasco to Arcelor**. **S3's board refused** → litigation.

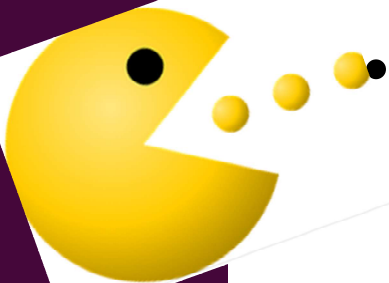
ArcelorMittal



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## VISTULA *VS* W.KRUK 1 8 4 0

- **Mr. Wojciech Kruk** was W.Kruk's largest shareholder with **22%** of shares, the **rest was dispersed**. Mr Kruk enjoyed special individual rights (354 KSH), later eliminated under the pressure from the funds.
- On 5 May 2008 **Vistula launches a hostile takeover bid for the acquisition of 66%** shares of W.Kruk.
- A few days before the closing of the bid – 50% threshold not matched. **Increase of the offer price** from 23,7 to 24,5 PLN.
- 30 May 2008 – **bid turns out successful** because **Mr. Kruk sells his block** to the bidder.





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V I S T U L A

VS

W.KRUK  
1 8 4 0

- Mr. Kruk **acquires** a substantial block of **shares in Vistula for the cash he received for his W.Kruk shares**
- 18 June 2008 – **further indirect acquisitions** of Vistula shares by Mr. Kruk
- 20 June 2008 – **friendly investor**, Mr. Jerzy Mazgaj joins in to **act in concert** with Mr. Kruk
- **Kruk & Mazgaj capture control over Vistula**  
→ 30 June 2008 replacement of the whole SB
- 18 July 2008 – „**reconquest**” of **W.Kruk** – Mr. Kruk again becomes the president of the SB
- 31 December 2008 – completion of the **merger** between W.Kruk and Vistula



(Austria, March-April 2015)

- **CA Immo** via its SPV subsidiary acting **in concert with O1** launch a hostile takeover for a **minority block of Immofinanz** shares (approx. 21%)
- Defensive strategy of Immofinanz:
  - reverse bid: public offer by Immofinanz to acquire a minority block at CA Immo (**Pacman**)
  - **amendment of articles** of association so as to:
    - **lower the control threshold from 30% to 15%** (trigger of mandatory bid for all outstanding shares on contractual basis)
    - increase the majority needed to **replace SB members to 75%**
  - **litigation**
- Defensive steps by CA Immo:
  - reallocation (parking) of all **Immofinanz** shares at **O1**





FMCG retail and  
wholesale company

VS



Supermarkets and  
real estate

- **Merger talks.** 13 Sep. 2010 – **Eurocash submits a proposal** for a friendly merger with Emperia
- 14 Sep. 2010 – decisively **rejecting stance by the Emperia's MB**
- Emperia undertakes defensive measures
  - 16 Sep. 2010 – Emperia's SB approves the **issuance of new shares free of pre-emption rights**
  - 16 Sep. 2010 – Emperia's SB approves **share buy-back** – prompt execution by the MB (21 Sep.)
  - 21 Sep. 2010 – publication of a **new dividend plan**
  - 11 Oct. 2010 – announcement of a **division of Emperia**





- 28 Sep. 2010 – MB of **Eurocash** decides to **increase share capital** (within authorised capital approved in advance by the GM) by issuance of new shares that could be **offered in exchange for Emperia's shares**
- Nov. 2010 – **division plan of Emperia** foreseeing the **spinoff of Tradis** (supermarket operator, e.g. of **Lewiatan**)
- 21 Dec. 2010 – **investment agreement** between Eurocash and Emperia providing for the **sale of Tradis to Eurocash** (PLN 926 m)
- 9 Aug. 2011 – **Emperia withdraws** from the investment agreement
- Sep. 2011 – parties involve in the dispute over the termination of the investment agreement – **arbitration proceedings** initiated
- 6 Dec. 2011 – change of **Emperia's articles of association**:
  - the acquirer of **33%** voting shares shall be obliged to buy-out all the outstanding shares upon the seller's request (**put option – „sell-out”**)
  - proposal (eventually not adopted) for a special **individual shareholders' rights to appoint board members** backed by these shareholders' veto right to block some decisions of the board members appointed by these shareholders
- 21 Dec. 2011 – **amicable settlement: sale of Tradis** to Eurocash for PLN 1,1 bn





VS



**Enea** – one of the leading energy companies in PL (market share >15%), controlled by the State (50,5%)

**Bogdanka** – one of the largest and most profitable coal mining companies in PL, WSE-listed since 06/2009; 03/2010 the state disposes of majority stock

- 21 Aug 2015 – **Enea** terminates a long-term contract for supply of coal by **Bogdanka** (contract's initial expiry date: 31 Dec 2025) → sudden fall of **Bogdanka's** share price
- 14 Sep 2015 – takeover bid by **Enea** targeting **Bogdanka's** shares
- 18 Sep 2015 – **Bogdanka's** Board convenes a GM to be held on 15 Oct 2015. Agenda: introduction of a voting cap. Attempt failed.
- 30 Oct 2015 – **Enea** acquires a controlling stake in **Bogdanka** (66%)

Financial Supervision Authority (KNF) examines the case but denies a stock price manipulation by **Enea**



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# The EU architecture for takeovers



## Objectives pursued by the Takeover Directive

- Facilitation of takeover bids;
- Reinforcement of the single market, by enabling free movement of capital throughout the EU;
- Legal certainty and community-wide clarity and transparency in respect of takeover bids;
- Protection of the interests of dispersed shareholders, of employees and other stakeholders through transparency and information rights.



## Overview of the main problems

- **Mandatory takeover bid**
  - Trigger
  - Price
  - Exceptions
- **The „no frustration“-rule** (board neutrality)
  - stronger form (*ex post*, post-bid approval)
  - weaker form (*ex ante*, pre-bid approval for a limited period (e.g. Germany, similarly: Japan))
- **Break-through rule**
- **Reciprocity** principle
- **Squeeze-out** and **sell-out** right
- **Competent authority** and **applicable law**

## Mandatory takeover bid (Article 5 TBD)

- **Rationale**: shareholders protection
  - **exit** for minority in the change-of-control setting
    - control „creation”
    - control shift
  - **equal distribution of control premium**
  - **preference reconciliation** among the shareholders
- **Criticism**:
  - costly
  - hindering some of the economically efficient takeovers
  - no reason for providing exit mechanism
  - why would the highest price paid in the last 6-12 months be indicative for the control premium?



## Obligation to make a bid (Article 5 par. 1 TBD)

*Where a natural or legal person, as a result of his/her own acquisition or the acquisition by persons acting in concert with him/her, holds securities of a company [...] which, added to any existing holdings of those securities of his/hers and the holdings of those securities of persons acting in concert with him/her, directly or indirectly give him/her a specified percentage of voting rights in that company, giving him/her control of that company, Member States shall ensure that such a person is required to make a **bid** as a means of protecting the minority shareholders of that company. Such a bid shall be addressed at the earliest opportunity to all the holders of those securities for all their holdings at the equitable **price** as defined in [Art. 5 par. 4].*



## Trigger: acquisition of control

- Art. 5 par. 3. The percentage of voting rights which confers control for the purposes of paragraph 1 and the method of its calculation shall be determined by the rules of the Member State in which the company has its registered office.
- Implementation in EU Member States:
  - 25%: Hungary, Slovenia, Italy (since 2014);
  - 30%: Austria, Cyprus, Finland, Germany, Ireland, the Netherlands, Spain, Sweden, UK;
  - 33%: Grece, France, Luxemburg, Slovakia;
  - 40%: Czech Republic, Lithuania;
  - 50%: Latvia, Malta
  - 66%: Poland (33% for mandatory partial bid)
  - open-ended standard (actual control) : Estonia
  - additional (independent, non-cumulative) trigger – actual control: Spain



## Exceptions and derogations

- **[Exception]** Art. 5 par. 2: *Where control has been acquired following a voluntary bid made in accordance with this Directive to all the holders of securities for all their holdings, the obligation laid down in paragraph 1 to launch a bid shall no longer apply.*
- **[Derogations]** Art. 4 par. 5: [...] MS may provide in the rules that they make or introduce pursuant to this Directive for derogations from those rules:
  - (i) *by including such derogations in their national rules, in order to take account of circumstances determined at national level [← legislative]; and*
  - (ii) *by granting their supervisory authorities [...] powers to waive such national rules, to take account of the circumstances [...] in which case a reasoned decision must be required [← administrative]*



## Derogation categories

- Discretionary power of the national supervisory authority to grant an exemption (FI, IE, UK, to a limited extent also FR and DE);
- Whitewash procedures where shareholders of the target company may decide to waive the obligation to launch a mandatory bid;
- Situations where there is no real change of control, for instance when the change of control is temporary or the acquisition has taken place within the same company group or "acting in concert" group;
- To protect the interests of the offeror or the controlling shareholder, for instance when the change of control was not caused by a voluntary act, the acquisition was indirect, or followed a personal event, such as inheritance;
- To protect the interests of a creditor, for instance in situations where the acquisition is the consequence of an exercise of financial security by a creditor;
- To protect the interests of other stakeholders, for instance when the target is in financial distress, when control is acquired through a specific type of corporate transaction, such as a merger or scheme of arrangement, or when control is acquired following a sale of securities by the state (privatisation).
- When passing the statutory threshold does not actually confer control (legal or administrative), e.g. another shareholder holds 45%



## The equitable price

[General rule] Art. 5 par. 4 sec. 1:

- *The highest price paid for the same securities by the offeror, or by persons acting in concert with him/her, over a period, to be determined by MS, of not less than 6 months and not more than 12 before the bid referred to in paragraph 1 shall be regarded as the equitable price.*
- *If, after the bid has been made public and before the offer closes for acceptance, the offeror or any person acting in concert with him/her purchases securities at a price higher than the offer price, the offeror shall increase his/her offer so that it is not less than the highest price paid for the securities so acquired.*



## The equitable price

- **[Adjustments]** Art. 5 par. 4 sec. 2: [...] MS may authorise their supervisory authorities to adjust the price [...] in circumstances and in accordance with criteria that are clearly determined. [...] either upwards or downwards, for example where the highest price was set by agreement between the purchaser and a seller, where the market prices of the securities in question have been manipulated, where market prices in general or certain market prices in particular have been affected by exceptional occurrences, or in order to enable a firm in difficulty to be rescued.
- **Periscopus-case** (EFTA Court): TBD precludes national legislators from providing that the supervisory authority may adjust offer price arbitrary or under unclear conditions (this could e.g. lead to illegal defences of national champions, if price set too high)



## Selected bid-related problems

- **Acting in concert** – risk and tension with shareholder activism
- Problem of **equal treatment**
  - bid territorial limitations (carve-out clauses)
    - special case: US
- Problem of **conflict with bids outside the scope of the TBD**, specifically in dual-listing setting (CA Immo vs Immofinanz)
- **Conditional offers** – e.g. acceptance by 95% SH
  - financing may not be a condition,
  - mandatory bids may not be conditional
  - MS vary with respect to the admissability of conditions for voluntary bids

## The „no frustration”-rule (also called „board neutrality”)

- **Source:**

- Art. 9 of the Takeover Directive
- but MS’s opt-out possible (Art. 12)
- Company’s opt-in possible if MS opted out

- **Notion:**

- shareholders authorisation for the board required to take (allow) defensive measures

- **Reason:**

- mitigation of the agency conflict between the shareholders and incumbent management



## The „no frustration”-rule (NFR)

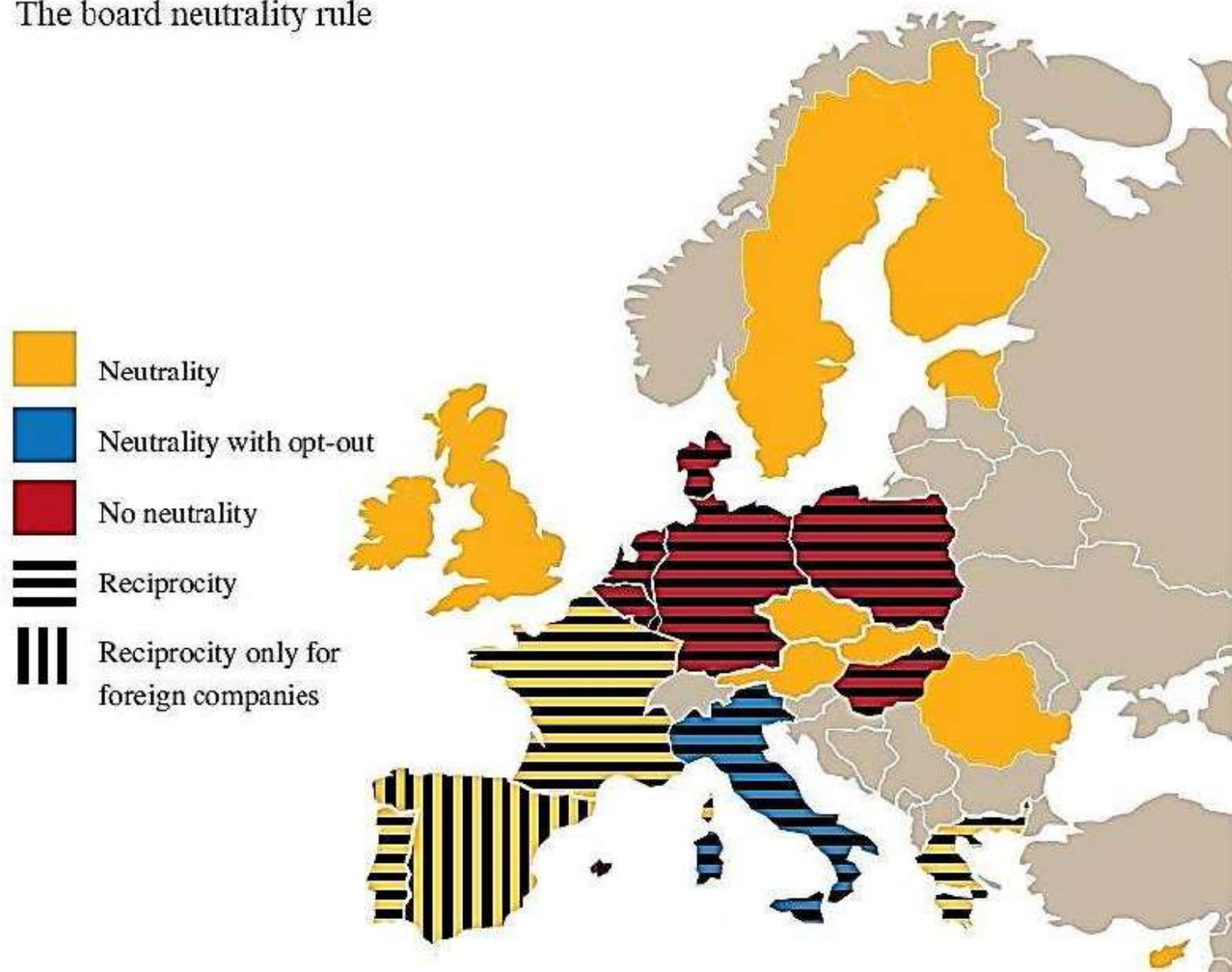
- **stronger form** (post-bid approval of defensive measures by GM required)
  - e.g. Bulgaria, Cyprus, the Czech Republic, Estonia, Finland, France (until recently), Greece, Ireland, Latvia, Lithuania, Malta, Portugal, Romania, Slovenia, the Slovak Republic, Spain, UK
- **weaker forms**
  - possible *ex ante* approval of defensive measures for a limited period pre-bid („*in abstracto*”)
    - e.g. Germany (also Japan)
  - NFR with opt-out for companies
    - Italy
- **lack of NFR** (MS opt-out, opt-in for companies possible)
  - e.g. Belgium, the Netherlands, Luxembourg, Denmark, Poland, recently also France and Austria



INSTYTUT ALLERHANDA

# The proliferation of NFR in the EU

The board neutrality rule



Source: The Takeover Bids Directive Assessment Report, 2012 at p. 197



## The „no frustration“-rule

- Actions **allowed** under the neutrality rule:
  - Shareholder information
  - Board's position, including persuasion to shareholders not to accept the bid
  - Appeal to the antitrust authorities
  - Search for a White Knight or White Squire



## Break-through rule (Article 11 TBD)

- **Meaning:**
  - elimination of certain restrictions in articles of association, by-laws, shareholder agreements and other contracts
- **Scope:**
  - elimination of any restrictions on the **transfer of shares** of the target during the acceptance period
  - restoration of the „**one-share, one-vote**“-principle for the **GM vote on the allowing of takeover defences**
  - restoration of the „**one-share, one-vote**“-principle for the **post-closing GM** to change company's articles

## Break-through rule (Article 11 TBD)

- **Nature:**
  - optional for MS
- **Implementation:**
  - only a few MS adopted (Estonia, Latvia, Lithuania)

## Reciprocity principle (Article 12 par. 3 TBD)

- **Meaning:**
  - allows companies which are subject to the „no frustration”-rule and/or breakthrough rule (by law or based on the articles of association of the company) not to apply the rule when they are confronted with a takeover bid by an offeror who is not subject to the same rule
- **Nature:**
  - optional for MS
- **Implementation:**
  - Belgium, Denmark, France, Germany, Greece, Hungary, Italy, Luxembourg, the Netherlands, Poland, Portugal, Slovenia and Spain



## Squeeze-out right

- **The rationale:**
  - to address the hold-out problem, where the minority would be likely to opportunistically refrain from accepting the bid, even a fair one with a view of *ex post* bargaining
  - to facilitate going private transactions
- **The conditions (Article 15 TBD):**
  - where the offeror holds securities representing not less than 90-95% of the capital carrying voting rights and 90% of the voting rights in the offeree company  
or
  - where, following acceptance of the bid, the offeror has acquired [...] securities representing not less than 90% of the offeree company's capital carrying voting rights and 90% of the voting rights comprised in the bid



## Squeeze-out right

- **Execution period:** three months after the expiry of the acceptance period
- **Fair price:**
  - Following a **mandatory bid**, the consideration offered in the bid shall be presumed to be fair
  - Following a **voluntary bid** the consideration offered in the bid shall be presumed to be fair where, through acceptance of the bid, the bidder has acquired securities representing not less than 90% of the capital carrying voting rights comprised in the bid.



## Sell-out right

- A **mirror image** of squeeze-out (thus reverse squeeze-out)
- **Rationale:**
  - exit right: escape from a bear hug
  - preclusion of the two-tier bid strategy
  - counter-balance to squeeze-out
- **Conditions** (Article 16 TBD)
  - **Threshold:**
    - holding between 90% and 95% of the capital carrying voting rights (in relation to the entirety of voting rights of the target company); or
    - acquiring 90% of the voting rights in the offeree (in relation to the shares subject to the bid)
  - **Time-frame:** within three months following the acceptance period



## Sell-out right

- **Fair price**

- the same form as the consideration offered in the bid or in cash. MS may provide that cash shall be offered at least as an alternative
  - following **mandatory** bid - the consideration offered in the bid shall be presumed to be fair.
  - following **voluntary** bid - the consideration offered in the bid shall be presumed to be fair where, through acceptance of the bid, the bidder has acquired securities representing not less than 90 % of the capital carrying voting rights comprised in the bid.



## Takeover bids supervision

- **MS must designate** a public authority or private body recognised by and empowered under national law to supervise takeover bids
  - **Exclusive competence** of that authority, unless:
    - junctions with other issues, such as disclosure under the Transparency Directive (e.g. FSA on CSD)
    - consideration in shares (for exchange against the target's shares) – Prospectus Directive may make the bidder's MS authority competent for this part
- **Cooperation** between supervisory authorities





## Competent authority (Article 4 TBD)

- If the company's shares are **listed in its MS of origin** → authority of the MS of origin, e.g. Italian company listed in Milan → CONSOB
- If this is not the case, then:
  - where the company's shares are **listed in MS other than its MS of origin** → authority of MS of listing, e.g. if an Hungarian company is listed only in Frankfurt → BaFin
  - where the company's shares are **listed in more than one MS other than its MS of origin** → authority of MS where the shares were first admitted to trading. If simultaneously, the company must determine the competent supervisory authority on the first day of trading

## Competent authority (Article 4 TBD)

- Scenarios:
  - **listing = seat** → Authority of that MS
  - **listing ≠ seat** → Authority of a MS of listing
  - **listing ≠ seat & multiple listings** → Authority of the MS, where the securities were first admitted to trading
  - **listing ≠ seat & multiple listings & simultaneous admission** → Authority of a MS selected by the company (issuer)



## Applicable law (Article 4(2)(e) TBD)

- Law of the **MS where the competent authority is located:**
  - **consideration** offered in the takeover bid – in particular the **price**
  - **procedural matters**
  - the provision of **information** on the bidders decision to launch a takeover bid
  - the content of the **offer document**
  - and **disclosure** of the bid
- Law of the **MS where the target company has its registered office:**
  - **company law**, in particular the **triggering control threshold**
  - any **derogation** from the obligation to launch a takeover bid
  - **takeover defences**
  - the **information** to be provided to **employees of the target company**
- Legal regime **split only, if the target is not listed in its own MS of origin**



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# US approach to hostile takeovers



## General landscape

- capital market (**equity**) financed economy
- **dispersed ownership**
- **flexible company law** (e.g. no pre-emption rights, little restrictions on share buy-backs)
- **managerial model** of corporate law, a lot of leeway for managers *ex ante*, focus on fiduciary duties – *ex post* review
- takeover law is mostly a **domain of corporate law** → **state law (Delaware)**
- Background: 1950s-60s – prevalence of **strategically abusive takeovers (two-tier offers: bid & freezeout merger)**
- **Federal and state-judicial responses**
- Recent developments

## Federal takeover law

- federal preemption: **Williams Act 1968** (add-on to US securities legislation)
  - focuses on **bid procedure** and on maximizing the **information** to and the ability of the shareholders faced with tender offers to make the best decisions with regard to the value of their shares
    - **5% disclosure** threshold
    - minimum duration of the **acceptance period** (20 business days, extension by further 20 b.days if any material change to the offer)
    - **adjustment of the price** (up) if the bidder increases the price offered for shares in the course of a bid
    - pro-rata reduction if over-subscription for the partial offers



## State law approach to takeovers

- Political economy: **Delaware** as the Mecca for incorporations → **pro-managerial bias**
- Policing takeovers: **response** of the Delaware **judiciary** to the **market failures** in corporate governance and minority protection:
  - wide acceptance for **defense strategies (poison pill)**
  - litigation culture
- ***Unocal*** test on the admissability of defensive measures:
  - the directors must have **reasonable grounds to believe that the takeover presents danger to corporate policy and efficacy of the company**
  - such **measures must be reasonable in relation to the thread** posed



## State law approach to takeovers

- auxiliary testing questions:
  - did the nature of the offer **coercively force shareholders to sell or to sell prematurely** against their best long term interests?
    - if yes – defence may be justified
  - was the **management defence unwarrantedly preclusive of the shareholders'** opportunity to exercise their **own judgment** as to what was the most valuable course of action? In particular, was it **self-interested** for the management (entrenchment) ?
    - if no – defence may be justified
- if takeover is inevitable, the directors' duties switches from protection or maintenance of the corporation as an entity into **obtaining the highest price for the benefit of the stockholders** → „managers turn into auctioneers” (*Revlon*)



## Changing context – recent developments

- Rise of **institutional investors**
    - hedge funds, pension funds, mutual funds
  - **Hedge fund** activism
  - Better coordination of shareholder actions through **proxy solicitors / proxy advisors**
  - Expansion of federal securities law e.g. on **executive compensation**
  - Growing role of **independent directors** and of the MoM-approval
- alternatives to monitoring takeovers through litigation
- **the emergence of new market mechanisms reduced the policing role of Delaware's courts as a rule maker for takeovers**

Trend: From the ***contestability of control*** to the ***contestability of influence***.



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# Creeping acquisitions



## Questions & problems of creeping acquisitions

- What are creeping acquisitions?
- What are the policy and governance problems caused by creeping acquisitions?
  - **no equal treatment** of shareholders – some may sell at a price that is still too low
  - **reduction of a prospect of future competing bids** → narrowing a chance of future participation in the control premium by the remaining shareholders
  - **risk of obtaining de facto control** by the acquirer **below the formal control threshold** → PBC
- Empirical evidence: usually the stock price goes temporarily up as a consequence of building a toehold, then it goes down below the pre-acquisition level



## Regulatory responses to creeping acquisitions

- **Mandatory disclosure** when passing a certain thresholds
  - EU: Transparency Directive (5%, 10%, 15%, 20%, 25%, 30%, 50% and 75%); MS may introduce additional thresholds;
  - US: Williams Act
- **Mandatory tender offer** (EU TBD – Art. 5)
  - „one-size-fits-all“-approach (law decides)
- **Poison pill** (US)
  - case-sensitive approach (board decides, subject to corporate governance monitoring and judicial review)



# SCHAEFFLER VS Continental

- 11 July 2008 – the CEO of **Schaeffler** (acquirer) informed the CEO of **Continental** (target) of plans to acquire 49% of **Continental's** shares. **Schaeffler** admits having a toehold of 36%.
- 14 July 2008 – **Continental** informs the public of **Schaeffler's** intentions to launch a hostile bid (→share price soars from € 55 to € 70,64)
- 15 July 2008 – **Schaeffler** confirms plans to launch a bid for all **Continental's** shares
- 16 July 2008 r. – MB of **Continental** makes a very critical statement on the offer
- Now rewind.... The **Continental's** exposure created between 25 March and 23 Mai 2008, following a derivative contract (Total Return Equity Swap) concluded by **Schaeffler** on 17 March

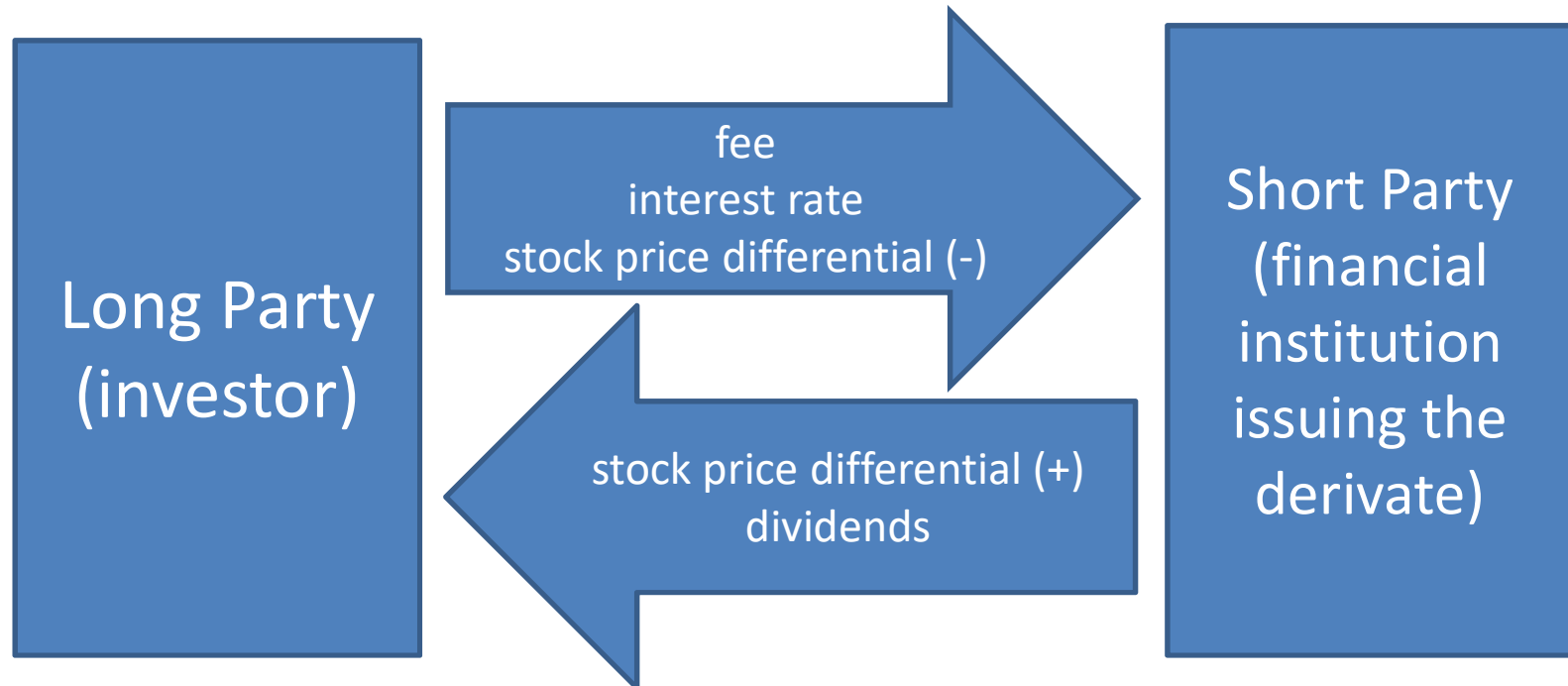
# SCHAEFFLER *VS* Continental

- **Schaeffler's** (via its subsidiary INA-Holding Schaeffler KG) position vis-a-vis **Continental**:
  - 2,97% shares (disclosure threshold: 3,00%), later increased to 3,06%
  - physically(equity)-settled swaps amounting to 4,96% (disclosure threshold: 5,00%)
  - cash-settled equity swaps amounting to approx. 28%



# equity swaps

**Total Return Equity Swap:** a derivative – a contractual arrangement by which the parties agree on a cash-flows to the effect imitating a genuine share-ownership by the long party (investor)



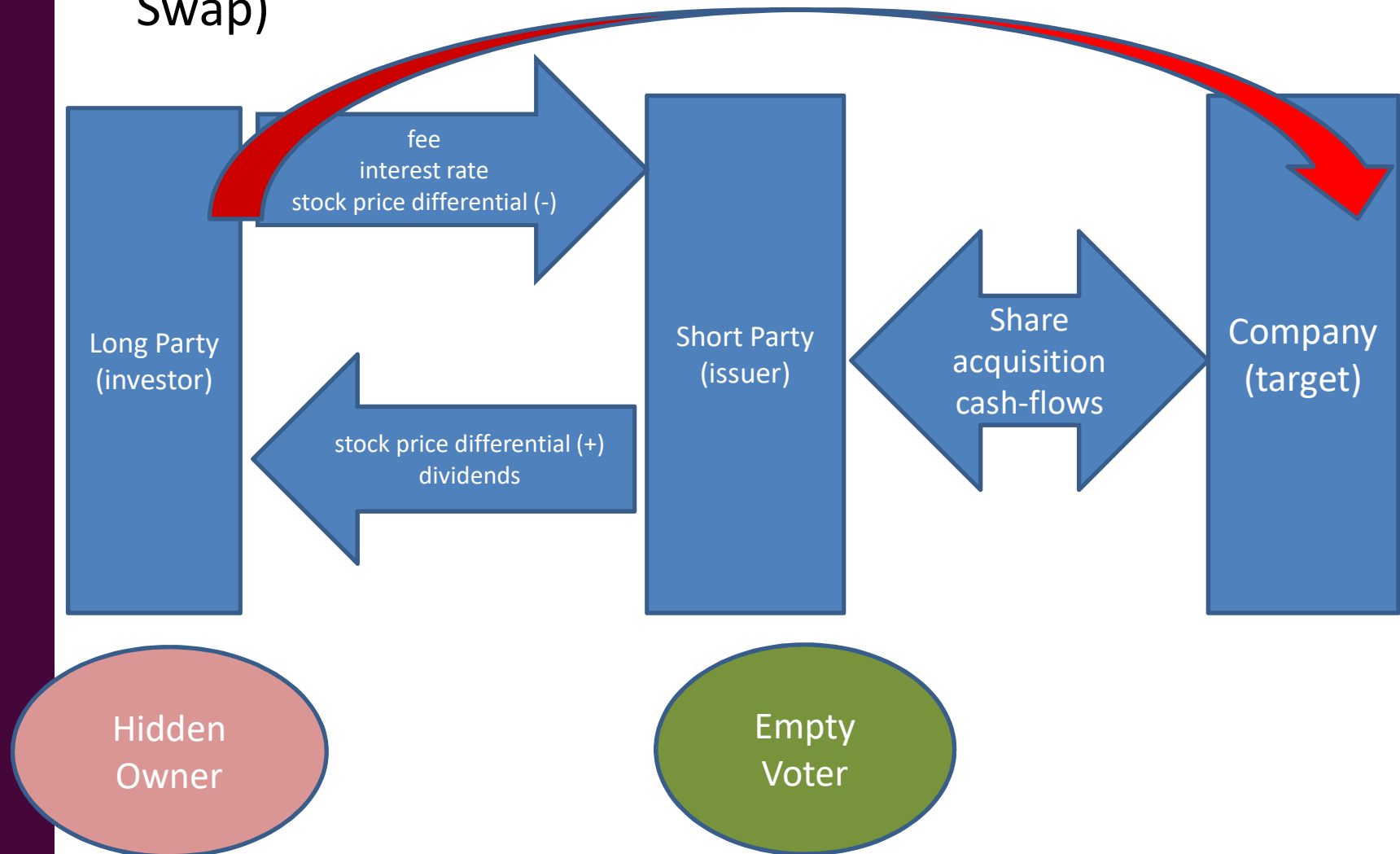
total return equity swaps

equity-settled  
derivates (ESD)

cash-settled  
derivates (CSD)

# total return equity swaps

- **Schaeffler** contracted Merrill Lynch International: issuance of derivatives by ML (Total Return Equity Swap)



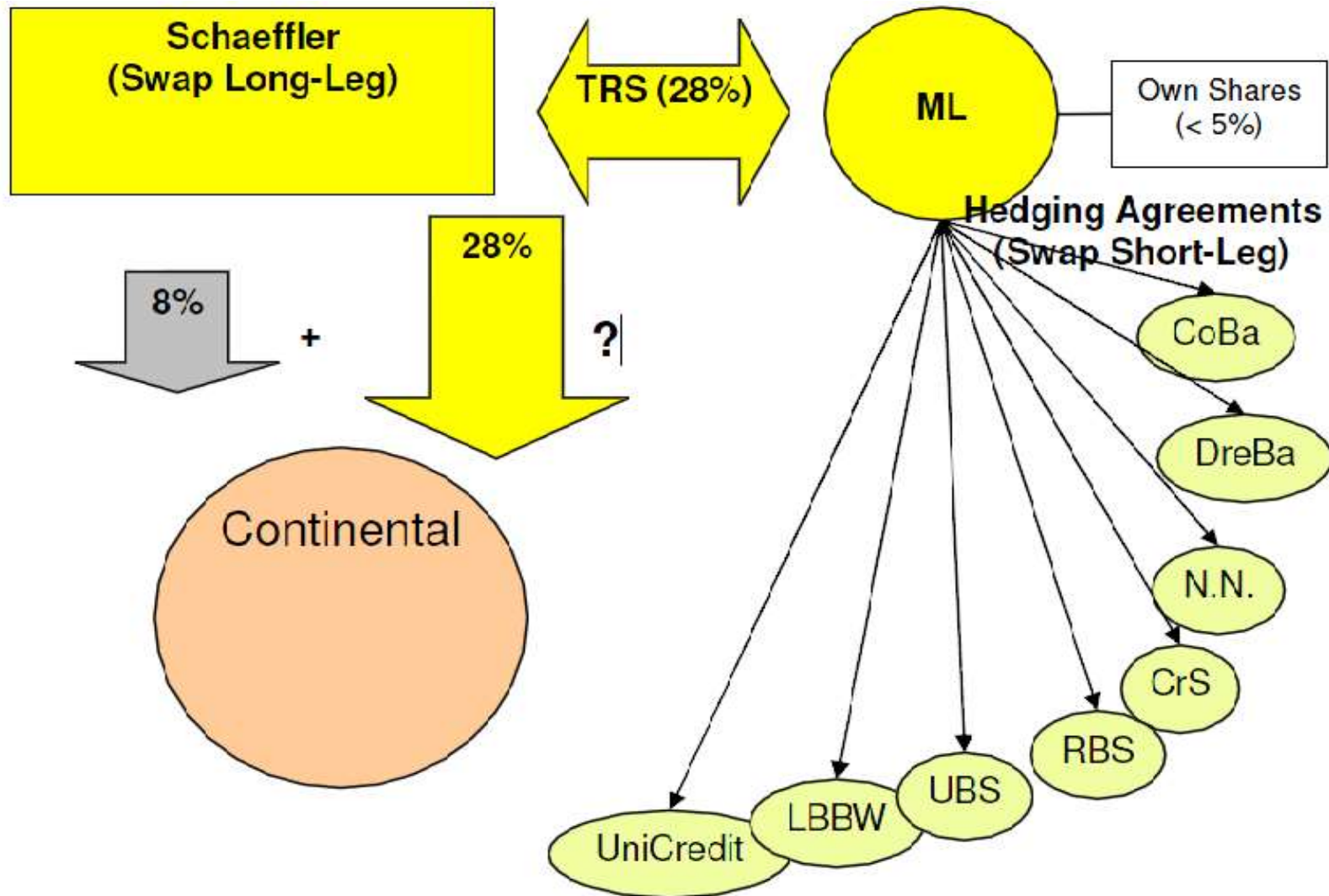




## Empty Voting & Hidden Ownership

- **Hidden (Morphable) Ownership** – where someone (acquirer) bears the economic risk equivalent to owning equity but is formally not a shareholder
- **Empty Voting** – where someone (financial institution) formally is a shareholder but without bearing the risk inherent to being a residual claimant. Empty voter is not affected by the way she votes at the GM

# SCHAEFFLER VS Continental



Source: D. Zetsche, *Continental vs. Schaeffler, Hidden Ownership and European Law – A Matter of Law or Enforcement?*, Heinrich-Heine-University Duesseldorf / Germany - Faculty of Law - Center for Business and Corporate Law Research Paper Series (CBC-RPS), No 0039 (10/2008)

# SCHAEFFLER VS Continental

## Schaeffler's strategy uncovered

1. Bank (ML) is **hedged by reverse transactions** with other financial institutions (risk neutrality)
2. The **holding** of the other financial institutions **below the disclosure threshold** (in fact they were all 2,99%(!))
3. Upon **termination of the contract**, the **financial institutions likely to sell**, so as to **avoid exposure** → Banks holding physically the shares are likely to accept the bid
4. **Schaeffler** is entitled to **unilaterally terminate** the derivative contract, and by doing so, to **trigger banks' willingness to sell**
5. If there is a **competing offer** (white knight / white squire) **Schaeffler** will gain from closing his long, cash settled position
6. It is quite **unlikely that the banks would vote against the hidden owner**, if there would be a vote in the Target's GM

# SCHAEFFLER VS Continental

## Case for regulatory intervention or for functional interpretation?

- Back then: 'Transparency Directive' (Art. 10, Art. 13) – silent on CSD.
- Implicit agreement? BaFin: no implicit agreement → no duty to disclose
- Follow-up developments: **UK, Switzerland, Germany** changed their laws to require disclosure of CSD
- Similar case in **Italy: Fiat / Ifil / Exor** – court held, there is no general duty to disclose CSD, but there was a duty upon specific request from CONSOB → fine upheld
- **2013 - amendment of the Transparency Directive:** new Art. 13(1)(a)(b):
  - *The notification requirements [...] shall also apply to [...] :*
  - *(a) financial instruments that, on maturity, give the holder, under a formal agreement, **either the unconditional right to acquire or the discretion as to his right to acquire**, shares to which voting rights are attached, already issued, of an issuer whose shares are admitted to trading on a regulated market;*
  - *(b) financial instruments which are not included in point (a) but which are referenced to shares referred to in that point and with economic effect similar to that of the financial instruments referred to in that point, **whether or not they confer a right to a physical settlement**.*
- **US: TCI vs CSX** – court held, there was a duty to disclose CSD



# **Thank you for your attention!**

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