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2018 was the year of the mega-deal, with an unprecedented number of big-ticket mergers taking place across a range of jurisdictions and sectors. In the first six months of 2018, global deal value rose by 59 per cent compared to 2017, despite volumes falling by 12 per cent. Although there was a considerable drop off in activity in the second half of the year, 2018 nonetheless saw robust overall performance by market participants, with global activity in 2018 exceeding US$3 trillion for the fifth consecutive year.

The United States remained the most targeted and acquisitive region globally in 2018; however, the deal-making landscape in the US for the remainder of 2019 presents a mixed picture. On the one hand, tax reform, a more relaxed US regulatory climate and growing cash reserves present a favourable environment for investors. On the other, dealmakers are likely to be concerned by the trade dispute between the US and China – which is already threatening economic growth and, at the time of writing, shows no sign of abating – and the ongoing uncertainty regarding antitrust policies, which may lead to increased scrutiny of M&A deals.

In Europe, after a record-breaking start to the year, the prolonged uncertainty caused by stuttering Brexit negotiations and wider political tensions across the continent finally caught up with dealmakers in the second half of 2018. In line with a softening of the global economy, the value of European deals in H2 plummeted to its lowest level since 2013, and the volume of transatlantic deals between North America and Europe also fell by 29 per cent year-on-year.

One of the main disruptors to M&A activity over the past 12 months has been the rise in political intervention in cross-border deals. In particular, concerns over national security have led to the tightening of foreign investment regimes and antitrust regulations, coupled with more active enforcement by regulators. This growth in protectionism is likely to remain one of the main obstacles facing dealmakers in the near future.

Nevertheless, looking forwards into the remainder of 2019, there is certainly cause for optimism: private equity continues to enjoy record-breaking levels of dry powder, and developments in technology are driving both the sector itself and the facilitation of deals more broadly. Finally, and perhaps most importantly, the past 12 months have highlighted the resilience of companies and private equity firms in their navigation of global political uncertainty and economic shifts.
I would like to thank the contributors for their support in producing the 13th edition of *The Mergers & Acquisitions Review*. I hope the commentary in the following 47 chapters will provide a richer understanding of the shape of the global markets, and the challenges and opportunities facing market participants.

**Mark Zerdin**  
Slaughter and May  
London  
July 2019
Chapter 1

EU OVERVIEW

Mark Zerdin

I OVERVIEW OF M&A ACTIVITY

Following on from a reasonably strong year for M&A in 2017, the start of 2018 saw high levels of activity across Europe. Indeed, the value of deals in the first half of 2018 reached €509 billion – up 16 per cent from the same period in 2017. Mega mergers were the driving force behind these record-breaking statistics, consistent with the emerging global trend towards fewer, but larger, deals. In the first quarter of 2018, six deals surpassed the US$10 billion mark – the highest Q1 deal value since the financial crisis – and, in Q2, the value of deals rose even further to €292.5 billion.

European deal-making spanned a wide range of sectors throughout 2018, but the most notable in terms of deal value was the technology, media and telecoms (TMT) sector, in which four of the top 20 deals in Europe were recorded. Most M&A activity was concentrated in the UK, which accounted for 25 per cent of total value for the first half of 2018, followed by Germany (15 per cent of value) and the Republic of Ireland (14 per cent). Particularly notable European deals included the Japanese drugs giant Takeda's £46 billion acquisition of Irish pharmaceuticals firm Shire; Comcast's high profile takeover of Sky for €42 billion; and the renewable energy deal struck by RWE, E.ON and Innogy for over €37 billion.

Nevertheless, in the face of continued geopolitical uncertainty, European M&A experienced a considerable decline in the second half of 2018. Following an exceptional start to the year, M&A activity fell suddenly by 52.8 per cent in H2. In Q4, the value of European deals dropped to US$146.2 billion – the lowest quarterly value since Q1 2013. Indeed, of the 11 deals worth over US$10 billion recorded in 2018, all were announced in the first five months of the year. Only 10 deals worth over US$5 billion were announced in H2 2018.

In 2019, M&A activity has thus far been similarly subdued. In addition to the obvious concerns arising out of the continued political and economic uncertainty, an important contributing factor to this fall in activity has been the rise of protectionism across Europe and, indeed, globally. At both Member State level and EU level there have been moves towards greater scrutiny of foreign investment in strategic assets or critical infrastructure. Earlier this year, for example, the UK updated its merger and takeover rules to give the government stronger powers of veto over foreign takeovers of certain types of technology businesses. At

1 Mark Zerdin is a partner at Slaughter and May.
2 Mergermarket, 'Scanning the horizon: European M&A Outlook 2018'.
3 Ibid.
4 Mergermarket, 'Deal Drivers EMEA 2018 Full Year Edition'.
5 Mergermarket, 'Scanning the horizon: European M&A Outlook 2018'.
EU level, there have been proposals to increase scrutiny of foreign direct investment and to create a cooperation mechanism between Member States in cases where foreign investment poses a potential threat to security.

It has not, however, been a wholly bleak affair across the board: in a bid to deploy record amounts of dry powder, private equity firms have taken centre stage over the past 12 months. In 2018, European private equity saw €170 billion in buyout deal value – the highest so far this decade. This trend looks set to continue into 2019, with private equity buyouts accounting for 29.2 per cent of all European M&A activity during the first quarter – the highest figure at this stage of the year on Mergermarket records. The top three deals thus far have all been inbound investments conducted by North American investors and consortia, such as the €5.7 billion acquisition of Scout24 by the Hellman & Friedman and Blackstone consortium.

Going into 2019, the TMT sector was the most profitable and active sector in the first quarter of the year, with buyout deals valued at €7.5 billion and 54 exits recorded. This is the first time on Mergermarket records that the TMT sector has, on a quarterly basis, surpassed the industrials and chemicals sector (which saw €6.3 billion of buyout deals and 27 exits in Q1).

The clear drop-off in M&A activity since the second half of 2018 may concern dealmakers and, with the European Central Bank ending quantitative easing and the eurozone economy entering a slower rate of growth, 2019 is unlikely to present a favourable environment for M&A activity. On top of these conditions, geopolitical uncertainty and growing protectionism will be important factors for market participants to consider before making significant investment decisions. Nevertheless, as companies learn to navigate uncertainty in Europe, it is hoped that market participants will have the confidence to remain inquisitive and acquisitive.

II RECENT EUROPEAN LAW MEASURES RELATING TO CORPORATE LAW

Brexit update

At the time of writing, there is significant uncertainty regarding the UK’s withdrawal from the European Union. On 29 March 2019, the date that the UK was originally scheduled to leave, the UK Parliament rejected the withdrawal agreement negotiated between the Prime Minister, Theresa May, and the EU for the third time. Consequently, EU leaders agreed to delay Brexit for up to six months. The revised departure date has been set for 31 October 2019, with the option for the UK to leave earlier if a withdrawal agreement is reached. At present, it remains to be seen whether a withdrawal agreement will come into force or if the UK will exit the EU without an agreement. Indeed, as political pressure for a second referendum mounts, it also possible that the UK will reverse its decision to leave.

On the assumption that the UK will ultimately leave the EU, the government has published several pieces of secondary legislation, which will come into force on exit day. The intention of this legislation is to facilitate the effective functioning of the UK’s company law framework and the operation of the UK takeovers regime on a freestanding basis outside the EU framework post-Brexit.

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6 Mergermarket, ‘EMEA MA activity during Q1 2019’.
7 Ibid.
ii  General Data Protection Regulation

As discussed in the previous edition of *The Mergers & Acquisitions Review*, the General Data Protection Regulation (GDPR) was published in the Official Journal on 4 May 2016 and, as a regulation, it has had a direct effect in all EU Member States from 25 May 2018. The aim of the GDPR is to harmonise the data protection regime across the European Union, replacing existing national laws based on the Data Protection Directive of 1995 (which is implemented in the United Kingdom through the Data Protection Act 1998). Under the GDPR, the territorial scope of the EU data protection regime will be significantly expanded to apply to any organisation that offers goods and services to individuals in the European Union (including those that are free of charge), or any organisation that monitors their behaviour. This means that a larger number of overseas businesses are likely to be affected. The GDPR also brings with it greater enforcement powers, and sanctions for non-compliance may lead to fines of up to 4 per cent of annual worldwide turnover or €20 million (whichever is greater). As under the current law, the GDPR will regulate the transfer of personal data to countries or companies outside the European Union, providing formal mechanisms to permit international data flows.

Despite the many similarities between the GDPR and the preceding Data Protection Act, companies need to ensure that their data processing systems are compliant with the new elements and enhancements introduced by the GDPR. The Information Commissioner’s Office (ICO), the UK’s data protection regulator, maintains and frequently updates a guide to the GDPR, which aims to help organisations comply with the GDPR requirements.8

After formally exiting the European Union, the GDPR will continue to apply to the United Kingdom because, as stated above, the United Kingdom intends to enact EU legislative provisions directly into domestic legislation to prevent uncertainty about the status of EU law after Brexit. Thus, the provisions of the Data Protection Bill 2017 will align the United Kingdom with the GDPR by repealing and replacing the Data Protection Act 1998.

iii  New Prospectus Regulation

On 30 June 2017, the New Prospectus Regulation9 was published in the Official Journal of the European Union; it repeals and replaces the Prospectus Directive.10 The stated aim is to lower one of the main regulatory hurdles that companies face when issuing equity and debt securities, by simplifying administrative obligations related to the publication of prospectuses but in a manner that still ensures that investors are well informed.11

One of the key changes that the New Prospectus Regulation provides for is a simplified disclosure regime for small and medium-sized enterprises and secondary issuances. For example, the reformed prospectus regime limits the inclusion of risk factors to those that are specific to the issuer of the securities and that are material to making an informed decision. Risk factors will be divided into a limited number of categories and, within each category, the most material risk factor will need to be mentioned first. The summary of the prospectus will now be limited to seven sides of A4 paper when printed, and the requirement for the format

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to consist of five tables has been removed. While the new rules still require the summary to have a uniform format, it is less prescriptive both in terms of content and structure. The increased emphasis on uniformity and materiality should also reduce the cost of accessing European capital markets.

While a handful of changes have already been implemented, the majority of the provisions of the New Prospectus Regulation and delegated acts will come into force on 21 July 2019. On 31 January 2019, ESMA published a new Q&A on the application of the Prospectus Directive and its implementing measures, which includes guidance on how the New Prospectus Regulation will apply in the event that the UK leaves the EU without a withdrawal agreement.

iv  The Fifth Anti-Money Laundering Directive

The Fifth Money Laundering Directive (MLD5)12 came into effect on 9 July 2018 and will amend the Fourth Money Laundering Directive (MLD4)13 once it has been transposed by Member States, which must be done by 10 January 2020. MLD4, and therefore also MLD5, are part of the European Commission’s proposal to strengthen the fight against terrorist financing against the backdrop of the Panama Papers revelations in April 2016 and recent terrorist attacks. They apply to a wide range of businesses: in essence, any business deemed at risk of being involved in money laundering or terrorist financing. The aim of the directive is to ‘ensure more transparency and help competent authorities to effectively detect criminal and terrorist financing flows’.14 The proposed amendments, which extend the scope of MLD4 even further, seek, among other things, to address the risks associated with prepaid cards and virtual currencies; broaden access to information on beneficial ownership; and to award further powers to financial intelligence units (FIUs), including a requirement for Member States to establish national central mechanisms allowing FIUs to better identify holders and controllers of bank and payment accounts and safe-deposit boxes.15

v  Cross-border insolvency

The EC Regulation on Insolvency Proceedings16 (ECIR) was introduced to facilitate the efficient conduct of cross-border insolvencies by, inter alia, allocating jurisdiction between Member States (excluding Denmark, which has opted out), and providing that there will only be one main insolvency proceeding. On 20 May 2015, the European Parliament approved a recast version of the ECIR (Recast Insolvency Regulation), which included changes such as extending the regulations to rescue proceedings (including debtor-led pre-insolvency proceedings); the removal of a restriction that secondary proceedings must be winding-up proceedings; and the introduction of a concept of group coordination proceedings where a group coordinator is appointed to oversee the insolvency or restructuring of a group of

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15 Practical Law Financial Services, 'Hot topics: MLD5'.
companies. The Recast ECIR came into force on 26 June 2017 and applies to proceedings that are based on a law relating to insolvency. However, it does not apply to proceedings that are based on general company law.

From a UK perspective, the impact of the Recast ECIR on acquisitions from or of insolvent companies will largely depend on the terms of the UK’s planned withdrawal from the EU. If a deal is reached and the EU withdrawal agreement comes into force, the Recast ECIR will, broadly speaking, continue during the transition period, which, unless extended, is due to run until 31 December 2020. In the event of a no deal scenario, however, the Insolvency (Amendment) (EU Exit) Regulations 2019 made on 30 January 2019 will come into force on exit day. The most significant overall effect of these regulations is likely to be that cross-border insolvency proceedings will become more complex, as proceedings started elsewhere in the EU will no longer be automatically recognised; parties will instead be required to seek permission for proceedings in each jurisdiction.

III  RECENT COMPETITION LAW DEVELOPMENTS

i  Treatment of mergers by the European Commission

Between January 2018 and the end of March 2019, the Commission received 506 merger notifications under the European Merger Regulation (EUMR). During that period, 460 cases were cleared unconditionally at Phase I. In 22 cases, Phase I clearance was conditional on certain remedies being implemented, while 14 cases were referred to Phase II for in-depth consideration. Of the seven Phase II decisions made during the period, four cases were cleared unconditionally, seven cases were given clearance conditional upon remedies being implemented and two cases were prohibited.

In February 2019, the Commission prohibited two separate transactions on the same day, namely Siemens’s proposed acquisition of Alstom and Wieland’s proposed acquisition of Aurubis Rolled Products and Schwermetall. These landmark decisions have generated considerable debate around whether the EU merger control rules should be reformed to enable the creation of ‘European champions’ in the face of increasing competition from China and elsewhere. However, Commissioner Margrethe Vestager has defended the current rules, noting that European business champions cannot be built ‘with mergers that harm competition, or by looking the other way when Europe’s businesses break our rules’.

In terms of substantive assessment, the Commission has continued to focus on the effects of mergers on longer-term innovation and competition in several cases. The Commission has identified concerns in various industries where a transaction would remove a player with significant pipeline products or R&D capabilities, or both, or where it would otherwise negatively affect innovation, including the pharmaceutical and medical devices, energy and agrochemicals sectors. The former Deputy Director of General Mergers, Carles Esteva Mosso, has emphasised that ‘innovation analysis is an important part of our merger control practice [. . .] the Commission is keen to ensure that innovation competition is not

17 Regulation (EU) 2015/848.
18 The Insolvency (Amendment) (EU Exit) Regulations 2019 (SI 2019/146).
harmed by mergers, which is a particular risk in transactions combining close and important innovators in concentrated industries with high barriers to entry and well-paced innovation processes.\textsuperscript{20}

The trend of requesting significant volumes of internal documents as part of the merger notification has also continued, particularly in respect of more complex cases. The Director General for Competition, Johannes Laitenberger, has noted that ‘internal documents are important, because they can help us understand the plans that companies have for the future and make better decisions’.\textsuperscript{21} The best practice guidelines that were announced in 2018 and intended to clarify the Commission’s approach in this area are still awaited at the time of writing.

The Commission has also continued its strict approach to ensuring compliance with the EU merger control procedures. Following the imposition of a €124.5 million fine on Altice in April 2018 for implementing its acquisition of PT Portugal prior to notifying the merger to the Commission and receiving clearance, the Commission imposed a fine of €52 million on General Electric in April 2019 for providing incorrect information about its proposed acquisition of LM Wind.

\textbf{ii} Possible reforms to the EUMR

Possible reforms to the EUMR are still under consideration following a public consultation between October 2016 and February 2017. The consultation sought to explore the potential for further simplification of EU merger control review, streamlining of the referral system between the Commission and European national competition authorities, and the introduction of complementary jurisdictional thresholds based on transaction values. These latter proposals stem from a debate about the effectiveness of the turnover-based jurisdictional thresholds in the context of some high-value transactions (particularly in the digital economy) involving target companies with limited or no turnover, which were not notifiable under the EUMR but may have had significant competitive effects in the EEA. A similar debate has occurred at the national level in the EU, and the German and Austrian governments have recently introduced additional jurisdictional thresholds relating to the transaction value, which apply as an alternative to the existing turnover-based criteria. The Commission published a summary of the consultation responses received, which showed mixed views on the proposals, in particular in relation to the proposals for new jurisdictional thresholds.\textsuperscript{22}

A separate expert report commissioned by the Commission to examine future challenges of digitisation for competition policy concluded that the merger control regime is largely fit for purpose.\textsuperscript{23} In respect of the proposals for new jurisdictional thresholds, the report suggests that the Commission should wait and assess how the new transaction value-based thresholds

\textsuperscript{20} Innovation in EU Merger Control (speech by Carles Esteva Mosso at the ABA Section of Antitrust Law Spring Meeting, Washington), 12 April 2018.

\textsuperscript{21} Enforcing EU competition law in a time of change: ‘Is Disruptive Competition Disrupting Competition Enforcement’ (speech by Johannes Laitenberger), 1 March 2018.

\textsuperscript{22} Summary of replies to the Public Consultation on Evaluation of procedural and jurisdictional aspects of EU merger control, July 2017.

\textsuperscript{23} ‘Competition Policy for the digital era’, a report by Jacques Crémer, Yves-Alexandre de Montjoye and Heike Schweitzer, April 2019.
in Austria and Germany play out in practice, and examine whether the referral system is sufficient to ensure that transactions of EU-wide relevance are ultimately analysed at the EU level.

It is unclear at this stage if the Commission will propose any legislative changes to the merger regime in response to the 2016 consultation or the 2019 expert report.

IV RECENT TAX LAW DEVELOPMENTS

It appears that the Commission is increasingly frustrated with the lack of progress on tax policy initiatives: no progress has been made on the common consolidated corporate tax base or the financial transaction tax, and the Commission’s original proposals for a digital services tax were rejected late last year (see subsection ii). Therefore, on 15 January 2019 the European Commission published a proposal to reform the decision-making process for areas of EU taxation policy by transitioning from unanimous voting to qualified majority voting at the Council level. If this proposal is agreed (which is doubted), a more dynamic approach to EU tax legislation could be expected.

i State aid

Between 10 January 2019 and 2 April 2019, the Commission opened four new state aid investigations relating to tax rulings granted by the Netherlands to Nike\textsuperscript{24} and Luxembourg to the Finnish food drink packaging company Huhtamäki,\textsuperscript{25} Danish tax support measures for the Øresundlink public infrastructure project\textsuperscript{26} and Slovakia’s turnover tax for food retailers.\textsuperscript{27} State aid investigations are therefore still a live risk.

In an M&A context, reliance on tax rulings should be scoped out during the due diligence process. One crucial question in assessing the state aid risk in respect of a particular ruling is whether the ruling reflects the law or approves a more advantageous position. While the double non-taxation of McDonald’s Europe franchising pursuant to its Luxembourg tax rulings was not state aid, given that it was not the derogation from, but the application of, Luxembourg law and the double tax treaty between Luxembourg and the US that led to the double non-taxation,\textsuperscript{28} the Commission found that Engie’s favourable treatment pursuant to its Luxembourg tax rulings did amount to state aid.\textsuperscript{29}

The Commission’s decision\textsuperscript{30} in relation to the group financing exemption under the UK controlled foreign companies regime was good news for groups with offshore finance subsidiaries of substance that are merely funded from the UK. The Commission decided that exempting finance income that would otherwise be brought into charge as a result of it being derived from UK-connected capital is not state aid. In contrast, exempting finance income that would otherwise be brought into charge as a result of it being derived from UK activity is state aid. This means that, since 1 January 2019, when the group financing exemption was tightened to exempt only the former and not the latter, it has been fully compliant.

\textsuperscript{24} Press release IP/19/322.
\textsuperscript{25} Press release IP/19/1591.
\textsuperscript{26} Press release IP/19/1468.
\textsuperscript{27} Press release IP/19/1950.
\textsuperscript{28} Press release IP/18/5831 and decision C(2018) 6076 final.
\textsuperscript{29} Press release IP/18/4228 and decision C(2018) 3839 final.
\textsuperscript{30} Press release IP/19/1948 and decision C(2019) 2526 final.
In *Heitkamp BauHolding*, the CJEU overturned a 2016 judgment of the General Court (GC), and annulled the Commission's decision that the corporate rescue exemption from the German anti-loss-buying rules constituted state aid. This is good news for those looking to invest in distressed companies. Taken together with two other recent cases where the GC annulled the Commission's state aid decisions, it also shows that the European Courts do not merely rubber stamp the Commission's decisions.

### ii Taxation of the digital economy and beyond

Base Erosion Profit Shifting (BEPS) Action 1 seeks to address the tax challenges of the digital economy. Following the publication of an interim report on 16 March 2018, the OECD published a policy note and a public consultation document in early 2019 proposing a two-pillared approach to the discussion of further reform of the international tax system. The first pillar addresses the challenges of the digital economy, setting out the following proposals: profit allocation on the basis of user participation; the allocation of income associated with marketing intangibles and their risks to the market jurisdiction; and taxation on the basis of a significant economic, rather than a significant physical, presence. The second pillar addresses remaining BEPS issues that go beyond the digital economy, discussing the introduction of an income inclusion rule under which an entity would pay tax on the income of its controlled entities or permanent establishments if such income would not otherwise be subject to tax at a minimum rate, and of an under-taxed payments rule that would deny tax deductions for payments to related parties if such payments are not subject to a minimum effective rate of tax. A public consultation on the OECD’s proposal took place in February and March 2019, and the OECD submitted a progress report to the G20 finance ministers in June 2019. The OECD’s aim continues to be a consensus-based, long-term solution in 2020.

Meanwhile, there is a growing number of countries that are taking matters into their own hands. At the time of writing, six EU Member States (namely, Austria, Belgium, France, Italy, Spain and the UK) have introduced or announced digital services taxes. In contrast, similar proposals at the EU level seem unlikely to come to fruition. The Economic and Financial Affairs Council of the EU failed to agree the European Commission’s original proposals during its meeting on 4 December 2018, and then failed to agree an amended and more limited digital services tax during its meeting on 12 March 2019.

It is further noted that on 10 March 2019, the International Monetary Fund (IMF) published a policy paper entitled Corporate Taxation in the Global Economy that addresses issues similar to those under consideration by the OECD; among other things, the IMF paper looks at minimum taxes on outbound and inbound investment. It is clear that the political desire to address perceived avoidance is still strong. In particular, the OECD’s proposals, if widely implemented, may require a reevaluation of existing group and widely used acquisition structures.

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31 Case C-203/16 P.
32 Belgian excess profit exemption cases (T-131/16 and T-263/16) and the Spanish case Futbol Club Barcelona (T-865/16).
iii Acquisition structuring

The CJEU’s judgments in the Danish conduit cases call for caution in relation to acquisition structures set up to take advantage of the exemption from withholding tax under the Interest and Royalties Directive (IRD) or the Parent and Subsidiary Directive (PID), or both. The Danish tax authority had denied the exemption in respect of dividend or interest payments from a Danish company to its intermediate parent on the basis that the recipient was merely a conduit and the actual beneficial owners were non-EU entities, and the CJEU confirmed that the benefit of the IRD and the PID must be denied if there is an abuse of rights. This would be the case in respect of structures that meet the formal conditions of the IRD or the PID, but not its purpose, and were set up with the intention of claiming the exemption from withholding tax by artificially creating the pre-condition therefor. The factors that the CJEU indicated would be taken into account in determining whether there is an abuse of rights include:

- the circumstances around the set-up of the structure;
- a quick on-payment of payments received;
- the recipient’s ability to economically benefit from, and determine how to use, the payments received; and
- the recipient’s other activities (if any).

As part of the drive to discourage aggressive cross-border tax planning, DAC6 requires intermediaries to report cross-border arrangements if they meet certain conditions. These conditions are, however, so widely drawn that they may catch arrangements that would not normally be thought of as aggressive. In this respect, a lot will depend on the terms of the national implementation legislation of which, at the time of writing, only a few countries have published drafts. In any event, potential reporting duties should be considered in respect of certain existing and any new acquisition or financing structures: while no reports have to be made before 1 July 2020, structures implemented as early as June 2018 may have to be reported.

iv Warranty and indemnity insurance

In respect of warranty and indemnity insurance for cross-border transactions, the CJEU confirmed in A Ltd v. Finland that insurance premium tax is chargeable where the policyholder (rather than the target) is located.

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33 Judgment in the joined cases N Luxembourg I (case C-115/16), X Denmark (case C-118/16), Danmark I (case C-119/16) and Z Denmark ApS v. Skatteministeriet (case C-299/16); and judgment in the joined cases T Danmark and Y Denmark ApS (C-116/16 and C-117/16).
37 Case C-74/18.
I INTRODUCTION

Expectations in the private equity industry for 2018 were not as high as for 2017. Despite this, 2018 was a record-breaking year for the private equity market, with the highest deal volume in history. Although macroeconomic factors tended to support uncertainty, private equity, as in previous years, repeatedly demonstrated its robustness, proven by its ability to cope with disruptive times of economic turbulence, political uncertainty and social upheaval, but also increased public scrutiny and regulation. However, Brexit, whose terms are still not agreed between the EU and the UK, which led to the resignation of Theresa May as Prime Minister of the UK, the trade conflict between the US and China, a slowing economy in the US, the continuing banking and economic crisis in Italy and the weak economy in some other European countries still do not allow the private equity industry to rise above its uncertainties.

As a result, there continues to be a disconnect between the number of deals and transaction volume versus the capital available and raised by investors. The bulk of capital is also supported by banks and debt funds, which are continuously hungry to lend. Furthermore, interest rates remain low, as the European Central Bank and governments pursue loose monetary policies to spur investments and growth, which is another reason for the continuous flow of capital to private equity funds.

Thus, the challenges in 2018 remained basically the same as in 2017, since the global situation has not changed significantly, with a degree of geopolitical and economic uncertainty and currency volatility: there is plenty of capital causing fierce competition between investors that chase few and even-higher-valued targets.

Preqin’s latest report on global private equity developments shows that 2018 witnessed another large amount of capital (US$432 billion) raised. With record levels of dry powder, growth of raise funds and the nearly zero interest environment, the underlying macroeconomic conditions are almost perfect for private equity investment models. However, there has even been an increase in the shortage of acquisition targets compared to 2017 to meet demands, meaning that competition for deals remains fierce. The flood of money into private equity has driven up purchase prices significantly and eliminated the formerly large gap between private and public market valuations. According to Preqin, 68 per cent of investors consider valuations to be the greatest challenge facing the private equity industry in the year ahead.3

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1 Benedikt von Schorlemer is a partner and Jan van Kisfeld is a former associate at Ashurst LLP. The authors would further like to thank research assistant Manuel Freiwald for his contributions to this chapter.
3 Id.
The industry has focused again on new concepts, as it becomes more and more difficult to realise intended returns with traditional methods. Mere financial engineering has been a thing of the past for quite some time now. Optimising the operations of portfolio companies (with the effect of longer holding periods), in particular with a focus on digitalisation, has been one of the answers to date. There is an emphasis on driving down portfolio company costs and improving margins. Continuing trends also include more buy-and-build activities.

In this environment, Germany seems to have maintained its position as the new core market for private equity in Europe. The development of the private equity market in Germany, Switzerland and Austria will continue to stand out from the market in the rest of Europe in 2018, as in the previous year. Even if the record numbers from 2016 could not be reached, when the total value of the transactions rose by 51.7 per cent to €41.3 billion, 2018 was a solid year with overall activity (buyouts and exits) of €38.3 billion.

In terms of diversification of investments, the industrial and chemicals sector continued to be top-ranked in 2018 for number of transactions. Although these sectors lost some share in 2017 and 2018 compared to the period from 2013 to 2016, they still lead in volume with a 22 per cent share. The buyout value increased slightly compared to 2013 to 2016, when the industrial and chemicals sector accounted for 16 per cent of shares, and 17 per cent in 2017 and 2018.

A notable disparity could be seen in the energy, mining and utilities sectors. The high stake of 11 per cent in value and the lower stake of 3 per cent in volume show that the transactions dominating these sectors are few in number but large in volume.

II FACTS AND FIGURES: EUROPEAN PRIVATE EQUITY IN 2018

In 2018, the European private equity market reached a post-crisis high in terms of both value and volume.

In the buyout segment, volume increased from 1,417 transactions in 2017 to 1,566 in 2018. At the same time, the overall transaction value increased from €140 billion to €175 billion. This is reflected in an 11 per cent increase in volume and a 25 per cent surge in value. Furthermore, the number of buyouts valued at more than €1 billion (47) was the highest number of mega-deals since the financial crisis. In addition, an upward trend could also be observed in the lower mid-market (between €101 million and €250 million) with an increase in deal count of 15.6 per cent. Every other deal size bracket trended downwards in 2018.

This observation is no longer paralleled by developments in the exit market, in which the number of transactions decreased from 990 in 2017 to 945 company sales in 2018, resulting in a drop in exits of 13.1 per cent on a value basis.

After a setback in 2016, in particular regarding the UK and Ireland market, caused by the uncertainty since the Brexit referendum, investors do not appear to have completely adapted to the fact that the United Kingdom is leaving the European Union: the United Kingdom and Ireland continue to dominate the European private equity market in terms of value and volume, claiming 22 per cent of the total buyout activity in 2017 and 2018 compared with their share of 23 per cent in the years from 2013 to 2016. In value terms it is notable that the United Kingdom and Ireland have dropped from 31 per cent between

5 Id.
2013 and 2016 to 23 per cent between 2017 and 2018. Despite this drop, which has mainly benefited the Nordic countries, regardless of the Brexit uncertainty, the UK and Ireland remained the leaders in terms of buyout volume.

In value terms, the United Kingdom and Ireland account for 23 per cent, the Nordic countries for 16 per cent, France for 15 per cent, Iberia for 13 per cent, Germany for 10 per cent, Italy for 9 per cent and Benelux for 8 per cent of all European buyout volume.6

In 2018, there were nine transactions in the €1 billion-plus bracket. Among those, the €4.6 billion buyout of the German energy services provider company Techem by the financial investors Partners Group together with Caisse de Depot et Placement du Quebec and Ontario Teachers’ Pension Plan from Macquarie was the biggest private equity exit in Europe in 2018.

European exit activity in 2018 was less promising. The numbers decreased in 2018 compared to the previous year with a notable drop of 4.5 per cent, falling from 990 to 945 company sales. This means that the positive trend in volume observed in recent years (with the exception of 2016, a permanent increase in volume was seen from 2013 until 2017) did not continue. One of the reasons for this development might be seen in general partners (GPs) awaiting and observing publicly listed assets, which may be undervalued in unsettled stock markets.

III SIGNIFICANT TRANSACTIONS AND KEY TRENDS IN EUROPE

i Transactions

2018 was characterised by mega-deals exceeding €1 billion. Regarding buyouts, the €101 million to €250 million bracket grew by 15.6 per cent in 2018, while the other deal size segments trended downwards. In 2017, mega-deals recaptured the European market, and in 2018, their volume reached an elevated level.

In 2018, four of the top 10 European exits were located in the UK:

a. Global Infrastructure Partners’ divestment of a 50 per cent stake in Gatwick Airport to VINCI Airports, valued at €6 billion;

b. the exit of Sky Betting and Gaming by CVC Capital Partners to The Stars Group for €4.5 billion;

c. BTG, a UK pharma group, was acquired in a public takeover for more than €4 billion by Boston Scientific; and

d. the remaining stake of 60 per cent in EMI Music Publishing was sold by Mubadala Investment to Sony Corporation for approximately €1.6 billion.

Europe’s two biggest buyouts in 2018 were:

a. valued at €10.1 billion, the purchase of Dutch chemicals group Nouryon, a specialty chemicals division of AkzoNobel, by Carlyle Group and Singaporean sovereign wealth fund GIC; and

b. the buyout of the majority of Recordati, an Italian pharmaceuticals group valued at €6.3 billion, by CVC Capital Partners, Public Sector Pension Investment Board and Stepstone Group.

6 Id.
Key trends

As in 2018, the market concentrated on finding suitable assets, fee structures and compliance with tightening regulatory requirements on both sides of the Atlantic. Trends observed in previous years are still valid, including longer holding periods, extended buy-and-build activities, the application of warranty and indemnity (W&I) insurance policies and trading in secondaries.

Typically, private equity funds hold their portfolio companies for three to five years on average before exiting. This holding period has increased in small steps, reaching an average of six years in 2014. One of the reasons for these longer holding periods is macroeconomic stagnation and the uncertainty caused by the financial crisis that began in 2008. In 2017, the median holding period returned to a new normal of five years. Parallel and in line with the observed trend to longer holding periods are continuous buy-and-build activities, which are used to increase potential exit returns. This corresponds with the increasing number of add-ons, which funds can use to execute buy-and-build strategies. For several years, the number of add-on deals globally increased notably, and they make up around half of all deals today. On the other hand, quick flips (i.e., transactions with a holding period of up to three years) have decreased in the past few years. In 2008, at 44 per cent, nearly half of all buyouts were quick flips. More recently, the number has retreated by half to around 20 per cent. This sharp drop in quick flips is a result of factors such as high prices, limited future market beta and tax reform in the United States, under which carries generated from investments held for a maximum of three years will be taxed at the higher ordinary income rate. These factors make it rather unlikely that quick flips will experience an upswing in the foreseeable future, but rather indicate the continuous trend to longer holding periods.

A further trend is the growing use of W&I insurance policies in transactions, which are now standard in certain sectors, in particular for private equity transactions where purchasers require protection against deal risks and sellers look for a clean exit and an increased internal rate of return, all of which can be achieved with W&I insurance. Under these insurance policies, (usually) the buyer insures against the risks occurring in cases of a breach of the representations and warranties or indemnities that are given in a sale and purchase agreement. Damage claims incurred as a result of a breach of a representation and warranty or indemnity are paid by the insurance company (which, apart from certain exceptions, may not turn towards the seller), subject to the terms and conditions of the policy including baskets and caps as agreed. The bulk majority of W&I insurance policies are issued to buyers. Thus, W&I insurance significantly reduces the risks of sellers to become liable for damage claims under a sale and purchase agreement. As a result of the market entry of a number of new players and the intense competition among insurers, prices for insurance coverage have fallen drastically. This trend, which began in recent years, also continued in 2018. The average premiums for W&I policies in 2018 fell to 0.6 to 0.9 per cent of the insured sum for real estate transactions, and 0.8 to 1.5 per cent of the insured sum for corporate deals. In addition to standard W&I policies, special contingent policies covering already known risks (which are usually excluded) are also more and more common, and certainly at much higher premiums. The demand for W&I policies is still growing globally. Lower average premiums, lower retention levels and new insurers entering the market are the reasons for this development, resulting in continued fierce competition among W&I insurers.

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8 Id.
IV  LEGAL FRAMEWORK FOR PRIVATE EQUITY FUNDS IN GERMANY AND EUROPE

i  Legal form of private equity fund vehicles in Germany

The legal framework for private equity funds has not changed significantly in recent years. The biggest change on the regulatory side was introduced through the transformation of the Alternative Investments Fund Managers Directive (AIFMD) into national law. For this purpose, Germany established the Investment Code (KAGB), which came into effect on 22 July 2013. As to the legal form of vehicles, German (corporate) law offers various types. Generally, vehicles for funds can be organised in the legal form of a stock corporation (AG), a limited liability company (GmbH) or a form of a limited partnership (GmbH & Co KG). Furthermore, the KAGB provides variations of the AG and the limited partnership (KG), the investment-AG or investment-KG, introducing additional regulations. Generally, the legal form now depends on a specific fund’s concept with regard to the invested assets of an open or closed-end fund and its circle of investors.

From a practical standpoint and an investor’s tax perspective, the limited partnership in the form of a GmbH & Co KG still prevails for German private equity funds. The KG essentially has two kinds of partners: limited partners (LPs) and GPs. While investors subscribe for limited partnership interests, thus becoming LPs, the sole GP of a limited partnership is a separate company usually organised as a limited liability company in accordance with the Limited Liability Company Act. With the combination of these two legal forms, investors combine the advantages of both. In particular, the personal liability of investors is limited to their liability contribution, as LPs are only liable for debts of the limited partnership up to the liability amount registered with the German commercial register. Since German law does not require a minimum liability amount, usually only a small portion of the actual capital commitment of an LP is registered with the commercial register as liability amount, and as such revealed to the public. Once an LP has fulfilled his or her obligation up to the respective liability amount, and has not received a repayment in the meantime, the LP does not assume any further responsibility for the liabilities of the limited partnership. In contrast to LPs, a GP of a limited partnership is liable for all obligations of the partnership without limitation. In a GmbH & Co KG, the liability of the GP (as a limited liability company) is limited to the assets of the company. Its shareholders cannot be held liable for more than the capital contribution paid (or owed) by the respective shareholders.

Furthermore, based on the principle of freedom of contract, the partnership agreement can be tailored in a very flexible way to the needs and objectives of the investors. In general, investors as LPs only have limited information rights compared to other legal forms unless broader information rights have been agreed upon in the partnership agreement. The entry and exit of investors in and out of a GmbH & Co KG are also simple and do not require a notarial form. Thus, the accession of a new investor as a LP is uncomplicated and cost-efficient. In addition, there are beneficial tax rules if a GmbH & Co KG as a limited partnership is not engaged in business activities for German tax purposes. Last but not least, the limited partnership agreement does not have to be revealed to the public, and in particular does not have to be registered with the German commercial register.
ii Monitoring of private equity funds in Germany

According to the KAGB, alternative investment fund managers are now obliged to establish a depositary for alternative investment funds (AIFs) under their management. This depositary shall, inter alia, review legal title in an AIF’s assets on a continuous basis. The depositary’s obligation is not limited to holding companies, but applies to all subsidiaries in the case of a holding structure within the portfolio. Additionally, the depositary may not solely rely on an AIF’s due diligence, but is requested to also conduct its own review.

iii Transactions

Types of private equity transactions

The typical private equity transaction structure has not changed significantly in recent years. From a legal standpoint, the acquisition of interests or shares remains the most important type of transaction, in most cases, of a private equity transaction in the form of a leveraged buyout (LBO). In an LBO, usually all or the majority of interests of the target company are acquired by the private equity investor, although the acquisition is funded only fractionally with equity, while the larger portion of the purchase price is financed with bank or other third-party debt (leveraged transaction). The leverage shall be defrayed by the free cash flow of the target company.

Disclosure requirements

Under German law, several acts deal with disclosure obligations that apply to all shareholders and investors, and thus also for private equity investors. The most relevant disclosure obligations relate to stock corporations, and in particular listed companies. The German Securities Trading Act (WpHG) sets forth various thresholds for equity holdings in listed companies that trigger certain disclosure requirements, while the German Stock Corporation Act (AktG) governs all companies organised as a German stock corporation. According to the WpHG, everyone reaching, exceeding or falling short of 3, 5, 10, 15, 20, 25, 30, 50 and 75 per cent of the voting rights in a listed company by purchase, sale or any other means is obliged to notify both the company and BaFin, the German Federal Financial Supervisory Authority. The same obligations apply for persons who act in concert.

To capture all sorts of arrangements to build up positions in a German listed company, the German legislator has also extended the disclosure requirement for financial instruments by including other instruments that do not necessarily qualify as financial instruments but grant the right to acquire voting shares or to vote such shares.

To restrict undesired activities – in particular by financial investors – the WpHG enhanced, in a similar way to respective provisions under the US Securities Exchange Act, the transparency of certain financial transactions obliging an investor to disclose its specific intentions with the target company and the sources of the funds to finance the transaction. Thus, an acquirer of an essential participation (i.e., a participation reaching or exceeding a threshold of 10 per cent of the voting rights) is, subject to certain exemptions, required to disclose the aforementioned information regarding the purpose of the transaction and the origin of funds.

Concerning stock corporations (whether listed or not), the AktG sets forth that any enterprise (private investors are not subject to this obligation) is obliged to promptly notify the stock corporation regarding the following: reaching a threshold of more than 25 or 50
per cent in the capital of a stock corporation, or whenever the enterprise falls below these thresholds. If the enterprise fails to fulfil its disclosing obligations, it will lose its rights rooted in its shares.

To make the shareholder structure of non-listed stock corporations more transparent, the AktG limits the admissibility of bearer shares. This amendment came into effect on 31 December 2015. Since then, non-listed stock corporations may generally only issue registered shares.

On a European level, besides the above-mentioned implementation of the AIFMD into German law and the additional provisions introduced in the KAGB, the industry is facing further legal regime changes. Solvency II (adopted by the European Parliament on 11 March 2014) created new insurance regulations as of 1 January 2016 that require insurance companies to hold more liquid assets, restricting the amount that can be invested in private equity. The Markets in Financial Instruments Directive II (MiFID II), the update of the MiFID, was adopted by the European Parliament in April 2014 and published in June 2014 after its formal adoption by the Council of Ministers. In addition, the European Commission resolved on a revision of the EU Pension Funds Directive (IORP) – IORP II – which had to be transformed into national law by January 2019 (the corresponding implementation act in Germany came into force in January 2019) and which has far-reaching consequences for both the funding of pension schemes and the way they are managed.

V OUTLOOK

The sentiment in the private equity industry is rather characterised by optimism for the development of the private equity market in Europe in 2019. More than half (56 per cent) of private equity houses expect the European deal market for private equity to get slightly better in 2019, while 35 per cent of respondents assume it will stay broadly the same. This compares with only 7 per cent of firms anticipating that it will get slightly worse. German private equity firms are distinctly above the average in terms of optimism: 70 per cent of them expect a slight improvement, and only a tiny minority of 5 per cent expect a slight deterioration. The Benelux countries are confident about the development of the private equity market in Europe in 2019 as well: 58 per cent expect the situation to get slightly better in 2019, although a significant 13 per cent of respondents expect it to get worse.

On the whole, investors remain optimistic that Europe will still be a region for investments that have high potential in 2019. Most European countries still offer a high grade of legal certainty in a stable environment, which continues to be an essential argument for future investments. However, there are record levels of dry powder now exceeding US$2 trillion and leverage in the global private equity market, caused by the huge amounts of money successfully raised in recent years, which means that deals have never been more

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10 The following survey results are based on a survey conducted by Mergermarket's research and publication division on behalf of PwC, who spoke to 250 private equity principals in Europe.
11 See footnote 4.

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expensive. This has resulted in fierce competition among private equity investors.⁰¹³ All private equity firms expect competition for investments to remain the same or to increase in 2019, with 29 per cent believing competition will rise significantly and 44 per cent that it will increase slightly.⁰¹⁴ In addition, more competitors from outside the industry, such as pension funds, family offices and insurance companies, are developing a taste for the private equity model, which increases competition. Furthermore, additional players such as Chinese investors are becoming more and more established in the market, although the competition for deals from Chinese investors is not expected to increase but to stay broadly the same in 2019.⁰¹⁵ In light of the above, investors will most likely be pulled into fierce competition, and private equity houses are well advised to analyse pricing even more carefully.

Despite a very solid investment environment in Europe and investor confidence seen in the public market, certain risks should not be disregarded, with the following being some examples: the more critical outlook regarding economic developments in many regions of the world, including the trade conflict between the US and China and the US’s policy of increased protectionism; as well as the never-ending Brexit struggle that finally resulted in Theresa May stepping down as the United Kingdom’s Prime Minister. The impact of Brexit is mirrored in a survey by PwC in which 45 per cent of respondents stated that Brexit makes the UK a less attractive destination for investments in 2019.⁰¹⁶

Given the uncertainties in the market, private equity funds will have to closely analyse any possible scenarios for each investment. Nevertheless, the bottleneck of investment opportunities with a fierce price competition as a consequence will, in our view, continue to be one of the main limiting factors of the private equity industry in 2019.

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¹³ PwC Private Equity Deals Insights 1Q 2019.
¹⁴ Id.
¹⁶ See footnote 4.
M&A litigation has evolved dramatically in recent years. There has been further development of substantive doctrines under Corwin and MFW (discussed further in Sections II and III, respectively), which provide defendants with strong bases for dismissing many complaints. At the same time, more Section 220 ‘books and records’ actions have been filed as a means for stockholders to obtain pre-lawsuit discovery in order to plead a complaint that may stand a stronger chance of withstanding a motion to dismiss (discussed in Section IV).

Delaware also continues to see a number of M&A cases that are not filed by stockholder plaintiffs (discussed in Section V). For example, the Delaware courts recently held that a buyer properly invoked a material adverse effect (MAE) clause to terminate a merger agreement – the first decision so holding in Delaware. CBS’s recent proposal to dilute the Redstone family’s controlling stake in CBS in response to a perceived threat that the Redstones were going to force a merger between CBS and Viacom (which is also controlled by the Redstones) also played out in the Court of Chancery. That case led to interesting decisions on the availability of preliminary injunctive relief and attorney–client privilege before it settled.

Meanwhile, the Delaware Supreme Court has issued several key rulings on appraisal issues and continues to provide further guidance on appraisal rights (discussed in Section VI).

II POST-CLOSING DAMAGES CLAIMS: THE CORWIN DEFENCE

As we have written in previous versions of this chapter, the Delaware courts have underscored the deference afforded to merger transactions approved by a fully informed, disinterested and uncoerced stockholder vote. In Corwin v. KKR Financial Holdings, the Delaware Supreme Court unanimously held that arms-length transactions (i.e., ones that do not involve a controlling stockholder on both sides of the deal, as in a minority buyout) approved by a fully informed, uncoerced vote of a majority of the disinterested stockholders will be reviewed under the deferential business judgment rule.2

Since Corwin, the Court of Chancery has repeatedly dismissed post-closing challenges to non-controller stockholder-approved transactions at the pleading stage of the litigation.3

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1 Roger A Cooper and Meredith Kotler are partners and Mark McDonald and Vanessa C Richardson are associates at Cleary Gottlieb Steen & Hamilton LLP.

2 Corwin v. KKR Financial Holdings, 125 A.3d 304, 305-06 (Del. 2015).

3 See, e.g., In re Cyan, Inc Stockholders Litig, C.A. No. 11027-CB, 2017 WL 1956955 (Del. Ch. 11 May 2017); In re Paramount Gold & Silver Corp Stockholders Litig, C.A. No. 10499-CB, 2017 WL 1372659 (Del. Ch. 13 Apr 2017); In re Columbia Pipeline Group, Inc Stockholders Litig, C.A. No. 12152-VCL (7 Mar 2017)
Subsequent decisions clarified that Corwin applies to two-step mergers under Section 251(h) of the Delaware General Corporation Law (DGCL) (involving a tender offer followed by a short-form merger), and that the fully-informed, uncoerced and disinterested stockholder vote extinguishes all claims relating to the merger, including aiding and abetting claims against third parties.

However, some limits on the Corwin doctrine have emerged. First, the Court of Chancery has cautioned that this cleansing effect will apply only when the stockholder vote is not coerced.

Second, the stockholder vote also must be fully informed. In Appel v. Berkman, Chief Justice Strine wrote for the Court that the failure to disclose that the founder, largest stockholder, and chair of the target privately told the board that, in his view, ‘it was not the right time to sell the Company’, meant that the stockholders’ vote on the deal was not fully informed. In Morrison v. Berry, Justice Valihura wrote for the Court that the failure to disclose ‘troubling facts regarding director behavior’ in negotiating the deal, which ‘would have helped [stockholders] reach a materially more accurate assessment of the probative value of the [company’s] sale process’, precluded Corwin-cleansing in that case. The Court emphasised that plaintiffs were not required to allege that the information, if disclosed, would have made a reasonable stockholder less likely to approve the deal; rather, it was enough to plead that ‘there is a substantial likelihood that a reasonable stockholder would have considered the omitted information important when deciding whether to tender her shares or seek appraisal’.

Recent Court of Chancery opinions have continued to emphasise these points. For example, in In re Xura, Inc Stockholder Litigation, Vice Chancellor Slights held that claims against a CEO were not cleansed by the stockholder vote because alleged material facts purportedly showing his conflicted role in negotiating the transaction were not disclosed.

In re T angoe, Inc Stockholders Litigation, Vice Chancellor Slights held that claims against the target board were not cleansed by the stockholder vote because, among other things, allegedly material facts concerning an ongoing restatement process were not disclosed. In re PLX Technology Inc Stockholders Litigation, Vice Chancellor Laster held that claims against
an activist investor for aiding and abetting a target board’s breaches of fiduciary duty were not cleansed by the stockholder vote because alleged material facts bearing on a potential conflict of interest between the activist investor and the target’s remaining stockholders were not disclosed (in that case, however, the Court went on to find that the plaintiffs had failed to prove damages because there was no competent evidence the intrinsic value of the target exceeded the deal price).⑫

Of course, notwithstanding these decisions, Corwin remains a powerful tool for defendants in post-closing damages litigation. Indeed, because of the significance of Corwin-cleansing, boards are routinely advised to disclose all conceivably material facts to their stockholders before they vote on a deal.

III CASES INVOLVING CONTROLLING STOCKHOLDERS

As explained in previous versions of this chapter, until 2014, all controlling stockholder buyouts were evaluated under the onerous entire fairness standard regardless of the procedural protections used in the deal process. That changed with the Delaware Supreme Court’s decision in Kahn v. M&F Worldwide Corporation, commonly referred to as MFW, which held that the business judgment rule (not entire fairness) will apply if the controlling stockholder buyout is expressly conditioned ab initio on the approval of a special committee of the independent directors and approval of a majority of the disinterested stockholders (the dual approval conditions).⑬

In October 2018, in Flood v. Synutra International, Inc, the Delaware Supreme Court clarified that the ab initio requirement is satisfied as long as the dual approval conditions were in place before the onset of substantive economic bargaining, even if they were not included in the controller’s initial offer.⑭ Further, in April 2019, in Olenik v. Lodzinski, the Delaware Supreme Court further clarified the line between preliminary discussions – which may be conducted before MFW’s dual protections are put in place without forfeiting the ability to invoke the business judgment rule under MFW – and substantive economic discussions, which may not be.⑮ There, the parties had engaged in a joint valuation exercise in the months before the controller conditioned its offer on the dual protections, and the Court found it was ‘reasonable to infer that these valuations set the field of play for the economic negotiations to come’, an inference that was further supported by the fact that, as alleged in the complaint, the offers that were subsequently made and ultimately accepted were close to the ‘indicative valuations’ that had been presented several months earlier.⑯

This framework also has been extended by the Court of Chancery beyond the controller buyout context. In In re Martha Stewart Living Omnimedia, Inc Stockholder Litigation, the controlling stockholder was a seller to a third party along with the minority stockholders, but the plaintiffs alleged that she received greater consideration for herself than the minority

⑫ In re PLX Technology Inc Shareholders’ Litig., 2018 WL 5018353 (Del. Ch. 16 October 2018), aff’d, No. 571, 2018, 2019 WL 2144476, at *1 (Del. 16 May 2019).


⑯ Id. at *9.
In such case, the Court found that the business judgment rule would apply under *MFW*, as long as the dual approval protections were in place at ‘the point where the controlling stockholder actually sits down with an acquirer to negotiate for additional consideration.’

### IV RISE OF BOOKS AND RECORDS ACTIONS UNDER SECTION 220

In part in response to *Corwin* and *MFW*, which raised the bar for plaintiffs in post-close damages actions to plead facts to survive a motion to dismiss, there has been a recent uptick in stockholder inspection demands under Section 220 of the DGCL, and actions brought in the Court of Chancery to compel the production of books and records pursuant to Section 220(c). In the past year, some plaintiffs have used documents obtained in this way to plead a post-close damages complaint that survived a motion to dismiss, including in the *Appel* case discussed above.

In several recent decisions, the Delaware Supreme Court has held that Section 220 may entitle stockholders to more than just minutes and other formal board materials, but only to the extent such formal materials are insufficient to satisfy the stockholder’s proper inspection purpose. For example, in *KT4 Partners LLC v. Palantir Techs Inc*, the Court explained that ‘if a company . . . decides to conduct formal corporate business largely through informal electronic communications [rather than through formal minutes and resolutions], it cannot use its own choice of medium to keep shareholders in the dark about the substantive information to which Section 220 entitles them’. However, the Court emphasised that this ‘does not leave a respondent corporation . . . defenseless and presumptively required to produce e-mails and other electronic communications. If a corporation has traditional, non-electronic documents sufficient to satisfy the petitioner’s needs, the corporation should not have to produce electronic documents.’

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18 Id. at *19.
19 DGCL § 220(c) (‘If the corporation . . . refuses to permit an inspection sought by a stockholder . . . or does not reply to the demand within 5 business days . . . , the stockholder may apply to the Court of Chancery for an order to compel such production. The Court of Chancery is hereby vested with exclusive jurisdiction to determine whether or not the person seeking inspection is entitled to the inspection sought.’).
20 *Appel*, 180 A.3d at 1059 (noting plaintiff served Section 220 books and records demand before filing his post-closing damages suit). Notably, the material fact that the Delaware Supreme Court found was not disclosed in that case came from the target board’s minutes. Id. at 1057 & n.1.
21 *KT4 Partners LLC v. Palantir Techs Inc*, No. 281, 2018, 2019 WL 347934, at *2 (Del. 29 Jan 2019); see also *Inter-Local Pension Fund GCC/IBT v. Calgon Carbon Corp*, C.A. No. 2017-0910-MTZ, 2019 WL 479082 (Del. Ch. 25 January 2019) (holding that a stockholder had proper purpose to inspect records, and that the stockholder was entitled to emails because they were necessary and essential for that purpose); *Schnatter v. Papa John’s Int’l, Inc*, C.A. No. 2018-0542-AGB, 2019 WL 194634 (Del. Ch. 15 January 2019) (noting that ‘[a]lthough some methods of communication (e.g., text messages) present greater challenges for collection and review than others . . . the utility of Section 220 as a means of investigating mismanagement would be undermined if the court categorically were to rule out the need to produce communications in these formats’).
22 *KT4 Partners* at *12.
V  M&A LITIGATION WITHOUT STOCKHOLDER PLAINTIFFS

i  Broken deal litigation

In *Akorn, Inc v. Fresenius Kabi AG*, the target (Akorn) sought to compel the buyer (Fresenius) to close on its acquisition of Akorn, while Fresenius sought a declaration that it had properly terminated the merger agreement based on the occurrence of an MAE.\(^{23}\) After expedited discovery and trial, Vice Chancellor Laster concluded that an MAE had occurred, and thus Fresenius had validly terminated and was not required to close. That decision was affirmed by the Delaware Supreme Court.\(^{24}\)

*Akorn* is the first Delaware decision to release an acquirer from its obligation to close a transaction as a result of the occurrence of an MAE. Before *Akorn*, Delaware decisions had required acquirers to close, often despite a significant diminution in a target's value. However, the Court of Chancery's detailed recitation of the unusual facts of that case attest to the fact that MAEs remain difficult to establish, even after *Akorn*. Nonetheless, *Akorn* may embolden parties to litigate such cases in the future, where before the lack of precedent for finding an MAE may have discouraged them.

In *Vintage Rodeo Parent, LLC v. Rent-a-Center, Inc*, the Delaware Court of Chancery found that a target company properly terminated the merger agreement following the passage of the specified end date where the buyer failed to exercise its right under the agreement to give notice that it wished to extend the end date.\(^{25}\) The Court further determined that there was no implied duty to warn a counterparty of a mistake, and that an obligation to use commercially reasonable efforts to consummate a merger does not preclude exercise of an express right to terminate the merger agreement.\(^{26}\) The Court, however, requested additional briefing regarding the enforceability in this context of the US$126.5 million reverse termination fee to which the target claimed to be entitled, which constituted 15.75 per cent of the equity value of the transaction (the case settled before that issue was decided). The decision was a stark reminder that courts will strictly enforce the terms of a merger agreement as written, and that failure to comply with seemingly ministerial formalities can have severe consequences.

ii  CBS/Redstone case

One of the most extraordinary Delaware cases in recent memory, *In re CBS Corporation Litigation*, led to two notable decisions from the Court of Chancery before it settled shortly before trial.

In that case, a special committee of the CBS board of directors called a special meeting of the full board on 14 May 2018 (to take place three days later, on 17 May) to consider and vote on a stock dividend intended to dilute the voting control of National Amusements, Inc (NAI), a company owned by the Redstone family who, by virtue of CBS's dual class structure, owns approximately 10 per cent of CBS's common stock and 80 per cent of its


\(^{26}\) Id.
voting power. The special committee and CBS simultaneously filed a lawsuit against NAI in the Court of Chancery seeking approval of such dividend, alleging that it was necessary to prevent the supposed threat that NAI would remove CBS directors to force an allegedly unfair merger with Viacom, of which NAI is also the controlling stockholder. CBS also immediately moved for a temporary restraining order (TRO) to prevent NAI from taking action to protect its controlling stake until the board had a chance to approve the proposed dividend at the special meeting.

Before a hearing on the TRO motion on 16 May, NAI (which had no prior notice that the CBS special committee was considering such a drastic step) exercised its right to amend CBS’s by-laws by written consent to require, among other things, that any dividend be approved by at least 90 per cent of the CBS directors. Because three of the 14 CBS directors were affiliated with NAI, these by-law amendments likely would preclude the declaration of the dilutive dividend.

After an expedited briefing and a hearing on 16 May, the Court of Chancery denied CBS’s request for a TRO on 17 May, the day of the special meeting. In so ruling, the Court resolved an ‘apparent tension’ in the law between, on the one hand, past decisions suggesting the possibility that a board might be justified in diluting a controlling stockholder in extraordinary circumstances (arguably implying that, in such circumstances, the board should be permitted to act without interference by the controlling stockholder) and, on the other, cases recognising the right of a controlling stockholder to have the opportunity to take action to avoid being disenfranchised. The Court found the well-established right of a controlling stockholder to take measures to protect its voting control ‘weigh[ed] heavily’ against granting a TRO that would restrain it from doing so, and that ‘truly extraordinary circumstances’ would therefore be required to support such a TRO. At the same time, the Court noted that it had the power to review and, if necessary, set aside any such action taken by the controlling stockholder after the fact (itself another reason why a TRO in these circumstances was not warranted).

A second decision issued by the Court of Chancery in this case arose from a privilege dispute during discovery. Among other things, NAI argued that, because the three NAI-affiliated members of the CBS board were joint clients of CBS’s counsel (i.e., in-house and outside counsel representing the full board, not the special committee specifically), NAI was entitled to unfettered access to privileged communications with such counsel made prior to the filing of CBS’s complaint on 14 May. CBS, however, took the position that the NAI-affiliated directors were adverse to CBS management and other board members with respect to certain issues even separate from the proposed merger with Viacom (which the special committee was formed to consider) and prior to the commencement of the litigation. For example, CBS’s outside counsel filed an affidavit acknowledging that it had advised certain members of CBS management and the board (unaffiliated with NAI) about ‘the options available to CBS in dealing with its controller’ over many years.

In ruling on this issue, Chancellor Bouchard first held that, because the NAI-affiliated directors were joint clients of CBS’s counsel, under existing Delaware jurisprudence they

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28 Id. at *6.
29 Id. at *5.
had the right to unfettered access to legal advice rendered by such counsel absent an *ex ante* agreement among the parties, the formation of a special committee or ‘sufficient adversity’ between the director and the corporation ‘such that the director could no longer have a reasonable expectation that he was a client of the board’s counsel’.31 The Court determined that, as a result of the formation of a special committee by the CBS board of directors to consider the potential merger with Viacom, the NAI-affiliated CBS directors were not entitled to privileged communications with company counsel relating to the special committee’s mandate. The Court held, however, that the NAI-affiliated directors were entitled to communications with company counsel that were unrelated to special committee matters, finding that ‘no factual basis has been identified to support the conclusion that the NAI Affiliated Directors were made aware (or reasonably should have been aware) that CBS Counsel was not representing them jointly with the other CBS directors with respect to any matter other than the matters falling within the purview of the Special Committees for which CBS Counsel provided assistance’.32 This decision shows that mere adversity between directors is not sufficient to exclude some directors from privileged communications with board counsel; rather, such adversity must be made manifest to the directors who are excluded.

**VI FALL OF APPRAISAL ARBITRAGE**

Section 262 of the Delaware General Corporation Law provides stockholders with the right to demand a judicial appraisal of the fair value of their stock.33 To exercise appraisal rights a stockholder must:

- deliver a written demand prior to the vote;
- not have voted in favour of the transaction;
- continuously hold the stock through closing; and
- perfect appraisal rights after closing.34

The past decade has been marked by a notable increase in statutory appraisal filings in Delaware, driven by the appraisal arbitrage phenomenon.35 This phenomenon was made possible largely by the generous statutory rate of interest on appraisal claims (5 per cent over the Federal Reserve discount rate, compounded quarterly from the closing date of a merger) and a 2007 Court of Chancery decision in *In re Appraisal of Transkaryotic Therapies, Inc.*36 In that case, the Court permitted investors who purchased publicly traded shares in the open market, when neither petitioner nor respondent knew whether those shares were voted in favour of a merger (which would disqualify them from seeking appraisal), to pursue appraisal

31 Id. at *4-5.
32 Id. at *7 (emphasis in original).
33 In general, holders of listed stock (or stock held by more than 2,000 holders of record) have appraisal rights if they are required to accept as merger consideration anything other than stock of the surviving company, listed stock of any other corporation or cash in lieu of fractional shares. 8 Del. C. § 262(b).
34 8 Del. C. § 262.
so long as the total number of shares not voting in favour of the deal was greater than the number of shares pursuing appraisal. Several appraisal decisions finding fair value materially above the merger price added to the increase in filings.

Recent developments, however, have pumped the brakes on appraisal arbitrage. First, in 2016, Section 262(h) of the DGCL was amended to permit companies to cut off the accrual of statutory interest by prepaying any amount to the petitioner. In addition, in response to the concern that small appraisal claims were being filed solely to extract nuisance settlements, Section 262(g) was amended to provide that appraisal would be unavailable in the case of a company whose stock was publicly listed if the appraisal demands represent 1 per cent or less of the stock outstanding and the total value of the demands (as implied by the deal price) is US$1 million or less.

Secondly, in 2017, the Delaware Supreme Court reversed two appraisal awards – 7.5 per cent above the deal price in DFC Global and 28 per cent above the deal price in Dell – in both cases because the lower court had given insufficient weight to the deal price. As Chief Justice Strine explained in DFC Global, economic principles suggest that in open and arm’s-length mergers, ‘the best evidence of fair value [is] the deal price’. The Court rejected the arguments that regulatory uncertainty surrounding the target at the time of the transaction rendered the deal price unreliable, and that the buyers’ status as a financial sponsor rather than a strategic acquirer meant that it did not fully value the target. In Dell, Justice Valihura echoed this reasoning, and extended it to a management buyout involving a relatively limited pre-signing bidding process.

Both decisions left open that the deal price would not be entitled to significant weight in all cases, particularly those with an uncompetitive or otherwise flawed deal process. For that reason, even after Dell and DFC Global, the Court of Chancery declined to place any weight on the deal price in at least two appraisal cases. However, in those cases, the Court looked to the deal price as a check on its fair value determination, which ultimately was very close to the deal price.

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37 Scott Callahan, Darius Pala and Eric Talley, Appraisal Arbitrage and Shareholder Value, 3 J Law, Fin & Accounting 147, page 3 (2018) (describing how statutory interest rate in Section 262(h) and the Court of Chancery’s 2007 Transkaryotic decision led to arbitrage opportunity: hedge funds may ‘accumulate shares in the target company after an announced merger, perfect appraisal rights, and put forward a sophisticated expert to challenge the merger consideration, possibly obtaining an award in excess of the merger consideration. And, even if the award fell short of the merger consideration, it would accrue interest at the statutory compounded rate, often far outpacing the risk-adjusted return on the deal consideration itself’).


40 DFC Global, 172 A.3d at 349.

41 Id. at 349-50.

42 Dell, 172 A.3d at 31-35.

43 See, e.g., Blueblade Cap Opportunities LLC v. Norcraft Cos, Inc, C.A. No. 11184-VCS, 2018 WL 3602940, at *1-3 (Del. Ch. 27 July 2018) (refusing to give the deal price any weight, finding fair value to be 2.5 per cent above the deal price); In re Appraisal of AOL Inc, C.A. No. 11204-VCG, 2018 WL 1037450, at *2 (Del. Ch. 23 February 2018) (also refusing to give deal price any weight, finding fair value to be 2.6 per cent below deal price).
Thirdly, a separate line of appraisal cases has found fair value to be significantly below the deal price due to the fact that synergies are excluded from the statutory fair value standard. For example, in *ACP Master, Ltd v. Sprint Corp*, Vice Chancellor Laster held that fair value was US$2.13 per share, less than half the merger price of US$5 per share. In *Verition Partners Master Fund Ltd v. Aruba Networks, Inc*, Vice Chancellor Laster relied on the unaffected market price of the target’s stock, which was 30 per cent below the deal price, as the ‘most persuasive evidence of fair value’. On appeal, however, the Delaware Supreme Court reversed, holding that the deal price minus synergies realised in the transaction was the appropriate way to determine fair value based on the record of that case (which still valued the tie-up below its deal price).

These developments have already led to a sharp decrease in appraisal actions, with new appraisal filings falling by approximately two-thirds from their peak in 2016.
Chapter 4

REGULATION OF FINANCIAL INSTITUTION M&A IN THE UNITED STATES

Gregory Lyons, David Portilla and Nicholas Potter¹

I INTRODUCTION

M&A involving financial institutions, which for the purposes of this chapter are defined to include banks and insurance companies, constitute a major segment of the US M&A market every year. This chapter examines the evolving legal and regulatory features of M&A deals in the financial services market, and seeks to provide guidance as to how the changing face of regulation is likely to impact transactions in this important market segment.

II BANK M&A

With approximately 250 mergers per year over the past decade,² and almost 5,500 banks remaining in the United States,³ M&A has been and will continue to be a constant feature of the US banking landscape. Given that they constitute 85 per cent of US banks by number⁴ (if not by aggregate banking assets), community banks (defined for these purposes as those with less than US$10 billion of assets) always will dominate the M&A space. Indeed, in the years following the financial crisis there were very few deals outside of community banking, as larger banks enhanced their capital bases and focused on responding to the enhanced regulatory standards imposed by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) and enhanced scrutiny by the federal banking agencies.

However, more recently these larger banks have started to participate in more bank and non-bank deal activity. For reasons discussed below these institutions, as well as foreign banks seeking to gain greater access to the US market, can be expected to play an increasingly prominent role in the bank M&A market unless the environment turns more negative to growth due to political, economic or other factors.

More generally, while economic factors affect all M&A, the regulatory environment, encompassing not only the laws and regulations themselves but also the manner of their implementation by the bank regulatory agencies, impacts bank M&A more than virtually any other industry. This environment designates the possible participants (very limiting for private equity and non-financial companies), the preconditions for banks to participate (being healthy from a financial and regulatory perspective) and the regulatory burdens facing

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³ FDIC Quarterly Banking Profile, Q4 2018, p. 1.
⁴ Id. at p. 9.
the resulting institutions. Understanding this environment, both generally and as to the specific institutions contemplating a transaction, is critical to evaluating any possible M&A transaction.

i  US-based bank M&A

Before the financial crisis, regional and global US banks aggressively pursued M&A to increase their geographic and industry coverage and customer base, and to obtain the enhanced operational efficiencies resulting from spreading costs across a large revenue base. The financial crisis and Dodd-Frank interrupted this narrative. Dodd-Frank, as implemented by the federal bank regulators shortly after the crisis, applied enhanced prudential standards (EPS), including capital-related burdens and resolution planning, on banking institutions, which burdens increase as an institution crosses various asset thresholds (e.g., US$10 billion, US$50 billion, US$250 billion). Moreover, deals beyond a limited size would require a US bank with assets above US$50 billion to update its capital plan prior to obtaining regulatory approval for the transaction, while with larger deals the regulators also would require additional information so that they could confirm that a deal would not potentially have an adverse impact on the financial stability of the US. All these additional burdens combined to inhibit the traditional drivers of non-organic growth for larger institutions.

In this regard, one metric of the efficiency of a bank’s operations is its pre-tax, pre-provision income divided by its risk-weighted assets (basically, the bank’s assets, risk-weighted depending on perceived credit and market risk) (efficiency metric). Using this approach, the optimal size for a banking institution in 2016 (the end of the Obama administration) was between US$5 billion and US$10 billion of assets. In other words, in contrast to the pre-crisis trend favouring growth to achieve economies of scale, the increased burdens imposed on larger banks after the crisis resulted in banking institutions becoming less efficient with capital on average as they grew beyond US$10 billion of assets. This regulatory dynamic clearly chilled the incentives for these regional institutions to pursue transactions.

However, the regional banks have continued to strengthen since 2016. Moreover, the change in presidency resulted in new individuals leading the US federal banking agencies. These individuals generally are perceived to favour a more tailored approach to regulation than their predecessors, and indeed in October 2018, the regulators proposed regulations to reduce the burden of the EPS for banks between US$100 and US$250 billion of assets (and to eliminate the EPS burdens for banks US$50 billion to US$100 billion of assets) (proposed US tailoring rules).

As a result of these developments, in 2018 the more traditional relationship between increased size and efficiency returned, with banks above US$50 billion of assets (rather than US$5 to US$10 billion of assets) having the highest efficiency metric. The banking industry is showing evidence of responding. For example, in March 2019, Fifth Third Bancorp acquired US$20 billion asset MB Financial to create a US$170 billion asset bank. Also in 2019, SunTrust Banks (US$215 billion of assets) and BB&T Corporation (US$225 billion of assets) announced they were entering into a merger of equals. These deals are driven by many of the same factors as have historically applied, as well as a desire to invest funds in fintech.

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5 Keefe Bruyette & Woods; SNL Financial Data.
6 Id.
These banks need to compete with global banks like JPMorgan, which has announced it will spend US$11 billion on fintech in 2019, several times the entire annual profit of many regional banks.

However, inhibitors remain to mergers creating ever-larger US banks. The proposed US tailoring rules maintain material additional EPS burdens for banking institutions that cross US$250 billion of assets. Thus, given the apparent adverse relationship between the enhanced regulatory burden and the efficiency metric, a regional bank with US$100 to US$200 billion of assets may want to consider acquiring a banking institution small enough to keep it below the US$250 billion asset threshold unless a strong rationale for a larger transaction exists. For example, SunTrust and BB&T have stated that they believe their close geographic proximity allows significant economies of scale to invest in fintech, and each was by itself approaching US$250 billion of assets and thus likely would have encountered the higher EPS at that level in the near future in any event. Given the EPS burdens of a particular asset level apply in full to a bank once it crosses that asset level, banks have significant disincentive to barely cross a given EPS asset threshold. In other words, from an economies of scale relative to burden perspective, no bank would want to be just one dollar above the asset threshold (i.e., in the case of SunTrust and BB&T, US$250 billion) at which point a higher level of EPS burdens applies.

Moreover, the burden on the largest Wall Street firms, known in regulatory parlance as global systemically important banks, and the post-Dodd-Frank focus on ensuring financial stability as a factor in applications involving large deals, could prevent a return to the large national deals of the 1980s between two US firms, like the merger of NationsBank and Bank of America that resulted in the national retail giant of today. As JPMorgan’s heavy investment in fintech indicates, these large institutions appear to be focusing more on using mobile and other technology to enhance market share, rather than relying on traditional bank M&A. Given that JPM has grown deposits at twice the industry average since 2014 – US$215 billion in absolute terms (or equivalent to the seventh-largest US commercial bank) – this approach seems to have provided a nice complement to its branch network.7

Nonetheless, M&A remains a significant growth mechanism for the vast majority of US banks (and foreign banks, as discussed below), and the environment currently is as favourable as it has been for many years. Diligence by each party remains critical, anti-money laundering, a poor Community Reinvestment Act rating and other significant regulatory issues still can significantly delay or even prevent regulatory approval of a transaction. However, the time required for Federal Reserve Board (FRB) M&A approvals in 2018 reduced by more than one-third from the 2014 highs,8 and the FRB appears willing to consider deals as large as SunTrust and BB&T, which will result in the seventh-largest bank in the US.

### Foreign bank M&A

Large bank M&A in the US market is not limited to US-based banking institutions. Foreign banking organisations (FBOs) comprise 16 of the largest 20 global banks, with JPMorgan sixth after five Asian banks.9 FBOs also have a significant presence in the US, constituting 10 of the largest 34 US holding companies, and nine of 21 US holding companies with US assets

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7 BankDirector.com, ‘This Bank is Winning the Competition for Deposits’ (15 March 2019).
8 S&P Global Market Intelligence, ‘Bank M&A has gotten speedier in recent years’ (December 2018).
between US$100 billion and US$200 billion. These numbers do not include the substantial US branch presence of FBOs. For example, the Canadian FBOs Toronto Dominion, Bank of Montreal and Royal Bank of Canada (RBC) each have an aggregate US branch presence of US$346 billion, US$200 billion and US$164 billion, respectively, and the Japanese FBOs MUFG and Mizuho each have an aggregate US branch presence of US$274 billion and US$140 billion, respectively.¹¹ As a point of reference, the smallest of these, Mizuho, has US branch assets equivalent to a top 30 US holding company.

FBOs also have shown a strong desire to grow in the US market, in many cases given the continued relative strength of the US market and the much more concentrated banking sector in their home markets. RBC’s acquisition of City National Bank (Los Angeles headquarters) and Canadian Imperial Bank of Commerce’s acquisition of PrivateBancorp (Chicago headquarters) represent two of the largest US deals by value announced since 2015.¹² MUFG also has stated that it wants to be a top 10 US bank holding company,¹³ which would require it to more than double in size from its current US$168 billion of US bank holding company assets.

As with their US-based counterparts, the US regulatory regime likely will play a large role in the continued expansion of FBOs in the US. The federal banking agencies expressed concern after the financial crisis that the large presence of foreign banks in the US could impair the US economy in times of global financial stress. As a result, US regulators required all FBOs with US non-branch assets of US$50 billion or more to establish US holding companies to aggregate their US entities, and imposed capital and EPS standards on those holding companies at least equally burdensome as those that apply to their US-based counterparts. In April 2019, the federal banking agencies proposed FBO regulations intended to tailor the application of the EPS and other burdens to FBOs (FBO tailoring proposals) similar to the objectives of the US tailoring proposals.

The impact of the FBO tailoring proposals and other drivers of FBO M&A in the US is not yet fully known. However, particularly given the size of their global operations, which in many cases for FBOs with a significant US presence is significantly larger than all but the largest US banks, continued desire to meaningfully expand into the US market appears likely. Indeed, given their global size, larger US targets would be necessary to make an impact on their balance sheets. Indeed, if MUFG’s view about the desired size in the US holding company presence (which would still result in the US holding company presence being less than 15 per cent of its global presence) is representative of other FBOs, the US regional banks would appear logical targets for their growth.

III NON-BANK M&A¹⁴

While bank M&A tends to garner the largest headlines, both US-based banks and FBOs are also engaging in significant non-bank M&A in the US. While banks are acquiring a spectrum of financial companies, changes in the regulatory requirements after the financial

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¹³ American Banker, ‘MUFG’s big expansion is just getting started’ (26 March 2018).
¹⁴ Including asset managers, fintech and insurance companies.
crisis also are having an impact on these transactions. Banks are required to hold capital to support their assets, and the bank regulators increased their capital ratios (i.e., the amount of capital that they have to hold to support a given level of assets) after Dodd-Frank. Many banks thus have focused on acquisitions of asset managers, M&A-advisory broker-dealers and similar service-based entities that allow banks to generate revenue without generating significant balance sheet assets that require additional capital. A sampling of approximately a dozen US-based regional banks shows that on average they derive about 38 per cent of their income from non-interest (i.e., non-mortgage or investment security-based) revenue, showing that these types companies are an important part of their overall revenue mix.\textsuperscript{15} Other regulatory changes resulting from Dodd-Frank, such as the Volcker Rule, have materially limited the ability of banks to acquire private fund complexes or entities engaged in significant proprietary trading.

As banking institutions return to fiscal and regulatory health, they have a variety of options to consider as to where to engage in non-bank acquisitions. The proper placement of the target in a consolidated organisation can materially impact the ongoing benefits it can provide. Particularly for financial holding companies, a special designation for well-managed and well-capitalised institutions held by the vast majority of the regional and larger banks acquiring a non-bank entity as a subsidiary of the holding company generally permits the broadest range of permissible activities while requiring no bank regulatory approvals. On the other hand, acquiring a non-bank entity as a subsidiary of a bank permits the bank to fund and support the operations of that entity most efficiently. Particularly if, as is generally the case with larger institutions, the relevant banking institution has a national bank subsidiary, merging the non-bank into the national bank would permit the non-bank to obtain the benefit of the federal preemption over state laws afforded to banks, but this is generally the most burdensome type of acquisition from a regulatory perspective.

Banks are increasingly focused on the fintech space, both to increase internal operational efficiency (e.g., blockchain) and to provide enhanced revenue and services to customers (e.g., payments and lending platforms). While banks often acquire all or a majority stake in the former, in the latter case they often take non-controlling interests. If a bank were to take a controlling stake (certainly more than 25 per cent of the voting stock, but often much lower, particularly if combined with ongoing business relationships), then the fintech company would become subject to the bank’s regulatory framework. In that case, the bank would have to be concerned about regulatory and reputational risk with the fintech company, and the fintech company's permissible activities would be limited to those permissible for banking institutions. Moreover, whereas at one point fintech sought to compete with banks, banks have access to low-cost funding (via deposits) and a sticky customer base that fintech firms find desirable.\textsuperscript{16} As a result, a recent report stated that more than 75 per cent of fintech firms cite collaboration (often via minority investments and business relationships) preferable to competition with incumbents, such as the institutions that dominate the banking industry.\textsuperscript{17}

For acquisitions of all the stock or assets of a fintech company, the bank regulatory considerations are identical to those described above for other non-bank acquisitions. On the other hand, banking institutions typically will acquire a non-controlling interest in a fintech company off the holding company (and not the bank). While banks are also able to

\textsuperscript{15} Silver Lane Advisors; SNL Financial, Company Filings (30 September 2018).
\textsuperscript{16} American Banker, ‘Where fintech dollars will go in 2018’ (December 2017).
\textsuperscript{17} Capgemini, LinkedIn and Efma, World FinTech Report (December 2018).
acquire non-controlling interests in some circumstances, the holding company often provides greater structuring flexibility from a regulatory perspective. The principal concern with holding company acquisitions of minority interests in fintech companies historically has been the lack of clear guidance as to what levels of voting and non-voting stock ownership and business relationships the FRB will permit without deeming the holding company to control the fintech company from a bank regulatory perspective (which presents the disadvantages described above).

However, in April, 2019, the Federal Reserve sought to provide greater certainty as to what constitutes control with acquisitions of less than 25 per cent of the voting stock of a target (at 25 per cent voting stock ownership or above, a company is conclusively determined to be in control of a target under the US banking laws).\(^8\) This greater certainty also may increase the desire of both banking institutions and fintech companies to engage in these partnership investments with each other. The proposal creates a grid, with higher levels of voting stock ownership (in any event below 25 per cent) necessitating the acquirer having fewer other indices of control (e.g., interlocking directors, business relationships) to avoid a banking law control determination. Interestingly, as our firm highlighted shortly after the FRB published the proposal,\(^9\) as currently drafted, the proposal may provide more assistance to fintech companies and activist investors increasing stakes in banking institutions without being deemed in control of a bank than to banks seeking to gain meaningful non-control stakes in fintech companies.

Finally, insurance company M&A continued to proceed at a rapid pace in 2018, as private equity firms entered the market, the Bermuda companies consolidated and global companies such as AXA significantly enhanced their market presence through non-organic growth. Unlike bank M&A, insurance transactions tend to be regulated solely by state insurance regulators. These regulators have begun to become more comfortable with private equity firms as owners of insurance companies, and the rules governing risk-based capital for insurance companies may favour larger groups once the National Association of Insurance Commissioners group capital calculation (GCC) comes into effect. The precise impact of the GCC remains to be seen, as for now field testing is just under way, and it is to be expected that after an initial period of adjustment, the larger insurance groups will be able to benefit from aspects of the GCC not available to smaller or monoline insurance groups. This may well be a catalyst for M&A activity in a market otherwise characterised by low interest rates (especially relevant for life and annuity insurers) and increasingly positive pricing trends for organic business growth (for property and liability insurers and reinsurers).

## IV CONCLUSION

After a pause caused by the financial crisis and a subsequent harsher regulatory environment, both economic and regulatory factors appear to favour bank and non-bank M&A by both US-based banking institutions and FBOs. As with many other areas of the US, however, the current more favourable environment is not stable, and a recession or a change in the federal government leadership to a less business-friendly administration could significantly impair inorganic expansion. For this reason, many banking institutions currently are actively

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searching for targets to take advantage of the current arrangement. The regulation of fintech and insurance M&A also are at a stage where they may favour transactions with buyers who can fit within the rigorous regulatory framework or even take advantage, in the case of insurance groups, of the emerging GCC in the US.
Chapter 5

UNITED STATES
ANTITRUST OVERVIEW

Richie Falek, Neely Agin and Conor Reidy

I INTRODUCTION

Before reviewing key developments in the antitrust enforcement of M&A in the United States over the past year, it is helpful to begin with some brief background on US antitrust law and process.

Section 7 of the Clayton Act, the primary standard for the competitive review of mergers, acquisitions, joint ventures and other transactions in the United States, is deceptively simple. It prohibits M&A where the effect ‘may be substantially to lessen competition, or tend to create a monopoly’. The more-than-80 years since the Clayton Act was established, however, have given rise to a litany of case law interpreting this very broad standard. While most of those cases remain nominally good law, many decisions arguably are inconsistent with the continually evolving economic and commercial environment. Indeed, there are many newer industries for which there is little applicable case law: only imperfect analogies that can be drawn from more mature industries.

To help address these issues, the Federal Trade Commission (FTC) and the Department of Justice (DOJ) – the two agencies that share responsibility for competitive enforcement in the United States – have issued guidelines to help practitioners more predictably analyse the potential risk that a transaction may be challenged. However, here, too, there are limitations: the guidelines are generalised, and may support varying analyses of a given transaction. As a result, many US transactional lawyers take deep, expensive dives into case law and guidelines, only to be inconclusive in predicting the likelihood of government opposition to a proposed transaction.

For this reason, it is often a wiser course of action to begin with the Hart-Scott-Rodino Antitrust Improvements Act (HSR Act) rather than case law or guidelines. The HSR Act provides the FTC and DOJ an opportunity to review transactions before the parties close the transaction and the proverbial ‘eggs are scrambled’. While the HSR Act introduced some delay due to one or more waiting periods, the result – along with the FTC and DOJ’s enforcement – actually has created tremendous transparency and much higher levels of certainty.

1 Richie Falek, Neely Agin and Conor Reidy are partners at Winston & Strawn LLP.
3 Id.
4 Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines (2010). Note that the guidelines are almost a decade old.
The FTC and DOJ annually publish detailed statistics regarding the HSR clearance process.\(^6\) Virtually without exception in each year since the passage of the HSR Act, this quantitative analysis demonstrates that the HSR process is fast and almost always results in positive outcomes for parties. As such, while antitrust litigation is no doubt time-consuming and very expensive, it is very rarely necessary. Having said that, there are various ways in which parties can help ensure a positive outcome from the HSR process.

i Numbers trump case law, especially under the current administration

Very generally, a transaction in excess of certain value and party-size thresholds requires that each party make an HSR filing and then observe a 30-day waiting period before consummating the transaction.\(^7\) This initial waiting period can be shortened if the parties request and the agencies grant early termination of the waiting period. On the other hand, the waiting period may be lengthened if one of the agencies issues a Second Request, which includes a more extensive production of documents, data and interrogatory responses; depositions of individual representatives of the parties; and interviews and document requests issued to relevant third parties such as customers, suppliers and competitors. A Second Request will typically add months to the approval process.

In a Second Request scenario, there are three potential outcomes after the parties comply: the reviewing agency can clear a transaction; the parties and the agency can enter into a settlement (consent decree), which typically requires the divestiture of one party’s businesses to an approved buyer as a condition of allowing the broader transaction to be consummated; or the agencies can seek to block the transaction in federal court for violating Section 7 of the Clayton Act.

Every year, the DOJ and FTC jointly issue statistics covering the HSR process for the prior government fiscal year.\(^8\) The most recently released report, for 2017, found the following:

\(^a\) there were more HSR filings than ever: over 4,000;\(^9\)

\(^b\) 97.4 per cent of transactions were cleared without a Second Request, a higher rate than in any year other than 2008, during the Great Recession;\(^10\)

\(^c\) most transactions were resolved within the first 30 days, with early termination (typically shortening the period to between 10 to 14 days) granted almost 80 per cent of the time it was requested;\(^11\)


\(^8\) Id. at 26.

\(^9\) Id. at 6.

\(^10\) Id. at 6.

\(^11\) Id.
of these thousands of filings, the FTC issued 33 Second Requests and the DOJ issued 18; and\(^\text{12}\)
the agencies issued 15 consent decrees and brought 13 lawsuits.\(^\text{13}\)

ii Strategies to increase transparency and predictability

Focus on the current competitive landscape

Despite the fact that the overwhelming majority of transactions are approved, each transaction presents its own facts and circumstances, and so a positive outcome cannot be assumed. Careful preparation is thus always necessary. Preparation should begin with an assessment of the current competitive landscape gleaned from discussion with the parties, ordinary course documents and public sources. This assessment should include:

- if the parties compete, for what specific products or services, and in which specific geographies;
- identification of actual and potential competitors and their market shares, as well as the strengths and weaknesses of each;
- whether new competitors recently have entered the market; and
- how likely market entry is in the future.

This assessment of the competitive landscape provides the context to guide the application on past enforcement and case law to the current transaction.

Anticipating customer reactions

After assessing the competitive landscape, counsel should then investigate likely customer reactions. After all, the agencies’ first substantive step after reviewing an HSR filing often is to seek out the parties’ largest customers to get their perspectives on the transaction. Since these inquiries are not publicly disclosed, and the agencies provide no relevant statistics, it is not possible to precisely gauge the impact of customer reaction on the likelihood of further review.

That said, it is axiomatic that the antitrust laws are designed to protect competition and customers, not competitors. Thus it follows that a lack of customer complaint (or, even more so, favourable customer reaction) will lessen the potential for further review or possible litigation. After all, if no customers are willing to stand up in court and say that the transaction will hurt them, it will be very difficult for the government to prove that competition for customers is likely to be harmed.

In theory, it would be desirable for antitrust counsel to make these inquiries before the underlying transaction agreement is executed so that the parties can make an informed decision regarding what antitrust-related commitments they are willing to undertake. The problem, of course, is that a proposed transaction is almost certainly not public at this point. Direct customer outreach is thus not feasible. Nevertheless, counsel should work directly

\(^\text{12}\) Id. at 5.
\(^\text{13}\) Id. at 2. The FTC brought two and the DOJ brought 11, although the DOJ simultaneously filed a proposed settlement in nine of those 11 lawsuits.
with the parties to gauge customer reactions as best they can. For example, the parties may be able to anticipate likely reactions of key, longstanding customers without asking them directly.

**Make informed contractual commitments**

While there is no guarantee that any transaction will clear the HSR process, a careful analysis of the competitive landscape and possible customer reaction, followed by analysis of past enforcement and case law, helps maximise the possibility of success. It also helps the parties make informed decisions regarding the contractual commitments they will be willing to undertake.

For example, targets typically request a hell or high water provision, most often at the outset of negotiations. Such provisions require an acquirer to divest any assets or to take any action the agencies require (such as licensing intellectual property) to alleviate their antitrust concerns. If counsel's review has indicated that certain assets may be likely to cause antitrust concerns, and those assets are critical to the underlying economics of the transaction, an acquirer will obviously be less likely to agree to a hell or high water provision. Conversely, if review has indicated that issues are unlikely, an acquirer will be more willing to agree to a hell or high water provision, perhaps in exchange for a concession on a provision not related to antitrust.

There are numerous other potential provisions that may also arise over the course of negotiations, such as divestiture caps (limiting the dollar amount or type of assets the acquirer is willing to divest) and break-up fees (giving the acquirer the right to pay a fee and abandon the transaction if the agencies’ demands are too onerous). Understanding the larger context of the transaction will help both sides more clearly determine their positions on these matters.

**iii US antitrust enforcement: the year in review**

There were two trends that emerged in M&A antitrust enforcement this past year: the continued success of the FTC in obtaining preliminary injunctions in federal district court and attention to deal-specific vertical issues.

**Preliminary injunctions**

In December 2017, the FTC issued an administrative complaint challenging the merger of Tronox Limited and Cristal, two top suppliers of chloride process titanium dioxide, a white pigment used in a wide variety of products including paint, industrial coatings, plastic and paper. The FTC simultaneously asked a federal district court to issue a preliminary injunction preventing the parties from closing the transaction pending the conclusion of FTC administrative proceedings. The District Court for the District of Columbia determined that the FTC was likely to prove that the transaction would substantially reduce competition for chloride process titanium dioxide and granted the preliminary injunction in September 2018. Tronox and Cristal subsequently agreed to settle with the FTC, agreeing to divest chloride process titanium dioxide assets to a multinational chemical manufacturer. The FTC approved its final order in May 2019.

The FTC obtained another significant result when it issued an administrative complaint in April 2018 charging that Wilhelmsen Maritime Services’ proposed US$400 million acquisition of Drew Marine Group would significantly reduce competition in the market for marine water chemicals and services used by global fleets. The FTC claimed that if the transaction were consummated, the combined company would control at least 60 per cent of
that market. As in the Tronox/Cristal case, the FTC asked the District Court for the District of Columbia to issue a temporary restraining order and preliminary injunction to prevent the parties from consummating the merger pending the administrative proceeding. The Court granted the preliminary injunction, and shortly thereafter, Wilhelmsen and Drew Marine abandoned the transaction.

Vertical issues

Last year, the DOJ made clear that while it remains concerned about vertical mergers, case-specific facts are critical when evaluating the likelihood of a challenge. While the DOJ challenged the vertical aspects of the AT&T/Time Warner combination, it allowed the Cigna/Express Scripts and CVS/Aetna transactions, both of which followed the DOJ’s loss over AT&T/Time Warner, to close without any remedy, despite vertical concerns. It remains to be seen whether the DOJ’s unsuccessful challenge to AT&T/Time Warner will cause the DOJ to be more hesitant in the long term to challenge vertical transactions.

In November 2017, the DOJ challenged AT&T’s proposed US$84 billion acquisition of Time Warner. The DOJ alleged that the combined company would ‘use its control over Time Warner’s valuable and highly popular networks to hinder its rivals by forcing them to pay hundreds of millions of dollars more per year for the right to distribute those networks’, and that the combined company would also ‘use its increased power to slow the industry’s transition to new and exciting video distribution models’. In June 2018, however, the District Court for the District of Columbia denied the DOJ’s request to enjoin the transaction. The Court held that the DOJ had failed to prove that AT&T’s acquisition would substantially lessen competition, explaining that Time Warner’s networks were not ‘must haves’ for a distributor to compete, and that although Time Warner’s valuable content theoretically gave it leverage to negotiate, these arguments were insufficient to establish that the merger would result in increased leverage and harm to competition without more evidence of real-world impact. The DOJ appealed the District Court’s decision, but in February 2019 the Court of Appeals for the District of Columbia upheld the lower court’s ruling.

Following its loss in district court over AT&T/Time Warner, the DOJ closed its investigations into two other mergers with potential vertical concerns. In September 2018, the DOJ closed its six-month investigation into Cigna’s acquisition of Express Scripts, a health insurance company and pharmacy benefit manager, respectively. The DOJ analysed whether the merger would substantially lessen competition in the sale of pharmacy benefit manager (PBM) services or raise the cost of those services to Cigna’s health insurance rivals. In closing the investigation, the DOJ stated that Cigna’s US$67 billion proposed acquisition of Express Scripts was unlikely to result in harm to competition or consumers because Cigna’s PBM business nationwide was small, and at least two other large PBM companies and several smaller PBM companies would remain in the market following the merger.

While the DOJ brought a challenge against CVS’s proposed US$69 billion acquisition of Aetna, the challenge was based on horizontal rather than vertical concerns. The DOJ alleged that the combination of two of the country’s leading sellers of individual prescription drug plans would result in higher premiums, lower service and reduced innovation. It did not, however, include in its complaint any allegations regarding the addition of CVS’s pharmacy

and PBM business to Aetna’s health insurance business, although public commentators expressed concerns with input foreclosure and customer foreclosure. Regarding input foreclosure, the DOJ explained that the evidence showed that it was unlikely that CVS could profitably increase its PBM or retail pharmacy costs following the merger, as doing so would result in CVS losing business to other PBM or retail pharmacies. As for customer foreclosure, the DOJ noted that Aetna occupied only a small share of the market in many commercial health insurance markets, and thus CVS’s acquisition of Aetna was unlikely to result in customer foreclosure.

To address the DOJ’s horizontal concerns with the CVS/Aetna merger, CVS and Aetna entered into a settlement with the DOJ in which they agreed to divest Aetna’s Medicare Part D business to WellCare Health Plans. After reviewing the terms of the settlement, however, the District Court for the District of Columbia decided to hold an unprecedented two-day hearing to assess whether the settlement provided sufficient protection to consumers. The hearing, which concluded on 6 June, included testimony from witnesses who both supported and opposed the proposed remedy.

It remains to be seen if the above trends – the success by the FTC in obtaining preliminary injunctions and the agencies’ focus on deal-specific vertical issues – will continue to play a significant role in 2019. That said, practitioners should keep both trends in mind as they guide their clients through the M&A antitrust enforcement process.
I OVERVIEW OF M&A ACTIVITY

Since Mauricio Macri took office in December 2015, with the clear intent of shifting policy towards a pro-business model, investors have shown a renewed interest for opportunities in Argentina.

While the country still needs to go through some critical and long-term structural reforms, the current administration has been encouraging investments in several sectors, including technology, agribusiness, transport and aviation, energy, mining and infrastructure. Within this context, the Argentine economy still benefits from reasonable, well-priced commodities, an educated workforce and a strong entrepreneurial community.

M&A activity was significant in the period running from 2016 to 2018 (both in terms of number of deals and transaction volumes). For a number of reasons, including general conditions affecting emergency markets and local factors (such as the current economic recession and the typical political uncertainties as the country approaches the presidential elections in late 2019), a drop in M&A activity is expected for this year.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Argentine capital market is relatively small, lacks sufficient depth, has limited liquidity and is subject to regulations that are just now in the process of being modernised to meet international standards. Further, most Argentine public companies generally have a minority portion of their capital floating in the capital markets (between 10 and 30 per cent). Accordingly, public M&A transactions in Argentina are not frequent.

As a result of the foregoing, most of the M&A activity is done through private deals. These may involve shares, assets or a combination thereof. Share deals are preferred to asset deals.

Share deals are undertaken through stock purchase agreements that generally follow international standards for private transactions. These agreements can be subject to foreign law and jurisdiction (including foreign arbitration tribunals). This is generally the case in transactions for high-end Argentine companies. However, there are some aspects that will necessarily depend on and be governed by Argentine laws (e.g., matters relating to the consummation of transactions, certain matters covered by local securities regulations, labour laws, regulatory requirements).

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Assets deals (such as the bulk transfer of assets) are less common in Argentina for tax reasons (as further detailed below), which in general make such transfers expensive, as the transfer of each asset is subject to a different set of taxes; and because of timing concerns.

Public M&A transactions that involve the acquisition of a controlling stake may require the acquirer to launch a tender offer to all the minority shareholders in the target company. A mandatory tender offer is not required when the acquisition does not entail acquiring the control of a company (i.e., more than 50 per cent of the voting securities or de facto control) or when a change of control occurs as a result of a merger or a spin-off. The tender offer shall contemplate a fair value, according to the parameters of recently enacted regulations.

On a separate note, corporate foreign shareholders must register at the Public Registry of Commerce to be able to hold shares of a company incorporated in Argentina. A foreign shareholder must submit certain corporate and accounting information to obtain registration. The registration procedure and requirements have been substantially eased recently. Further, the Capital Markets Law exempts foreign shareholders from such registration when the target company is listed on the stock market.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

There have been no major amendments in corporate and takeover law in recent years, other than as described above.

Certain amendments introduced by the Macri administration to the foreign exchange regime have been critical to the development of the M&A market, in particular the elimination of foreign exchange restrictions to acquire foreign currency and for the transfer of proceeds outside Argentina (including dividends or other profits).

Argentina’s companies laws have been amended to allow a company to be set up as a single shareholder corporation (sociedad anónima unipersonal or SAU). Further, it is now possible to set up a company in the form of a simplified corporation (sociedad anónima simplificada or SAS) through an expeditious and online procedure. Both SAUs and SASs are aimed at promoting start-ups and entrepreneur activities in Argentina.

Finally, Congress has approved a new public–private partnership law. This regime seeks to replace the existing regulatory frameworks, which failed because of technical defects and the critical legal, institutional and economic context affecting Argentina during the past few years. The new law is ambitious, and includes various protections in favour of the private sector (contractors and lenders) to effectively foster the development of these associative schemes and generate massive infrastructure investments.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

As already mentioned, up to December 2015, foreign investment in Argentina decreased sharply as a result of a high level of state intervention in the economy, coupled with a shortage of foreign exchange, which resulted in the former (Kirchner) government freezing all outflows of dollars from Argentina. As a result, companies were not allowed to transfer monies abroad (such as in the form of dividends, royalties or payments for services), and thus foreign investment was drastically reduced.
In this context, most M&A activity involving foreign investors was related to the exit of foreign investors from Argentine assets because of the economic difficulties or as a result of multinationals leaving the region.

Following the election of a more pro-business government in December 2015, foreign investor appetite has increased and we are now seeing a renewed interest in Argentina. While the arrival of foreign investments is still moderate, there is a clear increase in the volume of M&A activity and the size of transactions.

Local and foreign hedge and private equity (PE) funds have been particularly active recently, and have closed transactions in the past four years in different sectors, such as the energy (including oil and gas and renewable energy), agribusiness, hotel, food and beverage, infrastructure and real estate sectors.

There are no specific required approvals for foreign investments either through PE funds or other types of foreign investments (other than antitrust approval, if applicable). However, depending on the type of portfolio company, activity or industry, as a general rule, certain investments may be subject to prior (or, in some cases, subsequent) approval by different regulatory agencies.

In some regulated industries, such as financial services, insurance, telecommunications, aviation, oil and gas, mining and utilities, the approval of the applicable regulatory authority is necessary to transfer either the control of, or a relevant portion of the shares of, a company operating in those industries. Investments in real estate (rural lands or land adjacent to country borders) may in certain cases require regulatory approval, and restrictions may apply for foreign entities or individuals.

These processes generally involve the filing of detailed information about the acquirer company, and the various formalities (e.g., translations, legalisations, specific forms) will depend on the type of agency. The timing will also depend on the regulatory agency involved in the process (typically, this may take more than three months to complete).

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

As already discussed, between 2003 and 2015 (under the Kirchner administration), M&A activity was extremely modest, both in terms of the number of deals and deal volumes, because of limited foreign direct investment (inbound). In contrast, during the same time period, many other countries in the region (in particular Brazil, Mexico, Colombia, Peru and Chile) experienced an increase in foreign direct investment and a resulting increase in M&A activity.

During those years, the M&A market in Argentina was marked by less sophisticated transactions, and deal amounts were far below the average in the region. Only a few transactions have come close to, or crossed, the US$1 billion barrier (YPF, Telecom Argentina, Apache). Instead, most deals closed at a price below US$100 million.

To restore confidence in the (local and international) business community and attract investments, the new Macri administration quickly addressed some of the most urgent economic and legal issues the Kirchner administration had either created or failed to address. Before completing six months in office, Macri, inter alia, ended more than 12 years of legal dispute with the holders of Argentine sovereign debt in default, put Argentina back into international capital markets, eliminated taxes on certain exports and eliminated several foreign exchange restrictions (including on the transfer of dividends to foreign parent
companies). While it is expected that the deal flow in Argentina will increase significantly in the coming years, there is already a clear renewed interest in Argentine assets, and we have seen steady growth in the number of deals closed.

In our experience, there is an increased appetite for renewable energy (incentivised by a new special law); PE funds have already closed several deals in this sector. Additionally, several players have made investments in the renewable energy sector of more than US$6 billion following a series of auctions conducted by the government.

The recovery in the oil prices should also trigger renewed interest in oil and gas assets (including the shale oil and shale gas projects in Vaca Muerta (see also Section X)). Recently, for example, ExxonMobil and Qatar Petroleum signed a deal for a record investment in Vaca Muerta for at least US$620 million. ExxonMobil also invested in the midstream sector by acquiring a significant equity stake in Oldeval. International trader Trafigura has also completed a couple of deals to start its downstream operation in Argentina (including in association with its affiliate, Puma Energy). The same path has been followed by DeltaPatagonia, which acquired 125 service stations from YPF to start operations under the Gulf trademark, and Raizen, which acquired the downstream business of Shell.

Further, the offshore bidding round being organised by the government to award exploration permits over offshore blocks generated substantial foreign investment (including investors from the US, Japan, Norway, Germany, the UK and Qatar), and the government received bids for a total investment of approximately US$1 billion. Blocks were awarded in the Austral, West Malvinas and northern portion of the Argentina Basin, covering around 200,000 square kilometres.

The agribusiness sector also offers opportunities, and commodities prices have been recovering well in the past few years. This sector is critical to the Argentine economy, as it will trigger a cascade effect on the industrial and services sectors (in which deal volume remains modest).

PE funds have invested in different sectors, including pharma, credit card processors, telcos, logistics, technology and agribusiness. Owing to a decline in asset value and a willingness to sell by owners, subject to the stabilisation of the political scenario, PE investors may find attractive opportunities to invest in other areas, including infrastructure.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Acquisition financing originated in Argentina is very limited and costly. As a result, most foreign investors (including PE funds operating in Argentina) usually obtain their funding from foreign investors, including a wide variety of foreign institutional investors, pension funds, banks, hedge funds, multilateral institutions and individuals. Some PE funds incorporated abroad but managed by Argentine managers obtain funding from local family offices, private individuals and some investment companies. Local banks, insurance companies and government agencies do not normally invest in PE funds, and there are currently no regulations to promote or provide incentives for this.

Generally speaking, local portfolio companies are funded mainly through capital contributions. Therefore, debt obtained from foreign sources is used to a lesser degree, and local financing is available, although it may not cover all the financial needs of a portfolio company.
Interest under a debt has the advantage of being tax deductible. The Argentine Central Bank regulations contemplate that, under certain circumstances, some loans may need to be reported to the Bank. Currently, there are no foreign exchange regulations applicable to lending transactions or otherwise.

VII EMPLOYMENT LAW

In the assignment of a business, all liabilities in relation to employees will be transferred to the purchaser. If an employee is seriously affected by the assignment of a business, it is possible for that employee to consider him or herself in a position of constructive dismissal. The same applies in the case of the leasing or temporary assignment of a business.

The transferor and transferee (on any title) will be jointly and severally liable for the obligations deriving from the labour relationships that exist at the time of the transfer or assignment of a business. The transfer of personnel (without the establishment) shall only be carried out with the written consent of the affected employees.

The main effect of the assignment of a business is that the former employer is replaced by the purchaser or successor. It is not necessary that employees consent to the transfer.

A change of employer has consequences with respect to all the employment relationships that are in force, not only to all current labour relationships but also to those in which the obligation to effectively render services has been temporarily suspended (e.g., if personnel are on holiday or on sick leave).

A purchaser or successor may not oppose an employee whose services were suspended for any reason at the moment of the assignment of a business, even if the purchaser or successor has not been informed by the previous employer of the suspension.

The labour conditions currently in force regarding the assignment of a business, such as the office location, working hours and salaries, should be maintained by the purchaser or successor without prejudice to the legitimate right of the employer to modify labour conditions in the future within the limits established by the applicable labour law.

Pursuant to the mandatory case law, a purchaser or successor of a business is liable for the transferor’s obligations that derive from employment relationships that were terminated before the transfer. This implies that the purchaser or successor shall even be liable for the labour credits of previous employees who have worked for the transferor within the statute of limitations period, which for labour credits is two years.

Under the applicable law, an employee may consider him or herself to be in a situation of constructive dismissal if the assignment of a business causes serious damage to him or her – for example, if he or she was working for an economically sound company and, as a result of the assignment of the business, he or she has to start working for a markedly insolvent company. The sole fact of the assignment of a business to a purchaser or successor does not mean that an employee can automatically consider that he or she is subject to constructive dismissal.

In cases of the purchase of the stock of a corporation, there would be no assignment of a business, since the employer (the corporation) would remain the same no matter who the shareholders are.

According to the majority of local legal scholars, the transferor of a business does not assume any liability for the labour obligations of the purchaser or successor after the date of transfer. All liabilities with respect to employees shall be assigned to the purchaser or successor in interest.
VIII TAX LAW

Capital contributions are not subject to any tax in Argentina as long as the company receiving the contribution is located in Buenos Aires or a province that does not apply stamp tax (which some provinces do).

Holdings of shares issued by Argentine companies when the holder is a foreign resident are subject to a 0.25 per cent personal assets tax on their percentage net equity on 31 December every year. The Argentine company is liable for the tax, but it has a claim against the foreign shareholder for the amounts paid. Under National Supreme Court case law, branches of foreign companies are not subject to this tax.

Dividends distributed by Argentine companies to their foreign shareholders are subject to withholding tax depending on when the distributing company earned the profits out of which the dividends are paid. For fiscal years beginning on or before 31 December 2017, there is no withholding tax (provided the profits have been taxed at company level). For fiscal years beginning on or after 1 January 2018 and until 31 December 2019, dividends are subject to a 7 per cent withholding tax. For fiscal years beginning on or after 1 January 2020, dividends are subject to a 13 per cent withholding tax.

In a share deal, capital gains arising from the transfer of shares issued by an Argentine company (including redemption) are subject to a 15 per cent income tax when made by a foreign resident. In the case of a non-resident entity, the transferor may opt to pay a 13.5 per cent tax on the transfer price. If both the transferor and the transferee are non-resident entities, the tax shall be paid by the local representative of the transferor, any person mandated by the transferor to pay it, or the transferor itself from abroad. Stamp tax on the share transfer agreement may be avoided through a letter offer agreement in most provinces.

Capital gains tax also applies to transfers of shares of entities above the direct shareholder, but only when the transferred shares were acquired on or after 1 January 2018.

Transfers of assets as a going concern are subject to various taxes depending on the asset. The transfer of all sorts of assets is subject to income tax on any capital gain. For fiscal years beginning between 1 January 2018 and 31 December 2019, the income tax rate will be 30 per cent. For fiscal years beginning on or after 1 January 2020, the income tax rate will be 25 per cent. The transfer of real estate is subject to stamp tax at a rate of around 4 per cent, depending on the province where the real estate is located; the tax is customarily shared (half by the seller, half by the purchaser). The transfer of fixed movable assets is subject to VAT at a rate of 21 per cent (10.5 per cent on machinery and similar equipment). The transfer of inventory is subject to VAT at a rate of 21 per cent (10.5 per cent on some agricultural products) and to gross turnover tax (at a rate of around 3 per cent, but this depends on the province to which the tax basis is allocated). In all cases, the agreement is subject to stamp tax, but this may be avoided through a letter offer (with the exception of transfers of real estate and automobiles). As already stated, the tax is customarily shared by the seller and purchaser.

IX COMPETITION LAW

A new antitrust law was passed by Congress in May 2018.

An important change introduced by this new law lies in the timing for auditing M&A. The old regime established an *ex post* control (i.e., transactions were reviewed after closing), whereas the new law establishes an *ex ante* control (i.e., transactions are now reviewed prior to closing).

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The Antitrust Law requires that transactions in which the aggregate business volume of all companies involved therein in Argentina is higher than 100 million mobile units (which is roughly equivalent to US$60 million (as at April 2019) be approved by the Antitrust Authority before closing. The aggregate business volume means the amounts resulting from the commercial activity and direct subsidies received by the companies involved in the transaction during the last financial year, corresponding to their ordinary business and calculated on an after-tax basis.

Authorisation will have to be obtained from the Antitrust Authority for a transaction to enter into force between parties and to be effective with regard to third parties. Failure to request and obtain authorisation, or if authorisation is not granted by the Antitrust Authority, shall render a transaction void, without prejudice to any sanction that may be applicable in the case of rejection.

The Antitrust Authority shall make the request for approval public so that interested parties can submit objections. Within 120 days of the request being made public, the Antitrust Authority will have to decide whether to approve the transaction, approve the transaction subject to certain conditions or reject the transaction. Failure to issue a decision within 120 days shall be regarded as an unconditional authorisation by the Authority.

Transactions closed prior to obtaining the Antitrust Authority’s authorisation will render the companies involved subject to fines, regardless of the Authority’s decision regarding the transaction. If the Authority finds that it was a prohibited transaction under the Antitrust Law, the companies will have to divest the acquired assets. The transactions subject to review and approval are:

a) mergers;
b) the bulk transfer of assets, including transfers of ongoing concerns;
c) the purchase or acquisition of any interest in stock, equity participations or debt instruments convertible into stock, or equity participations that provide the right to influence the decisions of the issuer thereof, when, in either case, the purchaser of the same obtains through the acquisition of those securities or equity interests the control of or a substantial influence over the issuer; and
d) other transactions that entail a de facto transfer or a dominant influence upon the decisions of the company in question.

The law does not contain any specific definition of substantial influence. However, recent rulings by the Antitrust Commission have concluded that the right to appoint a certain number of directors or to appoint key officers, or the existence of supermajorities, are relevant factors for deciding in a particular case whether the buyer of a non-controlling interest in a company nevertheless acquires a substantial influence therein.

During the first year of the Antitrust Authority being established, a notice of any transaction subject to prior review and approval may be filed with the Authority either prior to its consummation or within one week of closing. However, until the Authority is created, and the aforementioned one-year period elapses, the old antitrust regime will continue to apply.

Companies involved in a potential transaction may submit their situation to the advisory opinion of the Antitrust Authority, which will determine whether the proposed transaction should be submitted for authorisation.

Significant changes to the previous regime are being introduced. Even though transactions were only considered valid between parties and with regard to third parties upon
review and approval under the old antitrust regime (a requirement that continues under the new regime), approval could be obtained after closing. The only real obligation of the parties was to notify the authorities either before closing or within a week of closing. Failure to notify was penalised with fines.

Although failure to obtain the required prior approval and denial of the approval after closing did not entail the imposition of penalties insofar as the filing had been made within the specified deadlines, by consummating the transaction without approval, the parties assumed the risk that approval could be denied or conditional, thus resulting in a need to divest the acquired assets totally or partially.

X OUTLOOK

As has been outlined, the change of administration in December 2015 triggered a change in expectations that translated into the renewed interest of foreign investors in Argentina.

The government has clearly indicated that one of its main goals is to attract foreign investments. This goal requires some pending structural changes, including those aimed at reducing the fiscal deficit and high inflation rates, reducing labour costs and improving quality standards within government institutions.

Infrastructure and energy are both in need of investment, and to that effect, the government has launched a public auction to construct projects to provide more than 1,000 megavolts of energy from renewable sources (mainly solar and wind). Additionally, Vaca Muerta (a rock formation in the province of Neuquén where a large oil and natural gas discovery was made in 2010 and it is considered to be one of the largest shale fields in the world) has attracted a lot of attention from foreign investors, who have positioned themselves in the area with substantial success, thereby creating multiple opportunities for related businesses.
I OVERVIEW OF M&A ACTIVITY

While 2017 was one of the top years in terms of M&A activity since 1988, with the years 2000 to 2007 being the strongest, peaking in 2005 with over 500 deals, both the number and the aggregate volume of transactions were significantly down in 2018. The number of deals fell from 345 to 324 (i.e., by 6.1 per cent), and transaction volume was reduced from €14.7 billion to €7.9 billion (as recently published in the EY M&A-Index Austria 2018). The same holds true for ‘blockbuster’ deals with a volume in excess of €1 billion: there were only two in 2018 (as compared to four in 2017). As previously, the vast majority of transactions were entered into by strategic investors; nevertheless, there was also a significant increase in financial investments (by private equity and venture capital investors) of roughly one-third (from 20 to 27 deals).

In terms of statistics, the EY M&A-Index Austria 2018 reveals that:

a domestic deal activity was down by 28 deals and 28.9 per cent, respectively;

b inbound investment by foreign investors into Austrian companies fell by nine deals and 6.8 per cent, respectively;

c there was a significant increase in outbound investment by Austrian investors, by 16 deals and 13.8 per cent, respectively; and

d the overall number of 324 transactions during 2018 was segmented into 69 domestic transactions (21.3 per cent), 123 inbound transactions (38.0 per cent) and 132 outbound transactions (representing 40.7 per cent of the number of deals).

In terms of industry sectors, investments in industrial targets (81 deals) outnumbered transactions in the technology sector (73 deals) and the real estate sector (72 deals), in each case by a close margin; in terms of deal volume, the real estate sector continues to lead the rankings (with an aggregate deal volume of €2.4 billion versus €1.9 billion in the industrial sector). As in previous years, among foreign investors into Austrian targets, German investors formed the strongest and most active group (with a total of 40 deals equalling a 32.5 per cent share); globally, foreign investment into Austria could be segmented into investments sourced in Europe (63.5 per cent), Asia (33.9 per cent) and the United States (2.6 per cent).
II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The main corporate law statutes are the Stock Corporation Act and the Limited Liability Company Act for corporations, and the Enterprise Act for partnerships. The Takeover Act and the Stock Exchange Act, supplemented by the Market Abuse Regulation, are relevant for listed companies (in relation to, public takeovers, stake-building, ad hoc disclosure, insider trading, directors’ dealings, etc.), whereas for private companies they do not apply. Merger control issues are governed by the Cartel Act, unless the EU Merger Regulation applies. In relation to corporate reorganisations, such as mergers, spin-offs and squeeze-outs, in particular the EU Merger Act, the Demerger Act, the Shareholder Squeeze Out Act and the Transformation Act complement the general corporate law statutes, while from a tax perspective the Reorganisation Tax Act provides for roll-over treatment under certain conditions. From a general tax perspective, the Corporate Income Tax Act as well as the Individual Income Tax Act are of most relevance, with, inter alia, transfer taxes being primarily subject to the Stamp Duty Act and the Real Estate Transfer Tax Act. In the employment law area, the Labour Constitution Act and the Act on the Amendment of Employment Contracts (AVRAG) are to be taken into account. In addition, for specific industries, sector-specific laws apply, such as the Banking Act, the Securities Supervisory Act, the Insurance Supervisory Act or the Telecom Control Act.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

A notable recent change in the legal framework relates to listed companies; historically, companies admitted to trading to the regulated Official Market of the Vienna Stock Exchange could not be voluntarily delisted unless in the form of a ‘cold delisting’ (as a consequence of a restructuring or if the preconditions for a listing ceased to apply). Thus, an admission to a regulated market was tantamount to a one-way street. In 2018, the legislator finally introduced an optional voluntary delisting (upon application of the issuer) subject to a vote or request of shareholders representing 75 per cent of the share capital; and, as alternatives, a takeover offer addressed to the remaining shareholders or an alternative listing in a different Member State being maintained. While mandatory offers or takeover offers are, likely to Austria’s limited market size, traditionally rare as M&A structuring instruments, we consider that this delisting option may create an incentive for more takeover offers being made in the future (there has been one precedent, Pankl Racing Systems AG, seen promptly upon the introduction of the new law).

Partial takeover bids (addressed to all shareholders of a listed company, but with an acceptance cap) also remain a popular tool for purposes of increasing an existing shareholding below the formal control threshold of 30 per cent (unless lowered in the articles of association, as implemented by several Austrian companies in particular in the recent past); partial takeover bids may also be submitted by the issuer itself thus acquiring its own shares, for example for purposes of acquiring treasury shares (which may be cancelled or designated for other purposes such as an acquisition currency, or for employee or management stock option programmes).

No change has been made to the formal control threshold of 30 per cent, which has been in place since 2006 and which triggers a mandatory bid obligation for all shares in the target, or are even limited to only 26 per cent, which is the ex lege cap of exercisable voting
rights (unless another shareholder holds voting rights in excess of that threshold or a bid is launched). Often, however, such bid is followed by subsequent bids, which usually triggers a mandatory offer.

Another recurrent topic is access to documents and information to conduct due diligence. In this context, certain differences depend on the legal form under which the target is established (largely based on the differentiation between whether a company is privately held, forms part of a group or is publicly listed).

As a general rule, in the case of stock corporations, third parties do not have a right to obtain information from the stock corporation apart from those pieces of information that are publicly available; the disclosure of any non-public information by a company is subject to a decision of its management (the management board in the case of joint-stock corporations, and managing directors in the case of limited liability companies), which must be taken in consideration of, inter alia and most importantly, the interests of the company (and not its shareholders). A board is thus not obliged to disclose confidential information to a prospective buyer. Even shareholders’ information rights are subject to important restrictions. Shareholders can request financial statements, including the management report as well as the supervisory board report. Furthermore, shareholders have an individual information right at the shareholders’ meeting in relation to items contained in the agenda, and to the extent such information is necessary to properly assess an agenda item. Given that such information will usually not suffice for the purposes of due diligence by a potential investor, shareholders will often request the management to disclose additional information. The decision on the disclosure of confidential information, and thus the decision on the admission or refusal of a due diligence, is a management measure, and thus generally does not require the consent of the supervisory board or the shareholders. The management has to avoid any damage to the company, and must consider all potential advantages, risks and disadvantages. Positive impacts may include, for example, new or cheaper means of financing, access to new customers or markets, access to product or technical know-how, and advantages for the company’s production or procurement or access to additional funding. Negative impacts could arise if, for example, a competitor or a major supplier or customer of the target can access the information. The decision to allow due diligence is not necessarily an all-or-nothing decision; the greater the interest of the company in a transaction underlying the due diligence request, the greater amount of sensitive data can be disclosed as well. The interest of shareholders also has to be taken into account by the management, whereby shareholders should generally be treated equally in equal situations. Another aspect to consider is the time frame. The more advanced the stage of the acquisition process, the more comprehensive and detailed the information that can be made accessible to the buyer. Due diligence will mostly only be permitted if the buyer’s intention to commit to a purchase has become more specific, for example by it signing a letter of intent. At the same time, the prospective buyer should also sign a non-disclosure agreement as a standard precautionary measure.

The situation for limited liability companies is generally comparable to that of stock corporations. Although its shareholders have only limited access to information rights, the Austrian case law has long established that every shareholder has to be granted a comprehensive information claim. Therefore, managing directors are, in general, obliged to provide requested information to shareholders. However, this information claim does not apply without restriction. The purpose of the comprehensive information right is to monitor managing directors, to control the business situation of the company and to prepare for general meetings. This information claim should thus only be used for these objectives. Accordingly, there is
some legal argument in Austria that the information claim would not include a due diligence for the sale of shares; meanwhile, others argue that managing directors may not deny access to documents or information for purposes of a due diligence. Overall, a due diligence claim by a shareholder of a limited liability company must be honoured, if and to the extent that it is essential for selling the shares to a potential buyer, and the shareholder’s request is not a misuse of the law (e.g., if the shareholder intends to avoid disclosure of the information to a prospective buyer), but only to the extent that is necessary to sell the shares, and only insofar as the interests of the company are not negatively affected. Regarding the question of what information the seller is allowed to share with a potential buyer, the company’s confidentiality interests must be carefully weighed against the shareholder’s interests in the dissemination of information, and will often require a shareholder resolution (at least in scenarios in which the sale of the shares is subject to shareholders’ approval). The shareholders of a limited liability company are subject to the duty of loyalty to the company and to the other shareholders. The nature of such duty of loyalty among the shareholders means paying due regard to the legitimate interests of the other shareholders even when exercising their voting rights.

M&A data protection is also in the spotlight. The General Data Protection Regulation (GDPR) came into effect on 25 May 2018. For the seller side in an M&A process, there are important GDPR concerns to be aware of. During a due diligence, there are potential risks of data and privacy breaches, when sensitive information is shared between potential buyers and the seller company. For the buyer side, the company’s GDPR compliance or readiness must be taken into account during the due diligence process if the potential acquisition target does business in Europe or deals with data related to European citizens, even if the company does not have a physical office location in the EU. The GDPR is a comprehensive set of rules and regulations, and there are several important steps organisations must carry out in order to comply, such as a classification of all personal data being processed by a company, performance of risk assessments, implementation of specific processes, and notifications of the competent authorities and – in some scenarios – the individuals who have been affected by a breach. Further, individuals have important rights under the GDPR (such as the right to be informed, the right of access and rectification, right of data portability, etc.). To avoid fines for non-compliance, which can be substantial, companies will need to have an in-depth understanding of where personally identifiable information is stored and processed throughout the organisation and will have to transfer such information into a record of all processing activities. Various opening clauses provide Member States with discretion to introduce additional national provisions to further specify the application of the GDPR. In this context, the Austrian legislation provides that declarations of consent to the processing of personal data lawfully obtained according to the current data protection framework shall remain valid under the GDPR if such declarations also comply with the new regulations of the GDPR. As Austrian case law has already been rather strict in this respect in the past, it can be expected that the need to adapt existing declarations of consent may be lower in Austria compared to other European countries. Compliance can potentially be very expensive, and these costs should be considered very carefully when it comes to the purchase price of a target company. Further, fines related to non-compliance with the GDPR can be very high – in some cases up to 4 per cent of the company’s prior year worldwide revenue or up to €20 million. Based on the announcement that the staff of the Austrian data protection authority will be increased significantly, it can be assumed that breaches of the GDPR will soon be prosecuted systematically.
FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

As a basic principle, there is no general foreign investment control or supervision regime in place in Austria.

However, under the Foreign Trade Act, the acquisition of an interest of 25 per cent or more, or a controlling interest in an Austrian business by a foreign investor (for the purposes of this law, that is an investor domiciled outside of the EU or the EEA and Switzerland; if the investor is resident in these regions or country, no advance approval is required, but *ex officio* investigations can be initiated without time limit) is subject to advance approval by the Austrian Minister of Economic Affairs where that business is involved in internal and external security (e.g., defence and security services) or public order and security, including public and emergency services, such as hospitals, emergency and rescue services, energy and water supply, telecommunications, traffic or universities and schools. Transactions subject to approval cannot be completed pending approval. Failure to obtain approval is subject to imprisonment and criminal penalties.

The acquisition of ownership and certain lease interests in real estate by non-EEA nationals or the acquisition of control over companies owning such interests is subject to notification or approval by the local real estate transfer commission. What interests are covered and whether notification or approval is required varies among the pieces of legislation of the nine states in Austria. Where the real estate is used for commercial rather than residential purposes, approvals are usually granted.

In regulated industry sectors (e.g., banking, insurance, utilities, gambling, telecoms or aviation), the acquisition of a qualified or a controlling interest is typically subject to advance notification to, or approval of, the competent regulatory authority. Sanctions for failure to notify or obtain approval in advance range from monetary penalties to a suspension of voting rights or a partial or total shutdown. Although such rules also apply to domestic investors, they usually are a more burdensome hurdle in the cross-border context.

SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

**Significant transactions**

During 2018, in terms of deal volume the market saw several notable transactions.

The five largest deals involving Austrian targets or other participants involved the following:

a OMV Aktiengesellschaft, a publicly listed oil and gas company that counts Austria and Abu Dhabi among its core shareholders, acquired a 20 per cent share in offshore licences for two oil fields in Abu Dhabi. Thus, OMV AG managed to substantially increase its reserves to approximately 450 million barrels. Upon its announcement, the agreed consideration and purchase price amounted to more than €1.2 billion. Later, in January 2019, OMV proceeded to acquire a 50 per cent share in Abu Dhabi’s national oil company, ADNOC Refining, and an additional 50 per cent share in a yet-to-be-established trading joint venture for an estimated purchase price (subject to adjustments) of US$2.5 billion. This transaction continues an extended sequence of outbound transactions that OMV AG has entered into over the past decade.

b ZKW Holding GmbH, the top company of a lighting and electronics systems specialist domiciled in Austria with a staff of over 3,500 in Austria and 9,000 worldwide, was acquired by South Korean LG Electronics for a consideration of more than €1.1 billion.
In the process, LG as acquirer agreed to grant job guarantees for employees domiciled in Austria. As per market sources, the transaction was concluded within the framework of a competitive auction process involving other prominent industrial bidders.

c Austrian AHT Cooling Systems GmbH, a specialist in cooling technology, which has been owned by a financial private equity investor (Bridgepoint Capital) since 2013, has now been acquired by a group company of a Japanese strategic investor, Daikin Europe NV, for a consideration in excess of €880 million. The parties to the transaction have stressed that synergies should enable a continuation of the global growth of the combined group.

d As a rare example of transactions involving publicly listed companies, a significant stake (blocking minority) in real estate company CA Imobilien Anlagen AG has been sold by its core shareholder and competitor, the publicly listed IMMOFINANZ AG, to the US-based Starwood Capital Group. The transaction involved a participation of 26 per cent in the share capital plus four registered shares (vesting special shareholders and nomination rights). The aggregate consideration amounted to approximately €750 million, which corresponds to €29.5 per share. The acquirer later also published a partial bid to the other shareholders in CA Immo, which was, however, only accepted by a small number of shareholders (only approximately 150,000 shares have been tendered).

e As an example for a successful outbound transaction, technology group Andritz AG acquired Xerium Technologies, Inc, based in North Carolina, USA, for a total consideration of approximately €650 million. The target specialises in supplying manufacturers of paper machines and, in terms of transaction volume, has been the largest acquisition completed by Andritz AG to date.

ii Key trends and hot industries

Overall, the number and volume of transactions decreased during 2018 after the record year of 2017.

Outbound transactions by Austrian investors have been on the rise, as compared to a reduction in domestic and inbound transactions.

Notwithstanding, the aggregate consideration paid in inbound deals by foreign investors in Austria outnumbered that paid or committed in outbound transactions, with €3 billion being paid in the top five inbound deals, largely due to two high profile deals: the highest transaction volume for inbound deals was attributable to the automotive supply sector (ZKW/LG), whereas for outbound deals, this would be the oil and gas sector (OMV/ADNOC).

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Corporates have found that the financing environment has somewhat improved, in particular for those with strong financials. Banks are also more active in approaching blue-chip companies, so financing opportunities for acquisitions are rather good.

The financing environment for buyout transactions has remained more or less unchanged, and is quite different for domestic market participants (as opposed to

2 EY M&A-Index Austria 2018.
international players), which typically seek financing from domestic banks, and international financial sponsors, which are able to tap international banks (at least on large-cap deals). Leverage levels for large-cap transactions have gone up slightly to around 5 times EBITDA, and relative debt-to-equity ratios of 40 to 50 per cent. Small to mid-cap transactions are sometimes financed through equity alone, or by domestic or German banks. Leverage levels and relative debt-to-equity ratios generally tend to be lower for small to mid-cap transactions than for large-cap deals.

Where leverage is employed on small and mid-cap transactions, there is usually only senior and institutional debt, as mezzanine structures tend to add another layer of complexity that is often not supported by the limited transaction size. On large-cap transactions, mezzanine financing is sometimes considered but, given the limited transaction size, is ultimately seldom employed. High-yield instruments are usually only considered for post-completion refinancing, as the time and cost involved tend to be disproportionate to any gains on the pricing side.

Experience shows that certain limitations under Austrian corporate law are often unexpected for foreign investors when structuring a deal, particularly in relation to intragroup (financing) transactions: Austrian law generally prohibits the return of equity to shareholders (i.e., up-and-side-stream transactions) of both a limited liability company as well as a stock corporation (and is applied by the Austrian courts by analogy to limited partnerships with only a limited liability company or stock corporation as unlimited partner). Based on this principle, Austrian courts have established that a company cannot make any payments to its shareholders outside arm’s-length transactions except for the distributable balance sheet profit, in a formal reduction of the registered share capital or for the surplus following liquidation.

The prohibition on return of equity covers payments and other transactions benefiting a shareholder where no adequate arm’s-length consideration is received in return; in relation to acquisition financing, typical examples for critical and potentially inadmissible transactions include upstream, side-stream and cross-stream loans as well as security rights (such that, for instance, a target company is typically prohibited from granting personal or asset security for the acquisition debt of its (new) parent for the acquisition of target shares). To the extent a transaction qualifies as a prohibited return of equity, it is null and void between the shareholder and the subsidiary (and any involved third party, if it knew or should have known of the violation.) Breaches may also result in liability for damages. Most of the above principles are also applied by the Austrian courts by analogy to limited partnerships with a limited liability company or stock corporation as (the sole) unlimited partner.

Austrian courts have developed case law suggesting that a subsidiary may lend to a shareholder, or guarantee or provide a security interest for a shareholder’s loan, if it:

- receives adequate consideration in return;
- has determined (with due care) that the shareholder is unlikely to default on its payment obligations, and that even if the shareholder defaults, such default would not put the subsidiary at risk; and
- that the transaction is in the interest of the Austrian subsidiary (corporate benefit).

In addition, the Austrian Stock Corporation Act prohibits a target company from financing or providing assistance in the financing of the acquisition of its own shares or the shares of its parent company (irrespective of whether the transaction constitutes a return of capital). It is debated whether this rule should be applied by analogy to limited liability companies. Transactions violating this rule are valid, but may result in liability for damages.
VII  EMPLOYMENT LAW

In the case of a transfer of a business within the meaning of the Act on the Amendment of Employment Contracts implementing Directive 2001/23/EC on safeguarding employees’ rights on transfers of undertakings, businesses or parts of businesses (Transfer of Undertakings Directive), the employment relationships of the employees associated with the business transfer together with the business to the purchaser (Section 3 Act on the Amendment of Employment Contracts). Employees can object to the transfer of the employment relationship within one month if the purchaser does not maintain dismissal protection pursuant to a collective bargaining agreement or take over pension commitments based on a single contract. This does not apply if the seller ceases to exist (e.g., in the case of a legal merger).

The Austrian Supreme Court has held that a dismissal of employees in the course of an asset sale (both by the seller and the acquirer) is against good morals (bonos mores) unless there are valid economic, technical or organisational reasons unrelated to the asset sale. If dismissals occur in close proximity to an asset sale, there is a (rebuttable) presumption that such exceptions do not apply. In addition, the general rules of Austrian employment law concerning appeals against dismissals apply.

There is no special protection against a dismissal in the context of a share sale (i.e., where not the business as such but the company is transferred). Only general rules of Austrian employment law concerning appeals against dismissals apply.

Another area of interest to investors is whether there are obligations to inform or consult employees or their representatives, or to obtain employee consent to a share sale or an asset sale. If a works council is established at the target company, the target company must inform the works council in accordance with Section 109 of the Labour Constitution Act, and consult with the works council on request in relation to a share deal. If no works council is established, no information or consulting requirements apply. In relation to an asset deal, the following has to be observed: the Labour Constitution Act provides for information and consultation rights of the works council in general, as well as specifically in relation to certain transactions and changes to a business. The information must be given sufficiently in advance, in writing and in a manner that allows the works council to assess the relevant transaction or change. The information must specifically include the reason for the transaction or measure, and the legal, economic and social consequences as well as any associated measures that may affect employees. The works council must be given an opportunity to comment on the transaction and propose measures mitigating adverse effects for employees. Where no works council is established, an asset sale only triggers information requirements if a transfer of a business is concerned. In that case, the seller or the purchaser must provide certain information to the employees affected. Affected employees do not, however, have consultation rights. There is no obligation to obtain the consent of the employees affected. However, where by operation of Section 3 of the AVRAG a transfer of a business results in the transfer of an employee to the purchaser together with the business, the employee can object to the transfer in certain limited circumstances (see above).

VIII  TAX LAW

As there is no tax exemption for capital gains realised from the sale of shares in an Austrian company (as opposed to shares in a foreign company), foreign investors will often choose an acquisition vehicle in a foreign country with which Austria has concluded a double taxation treaty that provides that only such other jurisdiction is entitled to tax the capital gains.
On the other hand, an Austrian acquisition vehicle allows the establishment of a tax group between the acquisition vehicle that incurred the debt and the target, which enables the purchaser to offset the interest expenses for the acquisition from the operational profits of the target. In general, non-Austrian corporations may also be part of an Austrian tax group, and their respective losses may reduce the Austrian tax burden under certain circumstances. However, such attribution of losses is limited to 75 per cent of the income subject to tax in Austria. Remaining losses may be carried forward.

Furthermore, foreign investors will usually opt for structures that avoid or minimise withholding tax. Dividends and interest payments are generally subject to withholding tax of 27.5 per cent (25 per cent in cases of corporations as the recipient). However, limitations and exemptions apply under domestic law as well as applicable tax treaties. In particular, withholding tax on dividend payments to non-Austrian investors is typically subject to the limitations under the EU Parent-Subsidiary Directive and applicable double taxation treaties. Interest payments on loans to non-Austrian lenders are, in principle not subject to Austrian withholding tax.

Debt-financed acquisitions should be structured carefully to secure the deductibility of interest as well as the offsetting of such interest expenses from business profits of the target company. Interest expenses are, for instance, not deductible in Austria if the interest is not taxed at the level of the related party lender at an effective tax rate of 15 per cent or more. It is worth noting, however, that there are no statutory rules on thin capitalisation in Austria. From a practical perspective, tax authorities usually accept debt-to-equity ratios of around 3:1 to 4:1. Besides the non-deductibility, the breach of such ratio would also result in interest payments being treated as deemed dividends, which – unlike interest on shareholder loans – would be subject to withholding tax in Austria (see below). Finally, it is worth noting that there is currently no interest barrier rule providing for a general limit on the deductible amount of interest expenses paid to unrelated parties (see below).

Besides the developments mentioned above, tax audits in relation to M&A deals are becoming more common and burdensome. In particular, transfer pricing issues, for example, in relation to interest on shareholder loans or certain fees payable to related entities, are under scrutiny. Accordingly, tax rulings are also becoming more popular.

Since 2019, controlled foreign company (CFC) rules and a legal definition for abuse of law are in place. In this context, the inclusion of the existence (or non-existence) of an abuse of law in the scope of binding tax rulings is likely to have high practical relevance. In Austria, the introduction of an interest barrier rule foreseen under the BEPS Anti-Avoidance Directive has been deferred for now. Although the European Commission initiated respective infringement proceedings against Austria, financing structures with unrelated parties should not be challenged by the tax authorities for the time being. If combined with intragroup financing, limitations, in particular thin capitalisation and the arm’s-length principle, have to be observed.

**IX  COMPETITION LAW**

The following types of concentrations are subject to merger control (intragroup transactions are exempt) under the Austrian Cartel Act:

- the acquisition of an undertaking or a major part of an undertaking, especially by merger or transformation;
- the acquisition of rights in the business of another undertaking by management or lease agreement;
c. the (direct or indirect) acquisition of shares, if thereby a shareholding of 25 per cent or 50 per cent is attained or exceeded;
d. the establishment of interlocking directorships where at least half of the management or members of the supervisory boards of two or more undertakings are identical;
e. any other concentration by which a controlling influence over another undertaking may be exercised; and
f. the establishment of a full-function joint venture.

A concentration must be notified to the Federal Competition Authority (FCA) if the following cumulative thresholds, which in an international comparison context are rather low, are fulfilled (based on the revenues of the last business year): the combined worldwide turnover of all undertakings concerned exceeds €300 million; the combined Austrian turnover of all undertakings concerned exceeds €30 million; or the individual worldwide turnover of each of at least two of the undertakings concerned exceeds €5 million.

However, even if the above thresholds are satisfied, no obligation to notify exists if the Austrian turnover of only one of the undertakings concerned exceeds €5 million; or the combined worldwide turnover of all other undertakings concerned does not exceed €30 million.

For calculating the turnover thresholds, the revenues of all entities that are linked with an undertaking concerned as defined under the Cartel Act are considered one entity (thus the turnover of a 25 per cent subsidiary must be attributed fully). Indirect shareholdings only have to be considered if the direct subsidiary (of at least 25 per cent) holds a controlling interest in the indirect subsidiary. Revenues of the seller are disregarded (unless the seller remains linked with the target undertaking as defined under the Cartel Act). Specific provisions for the calculation of turnover apply for mergers in the banking, insurance and media sectors.

Transactions that are notifiable in Austria may have an EU dimension under Article 1 of Regulation (EC) No. 139/2004 on the control of concentrations between undertakings (Merger Regulation). In that case, the European Commission generally has sole jurisdiction to assess such case. However, the Cartel Act contains specific rules regarding media mergers, which require a filing with both the European Commission and the FCA.

The relevant merger authorities in Austria are the FCA and the Federal Cartel Prosecutor, collectively referred to as the Official Parties, and the Cartel Court.

The Official Parties assess notifications in Phase I proceedings. Should a notification raise competition concerns, either official party may apply to the Cartel Court to open Phase II proceedings. Decisions of the Cartel Court may be appealed before the Supreme Cartel Court. The Competition Commission is an advisory body that may give (non-binding) recommendations to the FCA as to whether to apply for an in-depth Phase II investigation of a notified transaction.

A notifiable transaction must not be implemented prior to formal clearance. Possible sanctions for the infringement of this suspension clause are that the underlying agreements or acts are declared null and void, or the undertakings may be fined up to 10 per cent of their worldwide annual turnover (by the Cartel Court on application of the Official Parties).

Non-compliance with remedies imposed on the parties is equivalent in seriousness to breaching the suspension clause and may lead to similar fines.

A merger must be prohibited if it is expected to create or strengthen a market-dominant position. An undertaking is generally considered market-dominant for that purpose if it can act on the market largely independently of other market participants (the Austrian Cartel Act
contains a rebuttable presumption of market dominance if certain market share thresholds are achieved). Even where a merger is expected to create or strengthen a market dominant position, it must nevertheless be cleared if either it will increase competition, and therefore the advantages gained by implementing the transaction will outweigh the disadvantages; or it is economically justified and essential for the competitiveness of the undertakings concerned.

A media merger will be assessed not only against its compatibility with the competition rules, but also as to its adverse effects against media plurality.

X OUTLOOK

It is rather difficult to predict prospective market developments for the imminent future due to macroeconomic developments (e.g., Brexit) that may change the current investment environment in Europe and internationally. Generally, the first half of 2019 continued to be active and, based on the assumption that the economy remains stable, the Austrian M&A market should continue its previous performance. This outlook is also supported by the fact that private equity firms hold substantial cash reserves to be invested, and that many of their portfolio companies are overdue to be sold again.
I OVERVIEW OF M&A ACTIVITY

Following a slight recovery of 2017, Brazil’s economy experienced a modest growth in gross domestic product (GDP) of 1.1 per cent in 2018. M&A activity followed this lead. According to PricewaterhouseCoopers, there were 658 transactions in 2018, representing an increase of 2.3 per cent compared to the 643 deals completed in 2017. Foreign investors conducted 231 transactions, representing an 8 per cent decrease comparing to the 252 deals recorded in 2017, and private equity activity was down to 136 transactions among Brazilian and non-Brazilian investors, compared to 147 transactions in 2017.

Major deals announced in 2018 with Brazilian involvement included:

a. Boeing’s US$4.2 billion joint venture with Embraer;
b. Rhône Capital’s acquisition of Fogo de Chão for US$560 million;
c. Kroton Educacional’s acquisition of Somos Educação for US$1.5 billion; and
d. Suzano Papel e Celulose’s merger with Fibria Celulose, with a value of 36.7 billion reais.

The results of the presidential and Congress elections in October 2018 gave the market a more optimistic outlook for M&A activities in the first quarter of 2019. Although the expectations have not been fully met, the market was still very active and performing well: there were 233 announced transactions for a total aggregate value of 29.5 billion reais.

Deals announced to date in 2019 include the ongoing US$905 million acquisition of Nextel Brasil by América Móvil, the acquisition of Chevron Brasil by PetroRio for US$400 million, the ongoing US$615.5 million sale by Odebrecht Mobilidade of Supervia - Concessionária de Transporte Ferroviário to Guarana Urban Mobility, the 2 billion reais sale by Odebrecht Rodovias of Concessionária Rota das Bandeiras to Farallon Capital Management, and the acquisition of 100 per cent of the capital stock of Drogaria Onofre Ltda (owned by subsidiaries of CVS Health Corporation) by Raia Drogasil SA, Brazil’s largest pharmacy retail chain.

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1 Adriano Castello Branco and Claudio Oksenberg are partners and João Marcelino Cavalcanti Júnior is a senior associate at Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados.
3 Ibid.
II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A are regulated mainly by the Brazilian Corporation Law,\(^5\) and rules, regulations, opinions and precedents of the Brazilian Securities Commission (CVM) (CVM Regulations), including:

- **a** CVM Rule No. 319 (mergers involving public companies);
- **b** CVM Rule No. 358 (disclosure of material information by public companies);
- **c** CVM Rule No. 361 (tender offers);
- **d** CVM Rule No. 481 (disclosure of information prior to shareholders’ meetings and proxy solicitations);
- **e** CVM Rule No. 561 (remote participation and voting of shareholders at shareholders’ meetings);
- **f** CVM Rule No. 565 (disclosure requirements for M&A transactions);
- **g** CVM Rule No. 567 (disclosure requirements regarding share buyback programmes and transactions with own shares);
- **h** CVM Rule No. 568 (use and disclosure of information of significant investments in listed companies);
- **i** CVM Rule No. 570 (application of remote voting rules);
- **j** CVM Opinion No. 34 (conflicts of interest);
- **k** CVM Opinion No. 35 (fiduciary duties);
- **l** CVM Opinion No. 36 (poison pills); and
- **m** in the case of companies listed on the Novo Mercado or Level 2 listing segments of B3 (the São Paulo Stock Exchange), the corresponding listing rules (in addition to tax, antitrust and regulatory rules).

M&A deals involving solely closely held companies are only subject to the provisions of the Corporation Law (excluding those provisions exclusively applicable to publicly held companies), and the Brazilian Civil Code if they are limited liability companies (*limitadas*). Transactions that involve public companies, in addition to the CVM Regulations, are also regulated by the applicable listing rules.

Foreign investment is restricted in certain industries as follows:

- **a** aviation: after several legislative initiatives in recent years to end the limitations to non-Brazilian capital on the voting capital of Brazilian airline companies, such nationality restrictions are no longer applicable after the approval of Law 13,482/19 on 17 June 2019;
- **b** public services: telecommunications, electric energy distribution, gas distribution and rail transport, to name but a few public services in Brazil, are provided directly by the government (by means of state-owned companies) or by private parties who become responsible for the provision of such services through the execution of concessions agreements, permissions or authorisations As a rule, non-Brazilian investment is allowed, subject to certain restrictions (for instance, transfers of control of public service concessionaires may be subject to prior government approval);
Brazil

c real estate: the acquisition of rural land in Brazil by foreigners is subject to certain restrictions, which may apply to Brazilian companies where the majority of the capital is held or controlled by foreigners (e.g., prior authorisation from a government authority may be required for title transfer);
d mining: foreign investment must be made through a Brazilian entity, with mining in national border zones being restricted (transfers of mining rights are also subject to prior government approval);
e oil and radioactive minerals are a Brazilian state monopoly; oil-related activities by private or state-owned companies are subject to concession or authorisation;
f radio and television broadcasting and journalistic companies: foreign capital is limited to 30 per cent of the company’s capital; and
g banking: subject to the prior approval of the government, in addition to Brazilian Central Bank approval (transfers of control of financial institutions or of significant stakes therein are also subject to prior government approval).

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

On 2 January 2018, the new version of the Novo Mercado listing segment rules (New Rules) came into force, with certain provisions already in effect that impact on specific tender offer proceedings. Essentially, the New Rules aim to demonstrate B3’s intention to simplify tender offer proceedings, adapt tender offers to the market’s reality and reduce the extensive provisions once considered mandatory in the by-laws of companies listed with the Novo Mercado. The main changes can be summarised as follows.

The previous Novo Mercado rules (Previous Rules) set a relative presumption of control for any shareholder, or group of shareholders, that holds shares enough to ensure an absolute majority of the votes in the last three shareholders’ meetings, even if such shares do not represent an absolute majority of the company’s total voting capital. This presumption was excluded from the New Rules, and the concept of control under the Novo Mercado New Rules is aligned with the Corporation Law.

A mandatory tender offer as a result of an acquisition of control is still an obligation under the Novo Mercado. Pursuant to the Previous Rules, in the case of an acquisition of control by several different transactions, the purchaser was required to pay the difference between the price of the tender offer and the amount paid for shares acquired by the purchaser in a stock exchange in the six-month period prior to the date of such acquisition of corporate control, which is no longer necessary under the New Rules.

As to a delisting tender offer (DTO) from the Novo Mercado, pursuant to the New Rules, the prior approval of the delisting by a shareholders’ meeting is no longer required. The DTO must be accepted (or the delisting consented to) by more than one-third of the free float shares, unless a higher quorum is set forth in a company’s by-laws. Furthermore, the requirement to launch a DTO may be even waived by a shareholders’ meeting installed in the first call with the presence of at least two-thirds of the free float shares and approved by the majority of holders of the free float shares attending the meeting. With respect to the price of the DTO, the rules of CVM Rule 361 will be generally applicable, as opposed to the

6 Shares not held by the controlling shareholders, its related persons and the management, and treasury shares.
Previous Rules, which had several specific provisions applicable only to companies listed on the Novo Mercado. The New Rules also eliminate the obligation that holders of the free float shares had to elect the appraiser that would determine the economic value of the company (for purposes of the price to be paid under the DTO) based on a list of three prospective appraisers recommended by the board of directors. Nonetheless, the price per share of the DTO must be fair (based on book value, market value of the company’s assets, discounted cash flow, comparable multiples, market value or any other criteria accepted by CVM), and it can be challenged by minority shareholders with at least 10 per cent of the company’s outstanding shares, according to the Corporation Law.

Concerning a tender offer for the cancellation of a company’s registry as a publicly traded company, pursuant to the New Rules, it will follow the relevant proceedings set forth in CVM Rule 361, as opposed to the Previous Rules, which had a set of specific provisions applicable for such tender offer.

Finally, with respect to the board of directors’ opinion, required within a time frame of up to 15 days counted as of the release of a tender offer’s public notice, under the New Rules, in addition to the convenience and opportunity of a tender offer and the strategic plans of an offeror (which were already provided under the Previous Rules), the opinion must also state the available alternatives to the acceptance of the tender offer in the market, aiming to enable investors to be informed about the potential implications of choosing whether to participate in the relevant tender offer or not.

**IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS**

In 2018, Brazil experienced a slight downturn in foreign involvement in M&A transactions. Non-Brazilian investors saw a decrease in the number of transactions – 231 up to December 2018 – which represents a decrease of 8 per cent when compared to 252 transactions in 2017.7

Nevertheless, foreign investors took a leading role in major acquisitions announced in 2018. Examples of significant foreign investments in Brazil included the acquisition of the XL Group (and its Brazilian subsidiaries) by AXA Group for US$15.3 billion.

In November 2018, US-based Mohawk Industries acquired 100 per cent of the Brazil-based company Eliane Revestimentos Cerâmicos SA. The deal value was US$250 million.

In September 2018, Ardian acquired 40 per cent of Nuova Argo Finanziaria, which indirectly controls the management of important highways in Brazil, from Aurelia and Gavio Group for €850 million.

Also in September 2018, ExxonMobil and QPI Brasil Petróleo acquired Bloco Titá, an important oil extraction zone, from ANP for 3.12 billion reais.

In August 2018, Advent International acquired 80 per cent of Walmart Brasil for 1.9 billion reais.

In August 2018, Switzerland-based group Glencore completed its acquisition of a 78 per cent stake in the Brazil-based fuel distributor Ale Combustíveis. The deal value was 1.7 billion reais.

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V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

Some of the most active target sectors involved in announced M&A deals in Brazil in 2018 were information technology (IT), energy and power (including oil and gas), transportation, retail, financial and education.

In the IT sector, Digital Reality Inc, through its Brazilian subsidiary Stellar Participações, acquired 49 per cent of Ascenty, a large Brazilian data centre provider. The deal value was US$1.8 billion.

In the energy sector, Enel Brasil completed a tender offer for the acquisition of Eletropaulo, which is the company responsible for electricity distribution in the state of São Paulo, for 7.06 billion reais.

In the industrial sector, Omega Geração acquired 100 per cent of wind farm Assuruá, in the state of Bahia, from FIP IEER for 1.9 billion reais.

In the financial sector, Banco do Brasil acquired an assignment of claims portfolio from Votorantim for 593.8 million reais.

In the education sector, Neuberger Berman acquired 25 per cent of Uniasselvi, a distance learning institution, from Carlyle and Vinci Capital for 380 million reais.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

It is common knowledge that the cost of credit in Brazil remains prohibitively expensive. Acquisitions are usually funded via securities offerings (debt and equity) and bank loans, or via both. Private equity investment funds are also used as vehicles for funding in specific cases.

Furthermore, local financing is generally not available in all industries. Inbound cross-border investments are typically financed outside Brazil. Leveraged buyouts are not usual, although in certain cases (especially where the buyer is a local private equity fund) pre-acquisition debt is pushed down to the target following the closing (subject to certain conditions or requirements in cases in which the target is a listed company).

Security for acquisition financing normally consists of shares and assets, if any, of the target company, and guarantees of the acquiring group.

VII EMPLOYMENT LAW

Although the alternatives implemented by the Brazilian labour reform are still being adopted with caution by companies in general, in the first year following the enactment of the labour reform, the litigation numbers reveal a more business-friendly environment, and the constitutionality of some relevant changes to the labour legislation were confirmed by the Supreme Court.

i Litigation rates

Mostly due to the chances of being considered responsible for paying a company's attorney fees in cases where a labour claim is deemed groundless, in 2018 workers had filed 35 per cent less lawsuits than they had in 2017.
ii  Ratification of out-of-court agreements

Requests for the ratification of out-of-court agreements by labour judges, a procedure implemented by the labour reform, numbered more than 40,000 in the past year. This significant number reveals such mechanism was adopted as mutually beneficial tool for both workers and companies, allowing employees to receive their settlement amount within a limited period of time while granting employers legal certainty upon obtaining employees’ formal release.

iii  Outsourcing of services

Recent rulings of the Brazilian Supreme Court have confirmed the constitutionality of outsourcing activities irrespective of whether they are related to a contracting company’s core business, cancelling a contrary presumption established by a superior labour court precedent, without prejudice to the risk of recognition of a de facto employment relationship between an outsourced worker and the contracting company should employment features be observed in the rendering of services.

Union contributions

As result of the labour reform, the payment of union contributions (not included in this legal concept are the dues related to affiliated or associated members of a union) ceased to be mandatory and became voluntary. This change in legislation created significant backlash from employer and employee unions, and as a result, labour union income has decreased 88 per cent compared to the contribution amounts of the previous year. Despite a number of lawsuits (from labour unions representing employees or employers) challenging the labour reform in this regard, based on the freedom of association right, the Brazilian Supreme Court ruled in favour of the constitutionality of the labour reform provision under which contributions to unions are not mandatory, except in the event of an employee’s personal and previous written authorisation. Based on these union contribution conflicts, employment relationship negotiations have been impacted, resulting in a reduction in the number of direct collective bargaining agreements between employers and unions in relation to the years preceding the labour reform.

VIII  TAX LAW

This section presents general matters regarding the ultimate beneficial owner (UBO) disclosure requirements taking into account the recent rules enacted by the Brazilian Internal Revenue Service (RFB).

Normative Instruction No. 1,863634, dated 27 December 20186 May 2016, issued by the RFB (NI 1,863634), regulates the information that must be provided to the RFB in order for foreign investors incorporated as entities (NRIs) to obtain a national taxpayer identification number (CNPJ), which is required for an NRI to invest in the Brazilian financial and capital markets pursuant to the mechanism set forth by Resolution No. 4,373, dated 29 September 2014, of the Brazilian Monetary Council (4,373 investment and 4,373 investor), and also for an NRI to directly invest in Brazilian-resident legal entities pursuant to the mechanism set forth by Law No. 4,131, dated 3 September 1962 (4,131 investment and 4,131 investor).

When applying for a CNPJ, any prospective NRI must provide information regarding the respective legal representative in Brazil and its shareholding chain if it reaches an
individual (natural person) that is deemed to qualify as its UBO; or any of the entities listed in Paragraph 3 of Article 8 of NI 1,863634, which are exempt from disclosing the respective UBO (exempt entities).8

According to Article 8 of NI1,863634, an individual is deemed the UBO of the 4,373 or 4,131 investor if he or she ultimately, directly or indirectly, owns, controls or has significant influence over an entity, or is the individual on behalf of which a transaction is conducted. For the purposes of such rules, significant influence is deemed to exist whenever an individual owns more than 25 per cent of an entity's capital stock, directly or indirectly; or an individual directly or indirectly has, or exercises preponderance in, corporate resolutions, and has the power to elect the majority of an entity's directors, even without controlling it.

Furthermore, if the shareholding chain of a certain 4,373 or 4,131 investor reaches one of the listed exempt entities, there is no obligation to disclose the UBO. However, if there is an UBO, the RFB requires the disclosure of some personal information such as the UBO's date of birth, the UBO's country of birth and the UBO's country of residence, as presented in Annex XII of NI 1,863.

In addition to NI 1,634, the RFB issued Declaratory Act No. 09, dated 23 October 2017 (ADE 09/2017, jointly with NI 1,634 (UBO Regulation)) to further regulate the application of the UBO disclosure requirements. To do this, ADE 09/2017 also classifies the entities subject to UBO disclosure rules in three different categories: entities exempt from disclosing the UBO (group 1), entities resident abroad obliged to disclose information (group 2) and Brazilian-resident entities (group 3).

Group 1 entities correspond to the exempt entities listed by Paragraph 3 of Article 8 of NI 1,863634. Annex XII ADE 09/2017 provides that such entities are not obliged to provide information regarding the respective UBO considering their particular features, despite the information regarding the legal representative. Nonetheless, note that such waiver is only applicable if the 4,373 or the 4,131 investor qualifies as an exempt entity itself. On the other hand, group 2 entities are further categorised into three subcategories: those that obtain a

8 The following are listed as exempt entities: (1) legal entities, or their controlled companies, incorporated as publicly held company in Brazil or incorporated in countries that require public disclosure of all relevant shareholders, and that are not incorporated in favourable tax jurisdictions or submitted to a privileged tax regime; (2) not-for-profit entities that do not act as fiduciary managers and that are not incorporated in favourable tax jurisdictions or submitted to a privileged tax regime, as long as they are regulated and inspected by a competent governmental authority; (3) multilateral organs, central banks, governmental entities or those related to sovereign funds; (4) social security entities, pension funds and similar institutions, as long as they are regulated and inspected by a competent governmental authority in Brazil or in their country of origin; (5) Brazilian incorporated investment funds regulated by CVM, as long as the Brazilian Individual Taxpayers' Registry or the CNPJ of the respective quota-holders is informed to the RFB; (6) investment funds specially incorporated to manage complementary pension plan resources as well as insurance plans if regulated and inspected by the qualified public authority in its country of origin; and (7) collective investment vehicles domiciled abroad whose shares or equity holding representative securities are admitted to trading in markets regulated by an authority accredited by CVM; or collective investment vehicles domiciled abroad: (a) whose minimum number of shareholders is equal or higher to 100, provided no shareholder holds significant influence over the vehicle; (b) whose asset portfolio is managed by a professional manager registered before an authority accredited by CVM and in a discretionary manner; (c) which is subject to investor protection regulation by a regulation authority accredited by CVM; and (d) whose asset portfolio is diversified (i.e., the concentration does not amount to significant influence in the case of concentration in assets from a single issuer).
CNPJ through the RFB; those that obtain a CNPJ through the Brazilian Central Bank; and those that obtain a CNPJ from CVM. The information to be presented depends on the tier that the entity is ranked in.9

Besides this information, the UBO Regulation may also require some documents to be presented to the RFB up front, depending on the qualification of the 4,373 or the 4,131 investor, which must be reviewed on case-by-case basis.

Furthermore, note that there are deadlines for presenting the information and documents requested under the UBO Regulation. Failure to comply with the UBO Regulation may result in the suspension of a CNPJ, and the consequent inability of the 4,373 or 4,131 investor to carry out transactions in Brazil.

IX COMPETITION LAW

2018 was a year of important developments in the Brazilian merger control practice. The decisions taken by the Administrative Council for Economic Defence (CADE) in certain complex M&A transactions have demonstrated that the authorities continue to tend to take a rigorous approach in the analysis of those cases. Highlights included the increasingly active role of the Department of Economics Studies in the most complex merger cases, third-party intervention in merger cases, and the analysis of complex mergers that raise portfolio or conglomerate concerns.

The year’s highlights also included the publication of CADE’s Remedy Guide, aimed at providing general guidelines for the negotiation and implementation of remedies, and the increasing coordination and exchange of information between CADE and foreign competition authorities in the analysis of cross-border mergers.

CADE’s Remedy Guide

On October 2018, CADE issued the Antitrust Remedy Guide (Guide), which provides guidelines for the implementation of remedies in merger cases that raise competition concerns.

In accordance with the Guide, the implementation of remedies should observe the following principles:

- proportionality (meaning that a remedy must be necessary, adequate and sufficient to address concerns raised by a merger);
- timeliness (i.e., the remedy should address a concern as quickly as possible and in any case, in a timely manner);
- feasibility (that is, a remedy should be subject to easy implementation); and
- verifiability (meaning that CADE must be able to verify its fulfilment).

The Guide also sets CADE’s preferences in terms of types of remedies. In this sense, structural remedies (such as the divestiture of an asset) are preferred over behavioural ones (i.e., when the parties assume obligations, such as eliminating exclusivity clauses or maintaining non-discriminatory behaviour in supply agreements). The Guide expresses CADE’s concerns regarding remedies that may be difficult to monitor: it is desirable that the parties hire monitoring trustees to help CADE keep track of the fulfilment of the obligations assumed by

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9 Annex XII provides four additional tiers for entities qualified under this subgroup – each one of the entities is required to comply with different disclosure obligations.
the parties, and remedies should preferably not require continuous monitoring. The Guide also lists questionable remedies, such as obligations to make investments and the imposition of price caps.

Although the Guide is not binding, it is based on CADE’s experience and reflects the way CADE will likely approach remedies in future cases.

ii Increasingly complex analysis of M&A deals
The most recent complex cases that have been analysed by CADE show that the competition authority maintains a rigorous and sophisticated approach concerning the analysis of M&A transactions, which translated into an increasing number of cases challenged to CADE’s Tribunal, and blocked or approved with remedies:

a nine cases were recently challenged to the Tribunal and approved with remedies: Disney/Fox; AT&T/Time Warner; Itaú/Citibank; Bayer/Monsanto; ArcelorMittal/Votorantim; Dow/Dupont; WEG/TGM; Petrotemex/PQS; Itaú/XP; Praxair/Linde;

b four cases were blocked in 2017 and 2018: Kroton/Estácio; Ipiranga/Alesat; JBJ Agro/ Mataboi and Ultragaz/ Liquigas; and
c two withdrawals were made due to the risk of blocking: Owens-Illinois/Nadir and Saint Gobain/Rockfibras.

Portfolio or conglomerate effects, and coordinated effects
The analysis of conglomerate or portfolio effects are increasingly important, as CADE’s review becomes ever-more sophisticated. Examples include Bayer/Monsanto, BVMF/Cetip, Votorantim/ArcelorMittal, Tigre/Condor and Luxottica/Essilor, all of which involved important discussions about conglomerate effects; and Reckitt/Hypermarcas, Kroton/Estácio and Essilor/ Luxottica, in which portfolio effects were deeply analysed.

In addition, CADE has given a lot of attention to the analysis of coordinated effects, especially in sectors with a history of cartel convictions. Examples include Ipiranga/Alesat, ArcelorMittal/Votorantim, Prosegur/Transfederal, Bradesco/HSBC and Itaú/Citibank.

Third party-complaints
CADE is paying lot of attention to third-party complaints in the context of merger control cases. Such interventions have effectively affected both the timing and the results of the analysis of such cases (see, for instance, Petrotemex/PQS and Itaú/Ticket Serviços). There have also been third-party interventions through complaints about transactions that allegedly should have been notified to CADE, either because they met the thresholds criteria, or because of their potentially negative effects in the market (see All Chemistry/SM Empreendimentos Farmacêuticos).

Increasingly active role of the Department of Economics Studies in complex mergers
The Department of Economics Studies (DEE) is part of the Brazilian competition system and is responsible for advising the General Superintendence and CADE’s Tribunal in both merger review and conduct cases, as well as preparing studies to ensure CADE’s technical and scientific updating. The DEE had an important role in the recent analysis of the most complex merger control cases, such as Ipiranga/Alesat, Mataboi/JBJ, Ultragaz/Liquigás, Kroton/Estácio, ArcelorMittal/Votorantim, Bradesco/HSBC, Reckitt/Hypermarcas and British/Iberia/Latam. In
addition, the DEE has been taking an active role in its competition advocacy role, issuing studies and analyses of several sectors (such as the passenger and cargo air transport market, port services and fuel distribution).

iii  Cooperation between competition authorities

CADE continues to increase its cooperation and coordination with foreign antitrust authorities in cross-border mergers. Contacts between CADE and both the European Commission and the Department of Justice (United States) have been common for a while. The main goal is to exchange information and avoid conflicting decisions in cross-border cases. However, CADE has been diversifying its contacts with other foreign authorities: for instance, it has recently engaged in exchanges with the Russian and Indian authorities (regarding the Alstom/Siemens case).

Moreover, CADE has signed several memorandums over the past few years to regulate cooperation with other competition authorities. CADE has signed memorandums establishing cooperation between CADE and the competition authorities of several different countries such as South Africa and Russia, as well as a multilateral agreement with the BRICS\(^\text{10}\) economies, in recent years.

X  OUTLOOK

After a decrease in 2016 compared to recent years, and following the first signs of economic recovery, M&A activity increased in 2017 and 2018. The expectations for the remainder of 2019 are mostly positive. The outlook for M&A transactions in Brazil will certainly be enhanced by the approval and implementation of reforms proposed by the new Federal Administration, especially the pension system reform. The prospect of a combination of attractive prices, less expensive credit and banks willing to approve financing will benefit the volume of transactions in Brazil.

There have also been initiatives by the federal government to foster investments and create a better investment environment in general. For instance, the Provisional Measure of the Economic Freedom aims to reduce governmental bureaucracy and the amount of interference in private parties’ relations with the purpose of stimulating entrepreneurial activity in Brazil. Furthermore, in early 2019 the Ministry of Economy created an Inter-ministerial Committee for Digital Transformation, which is tasked with discussing, together with representatives of the civil society, how to create a better environment for business, entrepreneurship and innovation. Among the ideas being discussed by the Committee is a proposal for a Startups Act, which intends to reduce the obstructions to innovation and bureaucracy and enhance sustainable growth for emerging companies in Brazil.

With respect to scenarios or trends that can already be identified, it is possible to say that an important driver for M&A activity in Brazil will be the privatisation agenda, which is one of the main priorities for the government for this and following years and aims to attract the private sector to fill in infrastructure gaps. The main sectors announced to be privatised or awarded to private sector players include airports, ports, energy, railroads and roads, mining, and banking and related services. The government has already privatised 12 airports (including major hubs in northeast Brazil such as Recife) in 2019, and is in the

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\(^\text{10}\) Brazil, Russia, India, China and South Africa.
process of doing the same for major Brazilian ports. In addition, Petrobras has a continuing significant plan to divest non-core assets, such as its sale of 90 per cent of gas supplier TAG to Engie Group for US$8.6 billion, which was signed in April 2019.

As in previous years, the current foreign exchange levels may also continue to play a role in incentivising seasoned foreign investors (especially by private equity) to take advantage of investment opportunities in the country.

Finally, there are still industries with growth and consolidation potential (e.g., utilities, healthcare and education) that may be further explored as the country’s GDP continues to grow.
Chapter 9

CANADA

Cameron Belsher, Robert Hansen, Robert Richardson and Mark McEwan

I OVERVIEW OF M&A ACTIVITY

Canada saw 591 M&A deals announced in 2018 valued at US$91.3 billion overall. These results trended slightly downwards from 2017, when 628 deals worth US$97.5 billion were announced, but compare favourably to the US$77.5 billion invested in 668 deals in 2016. Deal counts fell and valuations rose for the first quarter of 2019, with the number of deals in 2019 decreasing to 129 from 153 in 2018, and aggregate deal values increasing from US$12.8 billion in 2018 to US$24.8 billion in 2019. The first quarter also experienced an increase in inbound M&A activity relative to the same period in 2018. This inbound activity, along with the trend towards fewer but higher-value deals, underlines the competition in the marketplace and the continuing confidence that buyers place in the Canadian market.

The most active sectors by deal count in 2018 were the technology, media and telecom industries, with 118 deals announced during the year for US$6.1 billion. However, energy, mining and oil and gas – all traditional drivers of deal flow in Canada’s resource rich economy – were close behind, with 115 announced deals and for a market-leading US$38.2 billion. The 95 announced deals in the industrials, manufacturing and engineering industries had an aggregate value of US$11 billion, making it the second most valuable sector in 2018. Cannabis, which was legalised for recreational purposes in late 2017, also became an important sector for M&A activity in 2018, as the top 20 cannabis deals of 2018 and 2019 accounted for approximately US$23 billion overall, over US$10 billion of which was deployed in 2019.

The Canadian private equity market continues to be a key driver of M&A activity, and enjoyed its second-best year since 2006 by deal value with overall activity declining only slightly in 2018 following sustained highs in activity and values. Aggregate deal value was C$48 billion, which was only slightly behind 2017’s high of C$53 billion, while deal volume experienced a modest dip to 303 deals from the all-time high in 2015 of 355. Funds continue

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1 Cameron Belsher, Robert Hansen and Robert Richardson are partners and Mark McEwan is an associate at McCarthy Tétrault LLP.
2 Mergermarket, Deal Drivers Americas FY 2018.
3 Mergermarket, Deal Drivers Americas FY 2018.
4 Mergermarket, Deal Drivers Americas FY 2018.
5 Mergermarket, Americas Trend Summary 1Q19
6 Mergermarket, Deal Drivers Americas FY 2018.
7 Mergermarket, Deal Drivers Americas FY 2018.
8 Mergermarket, Deal Drivers Americas FY 2018.
9 Pitchbook Data, Inc.
to fundraise actively, building on ever-increasing dry powder, and the market across Canada remains highly competitive, attracting interest from domestic and international investors. In 2018, there was a relative increase in private equity activity in the healthcare sector and a tightening of activity in the business-to-consumer and energy sectors, while the business-to-business, materials and resources, and IT sectors remained flat. The number of private equity exits was down approximately 20 per cent in 2018, but deal value increased by almost 40 per cent compared with the period running from 2015 to 2017.10

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

i Alternative transaction structures

In contrast to private M&A transactions in Canada, which are negotiated contractual arrangements set against a similar legal framework to the United States, public M&A transactions in Canada are subject to complex securities and corporate law regimes. Accordingly, Canadian dealmakers generally pursue one of two common methods to acquire control of a public company: a takeover bid or a plan of arrangement.

Takeover bids

A takeover bid is an offer made to a person in Canada to acquire outstanding voting or equity securities of a class of securities, which, if accepted, would result in the bidder (together with persons acting in concert with the bidder) owning 20 per cent or more of such class. Most commonly, a bidder will make an offer to all of the shareholders of a target company to buy their shares. Exactly the same offer must be made to all shareholders. This means that, subject to certain limited exceptions, it is not permissible to have collateral agreements with, for example, a controlling shareholder or a shareholder who is a senior officer that result in additional consideration flowing to that shareholder. The offer must remain open for shareholders to accept for at least 105 days (referred to as the bid period), subject to a target board’s ability to reduce the bid period to not less than 35 days in prescribed circumstances.

Any takeover bid must be subject to a non-waivable condition that a minimum of more than 50 per cent of all outstanding target shares owned or held by persons other than the bidder and its joint actors be tendered and not withdrawn before the bidder can take up any shares under the takeover bid. The takeover bid must also be extended by the bidder for at least an additional 10 days after the bidder achieves the minimum tender condition and all other terms and conditions of the bid have been complied with or waived.

Certain takeover bids are, however, exempt from compliance with these requirements, including transactions involving the acquisition of securities from not more than five shareholders of the target company, provided that the price paid does not exceed 115 per cent of the prevailing market price (referred to as the private agreement exemption).

If the bidder succeeds in acquiring at least 90 per cent of the target’s shares owned by third parties within 120 days of the commencement of the bid, then the bidder is typically able to effect a compulsory acquisition of the remaining outstanding shares pursuant to a process governed by Canadian corporate statutes. This process can take approximately 30 days, although timelines vary depending on the jurisdiction of incorporation of the target company. Alternatively, if the bidder acquires more than two-thirds of the outstanding shares,
the bidder may call a meeting of all of the shareholders of the target company for the purposes of voting on an amalgamation with an affiliate of the bidder. This vote can be generally be carried with two-thirds of the outstanding shares, and if approved can result in any remaining minority shareholders being squeezed out for the same consideration that was offered in the takeover bid. This second-step transaction takes longer than a compulsory acquisition because of the need to call a meeting of the shareholders of the target company.

**Plans of arrangement**

Most consensual acquisitions of Canadian public companies, however, are effected not by way of a takeover bid but through a statutory procedure under the target company’s corporate statutes. These statutes generally provide that companies can be merged, and their outstanding securities can be exchanged, amended or reorganised through a court-supervised process known as a plan of arrangement. Under this process, the target applies for an initial court order directing the target to seek the approval of its shareholders and fixing certain related procedural requirements. A second court appearance will be scheduled for shortly after the shareholders’ meeting for the court to consider the substantive fairness of a transaction, and at which any interested party may appear and object to the completion of the transaction. If shareholders vote to approve the transaction, typically by two-thirds of the votes cast at the meeting, and there are no meritorious objections from other interested parties, the court will approve and the transaction will proceed as intended. Plans of arrangement are often used to enable the shareholders of the target to exchange their shares for either cash or another form of consideration.

The plan of arrangement has two significant advantages in certain circumstances. One is that it allows for multiple transactions to happen simultaneously or in a specified sequence following shareholder and court approval. This is useful, for example, where there are multiple companies involved in the transaction, where several classes of equity and debt securities are outstanding, or where the sequencing of particular steps in the transaction is important to achieve an advantageous tax result. The other advantage to a plan of arrangement is that it will generally permit securities of the offeror to be issued to US holders of the target without requiring such securities to be registered in the US.

**ii Target board considerations**

Under the Canada Business Corporations Act (and other Canadian corporate statutes are substantially the same in this regard), directors have a legal obligation to act honestly and in good faith with a view to the best interests of the corporation; and exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

In the context of a potential M&A transaction, Canadian boards typically seek to discharge these duties by overseeing a process relating to the sale of a company. It is not mandatory that Canadian public companies be sold by way of an auction, and many companies are sold pursuant to a process whereby the target negotiates confidentially with one third party and then issues a press release after a support agreement has been signed. It is customary for these support agreements to include ‘fiduciary-out’ termination provisions, similar to the practices in the US market. At this stage, the target company’s board is recommending to its shareholders that they accept the transaction, but whether the bidder succeeds will depend upon the reaction of the shareholders. In the case of a takeover bid, the bidder will have to mail its takeover bid circular to target shareholders and its bid must be open for at least 35 days (provided the target company’s board has agreed to reduce the
bid period). In the case of a plan of arrangement, there is a period of approximately one month between the mailing of the target’s management information circular and the date of its shareholders’ meeting. In either case, during that time, potential competing bidders may come forward and seek to make a superior proposal. Depending on the terms of the support agreement, there may be obstacles to another potential acquirer making a superior proposal, including the size of any break fee and whether there is a right to match in the support agreement. In addition, some target companies in Canada have signed support agreements with go shop provisions whereby the target puts the bidder on notice that it intends to actively solicit higher offers from third parties.

iii Defensive measures

Any widely held public company with a depressed share price can be vulnerable to an unsolicited takeover bid. A target company will commonly react to a hostile takeover bid by initiating defensive measures. Although other potential responses may be available, two prominent defensive measures in Canada are shareholder rights plans and tactical private placements.

Shareholder rights plans

Until Canada’s takeover bid rules were amended in 2016 to increase the minimum bid period from 35 days to 105 days, shareholder rights plans were frequently used to delay a hostile bidder so that the target board had more time to canvass alternatives. Unlike in the United States, they could not be used to stop a hostile bid indefinitely. Now that Canada has a 105-day minimum bid period (subject to two exceptions), the formerly accepted rationale for shareholder rights plans has diminished significantly.

Shareholder rights plans nevertheless remain a relevant tool for deterring creeping takeover bids. Any purchase in the market that takes a shareholder above 20 per cent ownership of a target company requires the bidder to make a formal takeover bid to all the target’s shareholders on identical terms, subject to two key exceptions to the formal takeover bid rules. The first is a de minimis exemption that permits a shareholder to acquire shares in excess of the 20 per cent threshold through purchases of up to 5 per cent of the target’s outstanding shares annually at market prices. The second is the private agreement exemption described above. Many Canadian public companies have shareholder rights plans that prohibit the use of these two exemptions to acquire control of a company without offering an appropriate premium to all shareholders, and to prevent the acquisition of a negative control block that could deter a bid that the target board and other shareholders would find desirable.

Tactical private placements

There have been a small number of transactions in Canada in recent years where target companies have issued equity to friendly third parties at least in part to discourage hostile bids. Not only does the hostile bid become more expensive as a result, but the mandatory 50 per cent tender condition becomes harder to achieve.

Any private placement that impacts a hostile takeover bid may be challenged in court or before the securities regulators, or both. Relevant considerations in cases to date include:

a the timing of the private placement relative to a bid;
b whether the target required the financing;
c the impact of the private placement on the hostile bid or on a second bidder or locked-up shareholder; and
d whether the private placement was approved by shareholders.
iv Financing

In Canada, unlike in the United States, it is not permissible to make a takeover bid conditional on arranging financing. Before a bidder makes a cash takeover bid, it must have made adequate arrangements for its financing. Typically, the bidder will have signed a binding commitment letter with a bank or other source of funds prior to launching its takeover bid. The bidder will seek to have the conditions to the availability of the financing set out in the bank commitment letter as similar as possible to the conditions in the takeover bid circular that is sent to the target company’s shareholders. The law requires that the bidder must be confident that if the conditions to the bid are satisfied, the financing will be available.

III SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Private equity and pension funds

In Canada, domestic and international private equity firms and Canadian pension funds continued to have a major impact on both inbound and outbound transactions in 2018. Marquee transactions included Brookfield Infrastructure Partners’ acquisition of Enercare Inc, Searchlight Capital’s acquisition of Mitel and CPPIB’s consortium investment in the acquisition of Refinitiv and Ant Financial.

Private equity exits: dual-track processes

The parallel pursuit by equity sponsors of both an M&A exit and an initial public offering (IPO) is not a new development. Recent examples in Canada include GFL Environmental Inc opting for a sale to BC Partners in April 2018 over a go-public transaction, and the dual-track processes of Kinder Morgan Canada Limited and Neo Performance Materials Inc that culminated in IPOs in May and December 2017, respectively. However, private equity sponsors facing potentially volatile markets may rely on the dual-track process more heavily in the future to help increase valuations and to hedge against the risk of a failed or significantly delayed IPO. The US market has recently seen a significant uptick in dual-track processes, much of which has been driven by private equity sponsors, and many dealmakers expect such processes to become more common for significant sponsor exits in future years.

While a dual-track process may enhance valuations and pricing tension in certain circumstances, concerns may arise that a contemporaneous IPO is little more than a distraction from a sale process or an elaborate pricing exercise. These concerns, however, can be managed or moderated in a number of ways:

a Concerns relating to distractions, skepticism of bidders, market perceptions and confidentiality may be alleviated by a company making a ‘quiet filing’ with Canadian securities regulators. While the US Jumpstart Our Business Startups Act and recent policy changes from the US Securities and Exchange Commission allow for companies to file a registration statement confidentially, a similar blanket policy is not available for Canadian companies (other than in certain limited circumstances). As a result, confidential filings are generally not a common practice in Canada. However, in certain limited situations (including in certain dual-track processes), Canadian securities regulators may from time to time allow a preliminary prospectus to be filed on a confidential basis and allow a company to advance an IPO process to a certain point without any public disclosure. This permits the company to address comments from the securities regulators without having disclosed the prospectus to the public.
If the company then ultimately pursues a sale process, it can terminate the IPO. Prior consultation with the principal securities regulator is required in these circumstances to ensure that the regulator is aligned on the case for a quiet filing.

b Bidders’ concerns regarding the commitment of a company to an auction process running alongside an IPO process can be alleviated by offering break fees or expense reimbursements to a preferred bidder in a dual-track process. It is also important to note that the Canadian convention for underwritten IPOs is for the issuer to pay the expenses of the underwriters, including the fees of underwriters’ counsel (often up to a cap). If a company significantly advances an IPO but ultimately pursues the M&A track, the company will in most cases be required to reimburse the underwriters for their expenses (which can be significant, depending on the stage of the IPO). This is a significant difference from the convention in the US where underwriters typically pay the fees of their own counsel.

c Canadian securities laws provide for certain limited testing the water activities prior to the public filing of a preliminary prospectus (subject to a cooling-off period). These activities may allow for a company to confirm whether an IPO is a viable exit path before making a public filing as part of a dual-track process.

**Representations and warranties insurance**

While M&A representations and warranties insurance (R&W insurance) has become widespread in the US market, particularly in large or mid-market private equity deals, the Canadian market has been relatively slower in its adoption. Insurance brokers and dealmakers have, however, predicted over the past few years that it was only a matter of time before R&W insurance became increasingly prevalent in Canadian transactions. In 2018, this expectation became a reality. R&W insurance is now widely used by private equity firms and certain strategic acquirers in Canadian transactions.

A number of factors have led to the embrace of R&W insurance in Canada:

a Dispositions of Canadian assets are increasingly being managed through structured auction processes with the assistance of a financial adviser. In previous years, buyers would use R&W insurance (in lieu of, or as a supplement to, traditional indemnification) to competitively differentiate their bids. However, sophisticated sellers and financial advisers that are conducting robust auctions are now including, as part of the formal process, the requirement that any prospective buyer obtain an R&W insurance policy.

b Over the past year, R&W insurance policy terms have continued to become more attractive. Competition among underwriters has created downward pressure on premiums, which are now typically between 2.5 and 4 per cent of policy coverage. Retention amounts have also decreased significantly, with a retention amount of 1 per cent of the enterprise value now becoming standard.

c Just a few of years ago, policies contained numerous broad exclusions from coverage including in areas like tax, environmental matters, cybersecurity, pension funding and compliance with certain laws. This naturally led to specific or supplemental indemnities being negotiated in purchase agreements to ensure buyers still had recourse for these exclusions, which partially defeated the purpose of R&W insurance. As underwriters have become more sophisticated and have faced greater competition from new entrants into the market, the number and scope of exclusions have decreased considerably.

d Buyers have naturally been reluctant to shift from traditional indemnification to a relatively new insurance product due to concerns about claims recovery. In an effort to
increase adoption of the product and alleviate this concern, various prominent global underwriters have published reports that set out historical information promoting their claims coverage to build confidence in the effectiveness of the product among users.

R&W insurance brokers are becoming increasingly focused on the Canadian market. Many global insurance brokers have established permanent offices and staff in key Canadian markets to help market and place R&W insurance.

There is no question that there is growing acceptance of R&W insurance in the Canadian M&A landscape, especially where private equity firms are involved. Buyers and sellers are now seeing the transformative impact of R&W insurance on deal negotiation dynamics and post-closing relationships. As dealmakers become more familiar with the product, and in particular in a generally seller-friendly environment where underwriters seek to demonstrate that R&W insurance policies may provide more effective means of recovery than traditional indemnification, there is every reason to expect that the product will be further embraced in 2019, and that adoption rates will converge with those in the US in coming years.

ii The cannabis industry

The recent legalisation of cannabis for recreational purposes continues to stimulate deal-making both for M&A and capital markets transactions, and there were a number of notable deals announced during the year. While many cannabis companies were already engaged in the legal medical marijuana market prior to recreational cannabis becoming legal, their efforts to achieve scale and position themselves for new market opportunities, including in pursuit of outbound M&A deals and partnering with mature businesses in more traditional and established industries, was a key feature of M&A activity over the year. A notable transaction completed in June 2019 was Canopy Growth’s acquisition of a US$300 million call option to acquire US-based, publicly traded Acreage Holdings for a share-based consideration of US$3.7 billion, which option will be deemed to be exercised if the US federal government legalises the production and sale of cannabis.

The legalisation of cannabis at the federal level in Canada stands in contrast to the regulatory framework in the United States. Although a number of US states have legalised cannabis to some extent, it remains a controlled substance under federal law. The practice of the Department of Justice has, however, been not to enforce or prosecute federal prohibitions for commerce or consumption that is permitted by state-level legislation. This state of affairs caught the attention of the Canadian Securities Administrators, who have published guidance for companies with US-based cannabis activities, and of the Toronto Stock Exchange (TSX), which undertook a listing review of cannabis companies with US operations and maintains that its issuers are not permitted to participate in marijuana-related activities in the US. The Canadian Stock Exchange, in contrast to the TSX, has taken a more permissive approach, requiring only fulsome disclosure of these activities. The capital markets have thus far been receptive to US companies and companies with US assets, and it will be interesting to follow any changes to these diverging approaches to the listing requirements.
iii Strategic private investment in public entity or financing and acquisition transactions

Strategic private investment in public entity (PIPE) transactions have become increasingly common in Canada, especially among cannabis and junior mining issuers. A strategic PIPE transaction has features commonly associated with both corporate financings and takeovers, sometimes being referred to as a financing and acquisition (F&A) transaction.

In an F&A transaction, a publicly traded issuer will raise money by issuing equity or equity-linked securities, usually at the market price or at a premium, to an investor who may also receive warrants entitling the holder to acquire additional securities, giving the investor a path to control the issuer. Some examples of recent transactions include:

a CITIC Africa’s C$725 million investment to acquire a 19.9 per cent interest in Ivanhoe Mines, together with ancillary governance rights;

b Rhône Capital’s US$500 million investment to acquire a 21.8 per cent interest in Hudson’s Bay Company, together with ancillary governance rights;

c Constellation Brands’ C$5.1 billion investment to acquire an additional interest of approximately 30 per cent in Canopy Growth, together with ancillary governance rights and share purchase warrants entitling Constellation to acquire (upon payment of an additional C$4.5 billion) further shares that would result in aggregate holdings of approximately 55 per cent; and

d Altria Group’s C$2.4 billion investment to acquire a 45 per cent interest in Cronos Group, together with ancillary governance rights and warrants entitling Altria to acquire (upon payment of an additional C$1.4 billion) additional shares that would result in aggregate holdings of approximately 55 per cent.

From the issuer’s perspective, an F&A transaction offers equity financing at an attractive price (since public offerings and private placements are typically completed at a discount to the market price), often accompanied by an ancillary commercial relationship that may be perceived by market participants as a form of commercial sponsorship by the investor. The F&A transaction may be an especially attractive form of financing for a capital-intensive business that is not earnings positive or is operating in a challenging capital markets environment, or both. In addition, provided that the securities issuance is completed as a private placement, the F&A transaction does not require a prospectus or other offering document.

From the investor’s perspective, an F&A transaction offers an opportunity to acquire a substantial, non-controlling equity foothold in a company, usually accompanied by board nomination rights, shareholder approval rights, anti-dilution and preemptive rights and an option to acquire a controlling interest. Unlike an acquisition of securities effected under the private agreement exemption from the takeover bid requirement, there is no statutory limit on the premium payable in a private placement by an issuer. The F&A transaction can be structured using common shares, preferred shares or convertible debentures. Convertible debentures or preferred shares may be especially attractive for an investor that is evaluating an early stage issuer or an issuer that is experiencing financial difficulty, where there can be a real benefit to being higher up in the issuer’s capital structure before becoming an equity holder. An F&A transaction permits an investor to monitor (and often influence) its substantial investment before determining whether to acquire control (and consolidate the investee company) by exercising its path-to-control warrants.

As a type of PIPE, an F&A transaction is subject to securities laws and stock exchange requirements. The issuance of securities will be completed under an exemption from the
prospectus requirement, usually in reliance upon the accredited investor exemption. An accredited investor includes an institutional investor having net assets of at least C$5 million. Securities acquired under the accredited investor exemption will generally be subject to statutory resale restrictions for four months following the closing of the private placement, except where the investor is a control person, in which case additional restrictions will apply. If the investor acquires 10 per cent or more of the issuer’s voting shares, it will become an insider subject to insider reporting obligations. In addition, if the investor acquires 10 per cent or more of the voting or equity securities of any class (or convertible securities entitling the investor to be issued 10 per cent or more of such class), the investor must promptly issue a press release and, within two business days, file an early warning report (similar to a Rule 13D filing) with the Canadian securities regulators. Any issuance of equity securities by a listed issuer (or securities exercisable, convertible or exchangeable for equity securities) will usually require stock exchange approval. In the case of securities listed on the TSX or TSX Venture Exchange, the stock exchange will usually require disinterested shareholder approval if the securities being issued would result in a new 20 per cent shareholder or dilute the company’s existing shareholders by 25 per cent or more. In addition, depending on the strategic investor’s pro forma ownership in the issuer, the F&A transaction may trigger approval requirements or pre-merger notifications under the Competition Act (Canada) and, if the investor is a non-Canadian, under the Investment Canada Act.

F&A transactions are completed pursuant to a negotiated form of subscription agreement, which, in addition to the customary provisions found in share purchase agreements for private placements, will include some or all of the following provisions that are more typically reserved for M&A transactions: a non-solicit with a fiduciary out; deal protections, such as the payment of a termination fee and a right-to-match, in favour of the investor; and a standstill provision, restricting the investor’s ability to acquire securities of the investee company, or to propose a merger, prior to closing.

These provisions are customary because, in an F&A transaction, the investor is acquiring a meaningful equity position in the investee company that, even if not accompanied by path-to-control warrants, puts the investor in a good position to launch a takeover bid or merger proposal. Moreover, prior to signing the subscription agreement, the investor will have had an opportunity to complete a due diligence investigation and may have gained access to material information that has not been publicly disseminated. If the investor elects to commence a takeover bid or make a merger proposal, depending upon the investor’s ownership interest, the takeover bid could be subject to insider bid rules, and any merger could be subject to minority approval and formal valuation requirements under Multilateral Instrument 61-101: Protection of Minority Security Holders in Special Transactions.

The scope of ancillary contractual rights that accompany the investment in an F&A transaction is subject to negotiation in the context of the parties’ relative bargaining power and prevailing market conditions. Often, these rights are set forth in an investor rights agreement, which may contain some or all of the following provisions:

a. Board nomination rights allowing the investor to enjoy the right to nominate an agreed number of persons for election as directors. The actual number of nomination rights will usually be a function of the investor’s percentage ownership. The agreement will usually place restrictions on the company’s ability to change the size of its board, and may prescribe how the chair will be selected.

b. Top-up rights allowing the investor to subscribe for additional shares, at an agreed price or formula price, to maintain its percentage shareholding following the issuance
of dilutive securities, including shares issued as acquisition currency or pursuant to employee compensation plans. Top-up rights can, however, create complexity for compliance with stock exchange anti-dilution policies, and can inadvertently be an unnecessary administrative burden for the investee company.

c Preemptive rights allowing the investor to have conventional preemptive rights to participate rateably in any public offering or private placement.

d Shareholder approval rights allowing the investor to have the benefit of restrictive covenants, which will require the investee company to obtain the investor’s prior approval before, inter alia, amending its articles, entering into an agreed list of material transactions and declaring an extraordinary dividend. Notably, the investor is not subject to any common law fiduciary obligation to the investee in exercising shareholder approval rights. The scope of these shareholder approval rights may be taken into account by a stock exchange or a regulator in assessing whether they confer de facto control on the investor.

e The investee company may want to ensure that it has an opportunity to use the proceeds obtained from the F&A transaction to pursue its business plan before the investor is able to acquire control of the company or take it private. As such, the investor rights agreement may limit the strategic investor’s ability to acquire additional securities or propose a going-private transaction with a standstill provision that applies for a period following closing, or for as long as the investor holds an agreed minimum percentage of shares, except with the prior approval of the investee company’s board.

f The investee company may seek to align the strategic investor with the company for some minimum period following closing to prevent the investor from flipping its investment to a competitor of the company, or divesting all or part of its interest in a manner that places undue negative pressure on the market price of the company’s shares. These resale restrictions may contain springing provisions, entitling the investor to tender its shares to a third-party takeover bid.

g Conventional piggy-back rights or demand registration rights, or both.

h Path-to-control warrants allowing the strategic investor to acquire, on exercise, a sufficient number of additional securities to give the investor a controlling interest in the company. These warrants are usually priced at a further premium, above the premium paid by the investor for its front-end investment in the common shares, and may be subject to specified vesting limitations and other conditions.

The path-to-control control aspect of this type of transaction might seem curious to persons familiar with the Revlon doctrine, which is a shareholder primacy model of jurisprudence espoused by Delaware courts and followed in many other jurisdictions. Under the Revlon doctrine, in the context of a transaction involving a potential change of control, directors’ fiduciary duties are automatically transformed from focusing on the long-term interests of the corporation to maximising shareholder value in the near term. More specifically, the role of the board, when faced with the possibility of a change of control, changes from ‘defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company’.  

12 Revlon, at 182.
However, a number of Canadian courts have declined to follow *Revlon* in the context of change of control transactions, with one even going so far as to declare that ‘*Revlon* is not the law in Ontario’. In *BCE Inc v. 1976 Debentureholders*, the Supreme Court of Canada had an opportunity to weigh in on the topic in the context of a proposed C$52 billion leveraged buyout. In *BCE*, the Supreme Court’s main focus was to consider whether the company’s debenture holders were being oppressed in a proposed plan of arrangement that had been approved by an overwhelming majority of common shareholders. While the Court did not expressly reject *Revlon*, it reiterated a finding in its earlier decision in *Peoples* that, under Canadian corporate law, the fiduciary duty of directors is always owed to the corporation and not to any particular stakeholder or group of stakeholders. As such, under Canadian law, an informed board that is free of conflicts of interest has wider latitude to exercise its business judgment, even in the context of a prospective change of control, than may be the case in jurisdictions that follow the *Revlon* doctrine. In Canada, not every potential, or even prospective, change of control requires a board of directors to auction the company.

### IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

During the past two years, the review thresholds under the Investment Canada Act’s net benefit regime have increased significantly. Two of the three thresholds that will apply to most direct acquisitions of control of a Canadian business by non-state-owned enterprise investors from World Trade Organization (WTO) Member States have increased significantly: the private sector trade agreement investors threshold increased to C$1.568 billion (2019) in enterprise value of the target, and the threshold for investors from other WTO Member States increased to C$1.045 billion (2019) in enterprise value of the target. These increased thresholds have contributed to a decrease in the number of transactions subject to a net benefit review (falling from 22 in the 2016–2017 fiscal year to nine in the 2017–2018 fiscal year). While these increased thresholds represent a shift in the government’s emphasis away from net benefit reviews (focused on economic benefits to Canada), national security is increasingly in the spotlight. The national security review regime applies to any investment that involves a non-Canadian, regardless of size and whether control was acquired. Certain industries are likely to attract greater scrutiny, such as tech, critical infrastructure and defence. The government’s Guidelines on the National Security Review of Investments set out a non-exhaustive list of activities that may relate to national security. Although these guidelines provide some insight as to when a national security review may occur, there are notable gaps, and foreign investors often receive limited transparency during the national security review process. If the government believes that a transaction may be injurious to national security, the transaction can be blocked, subjected to conditions, or if already implemented, subject

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16 The threshold for direct acquisitions of Canadian businesses by state-owned investors from WTO Member States is C$416 million (for 2019) in gross book value assets.

17 The threshold for the direct acquisition of control of a Canadian business that carries on a cultural business by a non-state-owned enterprise investor from a WTO country remains the same: C$5 million in asset value of the target.

to remedies that can include divestiture. Since 2012, four transactions have been blocked, and various others have been subjected to conditions or were abandoned. The majority of the national security reviews that have been ordered were in respect of investors from China (10 orders) and Russia (two orders). In this geopolitical climate, national security considerations will be crucial for investors and targets in deal planning and risk allocation in 2019.

V COMPETITION LAW

Certain types of transactions that exceed prescribed thresholds require pre-merger notification under Canada’s Competition Act. Such transactions cannot be completed until notice has been given to the Canadian Competition Bureau and the statutory waiting period has expired or, alternatively, has been terminated early or waived by the Bureau. Generally, pre-notification of such transactions is required if both:

a the parties to the transaction (together with their affiliates) have combined aggregate assets in Canada, or combined gross revenues from sales in, from and into Canada, exceeding C$400 million; and

b the aggregate assets in Canada of the target (or of the assets in Canada that are the subject of the transaction), or the annual gross revenues from sales in or from Canada generated by those assets, exceeds C$96 million (2019; this threshold is adjusted annually).

Equity investments are also notifiable if the financial thresholds are met and the applicable equity thresholds are exceeded (more than 20 per cent in the public company context, more than 35 per cent in the private or non-corporate entity context or an acquisition of more than 50 per cent of a public company voting shares or private entity equity if a minority interest is already owned by purchaser).

It is important to note that the Competition Commissioner can review and challenge all mergers, whether they are notifiable or not, within one year of closing. Recent developments may increase the number of transactions that are subject to review. From a legislative perspective, recently expanded affiliation rules subject previously non-notifiable transactions to mandatory notification by extending the same control and affiliation principles to all entities, including corporations, partnerships, sole proprietorships, trusts or other unincorporated organisations, which in turn expands the net of relevant entities for the size of parties calculation. From an enforcement perspective, the Bureau has announced an increasing focus on non-notifiable transactions via an expanded intelligence-gathering mandate for the Merger Intelligence and Notification Unit. Furthermore, as part of the Bureau’s overall enforcement prioritisation of the digital economy, the Commissioner recently stated that the Bureau is going to be more vigilant about monitoring the acquisition of small firms by big tech. All of this serves to reinforce the importance of conducting substantive competition analysis of transactions of any size that may give rise to competition issues in Canada.

19 Aggregated statistics regarding the national security review process were first published in 2012.

20 Since the implementation of a formal national security review process in 2009, 15 national security review orders were issued between 2012 and 2018. In all 15 cases, the transaction was blocked, abandoned or subjected to conditions.
VI OUTLOOK

Buoyed by the general health of the economy, continued fundraising and existing dry powder in the private equity market, and cannabis companies seeking to execute growth strategies by entering into new markets and product lines through strategic M&A, 2019 promises to be a strong year for M&A activity in Canada, with a high likelihood of significant and innovative transactions emerging.
Chapter 10

CAYMAN ISLANDS

Suzanne Correy and Daniel Lee

I OVERVIEW OF M&A ACTIVITY

The Cayman Islands is recognised as one of the world’s leading global financial services centres. M&A activity is therefore largely driven by global rather than regional or national trends. The aggregate value of global M&A increased in 2018, reaching the highest level since 2015. The Bureau van Dijk M&A Review Global, Full Year 2018 Report (2018 Bureau van Dijk M&A Review Global Report) records deals worth US$5.3 trillion announced during the course of 2018.² Cayman Islands M&A-related activity also increased by value. According to the 2018 Bureau van Dijk M&A Review Global Report, announced M&A deals in the Cayman Islands in 2018 had an aggregate value of US$89.7 billion, some way from the high of US$143 billion in 2016, but ahead of the US$84.5 billion announced in 2017.

The three main types of entity used in the Cayman Islands are the exempted company, the exempted limited partnership and the limited liability company (LLC). During 2018, formation activity increased significantly: 13,893 exempted companies (2017: 11,138), 4,917 exempted limited partnerships (2017: 3,774) and 928 LLCs (2017: 711) were incorporated or registered in the Cayman Islands, with 90,268 exempted companies (2017: 83,675), 26,011 exempted limited partnerships (2017: 22,346) and 1,710 LLCs (2017: 889) being active as at 31 December 2018.³

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The key sources of regulation of M&A in the Cayman Islands are the Companies Law (2018 Revision) (Companies Law) and common law.

The Companies Law includes provisions permitting mergers and consolidations between one or more companies, provided that at least one constituent company is incorporated under the Companies Law. The Limited Liability Companies Law (LLC Law), discussed further below, also provides for a similar framework for Cayman Islands LLCs.

Mergers, amalgamations and reconstructions by way of a scheme of arrangement approved by the requisite majorities of shareholders and creditors, and by an order of the Cayman Islands court under Section 86 or 87 of the Companies Law, are still available for complex mergers (and are mirrored in the LLC Law). The Companies Law provides a limited minority squeeze-out procedure (which, again, is mirrored in the LLC Law).

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1 Suzanne Correy and Daniel Lee are partners at the Maples Group.
3 Cayman Islands Registrar of Companies and Registrar of Exempted Limited Partnerships annual statistics.
The Cayman Islands does not have a prescriptive set of legal principles specifically relevant to going private and other acquisition transactions (unlike other jurisdictions such as, for example, Delaware). Instead, broad common law and fiduciary principles will apply.

While there are no specific statutes or government regulations concerning the conduct of M&A transactions, where a target company’s securities are listed on the Cayman Islands Stock Exchange (CSX), the CSX Code on Takeovers and Mergers and Rules Governing Substantial Acquisitions of Shares (which exists principally to ensure fair and equal treatment of all shareholders) may apply.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Economic substance requirements

The Cayman Islands has recently introduced the International Tax Co-operation (Economic Substance) Law, 2018 (Economic Substance Law) and related regulations and guidance notes. The Economic Substance Law is responsive to the global Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting standards regarding geographically mobile activities.

The Economic Substance Law introduces certain reporting and economic substance requirements for relevant entities conducting relevant activities. Such entities will be required to report certain information on their relevant activities on an annual basis to the Cayman Islands Tax Information Authority, the first such annual report being due no later than 12 months after the last day of the relevant entity’s financial year commencing on or after 1 January 2019.

Relevant entities that do not conduct a relevant activity will have to make a simple notification to confirm whether or not they conduct a relevant activity (this straightforward notification is expected to be made online, via a dedicated portal, the first notification being made around September 2020).

For a relevant entity formed on or after 1 January 2019 that will conduct a relevant activity, the economic substance requirements will apply from the date that the relevant entity commences the relevant activity. For relevant entities conducting relevant activities that were in existence before 1 January 2019, the economic substance requirements will apply from 1 July 2019.

A relevant entity is an entity that is not an investment fund, an entity that is a domestic company and an entity that is tax-resident outside of the Cayman Islands.

The terms investment fund and domestic company are defined in the Schedule to the Economic Substance Law, and guidance notes provide some practical guidance as to the meaning of tax resident.

Entities without separate legal personality (such as certain forms of partnership or trust) are not within the classification of a relevant entity.

The Economic Substance Law applies economic substance requirements to the following categories of geographically mobile relevant activities previously identified by the OECD (and adopted by the European Union):

a banking;

b insurance;

c shipping;

d fund management;
Where a relevant entity conducts a relevant activity, the economic substance test will apply. Where a relevant entity conducts more than one relevant activity, the economic substance test will need to be satisfied in respect of each relevant activity conducted.

ii Merger regime and dissenting rights

The statutory merger regime contained in Part XVI of the Companies Law remains a popular tool for facilitating mergers involving Cayman Islands companies. Under this regime, two or more companies may merge, with their property and liabilities vesting in one of them as the surviving company.

Similar to other jurisdictions with equivalent regimes, the Companies Law provides for a right of dissenting shareholders to object to a merger and be paid a payment of the fair value of their shares upon their dissenting to the merger if they follow a statutory procedure. If the dissenting shareholders and the relevant company are unable to agree in accordance with the statutory procedure, the Grand Court of the Cayman Islands is required to determine the fair value of the shares, and a fair rate of interest, if any, to be paid by the company upon the amount determined to be the fair value.

These rights of a dissenting shareholder are not available in certain circumstances, such as:

a to dissenters holding shares of any class in respect of which an open market exists on a recognised stock exchange or recognised inter-dealer quotation system at the relevant date; and

b where the consideration for such shares to be contributed are shares of the surviving or consolidated company (or depositary receipts in respect thereof), are shares of any other company (or depositary receipts in respect thereof) that is listed on a national securities exchange or designated as a national market system security on a recognised inter-dealer quotation system, or are held of record by more than 2,000 holders.

Although the period between 2015 and 2017 saw a significant increase in the volume of dissent actions in the Cayman Islands, with 16 separate petitions having been filed between the beginning of 2016 and the beginning of 2018, recently the number of such filings has reduced. The increase in actions appeared to be driven, at least in part, by arbitrage investors, purchasing positions in companies particularly with a view to exercising dissent rights. Such actions now appear less common, however, in light of recent rulings both in the Cayman Islands (including those described below) and elsewhere (particularly in Delaware). It remains to be seen whether this level of dissenter activity leads to a re-emergence of schemes of arrangement, being the way in which most takeovers and take-privates were structured in the Cayman Islands prior to the introduction of the merger regime. Although schemes of arrangement involve court supervision, higher requisite majorities and generally higher deal costs, they do not involve dissenter rights or any other cash out or fair value option.

In 2019, the Grand Court ruled on only the third merger fair value appraisal that has gone to trial in the Cayman Islands. The decision in Re Qunar Cayman Islands Limited
advances the case law on the Cayman Islands merger regime following the 2017 decision in *Re Shanda Games Limited* and the 2015 decision in *Re Integra Group*.4 These decisions of the Court set out important guidance as to how, if a shareholder has dissented to a statutory merger, the fair value of the dissenter’s shares will be determined. The following guidance can be taken from the Court’s decisions:

- **a** Fair value is the value to the shareholder of his or her proportionate share of the business as a going concern: it is a value that is just and equitable, and provides adequate compensation consistent with the requirements of justice and equity. Fair value does not include any premium for the forcible taking of shares. In determining fair value, neither the upside nor downside of the transaction being dissented from should be taken into account (e.g., any costs savings obtained by a company going private).

- **b** Assessing fair value is a fact-based exercise that requires an important element of judgment by the court.

- **c** If a company’s shares are listed on a major stock exchange, this does not mean that a valuation methodology based upon its publicly traded prices is necessarily the most reliable. Whether this valuation methodology is appropriate will depend on whether there is a well-informed and liquid market with a large, widely held free float (as there was in *Qunar*, but notably not in *Shanda* or *Integra*).

- **d** The date for determining fair value was the date on which the shareholders approved the transaction: this was the date on which the offer could be accepted. Importantly, the Court concluded that dissenting shareholders could not take advantage of the cost savings going forward as a result of the merger. The Court’s view was that dissenting shareholders should not benefit from any enhancement in the value of their shareholding attributable directly to the transaction from which they have dissented.

Interestingly, in reaching its decisions in *Integra* and *Shanda*, the Court took into account guidance concerning similar statutory merger processes that exist in the state of Delaware and in Canada. In view of the litigious nature of United States M&A, there is a significant volume of case law on this topic in Delaware. We believe this may be the first time the Grand Court has specifically considered Delaware precedent. Both *Integra* and *Shanda* had followed Delaware and Canadian authority on this point, holding that in a fair value appraisal the dissenters’ shares were to be valued as a proportion of the value of the whole company, not as a block of shares offered for sale, such that there was no applicable ‘minority discount’.

The decision in *Shanda* was the subject of an appeal. Although the Court of Appeal affirmed most of the conclusions below, significantly it reversed the Grand Court’s position on minority discount. The Court of Appeal took a different view, and followed what it considered to be the public policy reflected in English case law, to the effect that ‘it was not unfair to offer a minority shareholder the value of what he possesses, i.e., a minority shareholding. The element of control is not one which ought to have been taken into account as an additional item of value in the offer of these shares’. The Court of Appeal held that Section 238 of the Companies Law requires fair value to be attributed to what the dissenters actually possess: if it is a minority shareholding, it is to be valued as such, and if the shares are subject to particular rights or liabilities or restrictions, the shares are to be valued as subject to those rights or liabilities. This question of minority discount is the subject of a further appeal to the Privy Council. Interestingly, in *Qunar*, the Court, while following the approach

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4 Maples and Calder acted for the successful dissenting shareholders in both *Shanda* and *Integra*.
of the Court of Appeal in Shanda, considered that the applicable majority discount was nil, given Qunar’s securities were highly liquid, and there was no risk on minority disadvantage regarding management control or payment of dividends.

As a separate point, a series of decisions culminating in a Court of Appeal ruling in Qunar affirmed that the Court has jurisdiction to make an interim payment order after a dissent petition is filed but before the trial, meaning that a dissenting shareholder may be entitled to receive an interim payment effectively at the outset of the proceedings. In many cases this has equalled the merger consideration, on the basis that the company has admitted that this reflects fair value (albeit this does not necessarily follow). However, the question of what the Court should and should not take into account when being asked to exercise this discretion has not been fully tested, and remains the subject of debate.

In a separate decision in Re Qunar, reversing earlier Grand Court decisions, the Court of Appeal affirmed the availability of documentary discovery from dissenters, both as to their own valuation analysis and as to their trading history in the company’s shares.

### iii LLCs

In June 2016, the LLC Law came into force creating a new Cayman Islands vehicle: the LLC. This vehicle takes its inspiration, in part, from the Delaware LLC. Its flexible nature means that it is well-suited to a broad range of general corporate and commercial applications. The introduction of the LLC has further strengthened the Cayman Islands’ position as the domicile of choice for offshore investment funds and corporate structuring vehicles.

An LLC is essentially a hybrid vehicle, combining certain characteristics of a Cayman Islands exempted company with those of a Cayman Islands exempted limited partnership. In developing the vehicle, certain Delaware concepts were taken into consideration and adapted, where appropriate, to mesh with Cayman Islands law and concepts. An LLC is a body corporate with separate legal personality, like a Cayman Islands exempted company, but without the constraint of having share capital.

Equivalent to the Delaware statute, the LLC Law provides a set of default rules as to how an LLC operates. However, the members of an LLC are free to legislate their own arrangements in the vehicle’s LLC agreement (the constitutional document of the LLC), which is not publicly filed.

Generally, the liability of a member of an LLC is limited to the amount a member has contractually agreed to contribute to the LLC. There is a limited statutory clawback, which applies only if a member receives a distribution when the LLC is insolvent and the member has actual knowledge of the insolvency at the time the distribution is made.

There is great flexibility in how LLCs are managed. They may be governed by the members themselves or appointed managers who need not be members (such as a board of managers). Unless otherwise expressly specified in an LLC agreement, the default duty of care in managing an LLC is to act in good faith. This duty may be expanded or restricted, but not eliminated, by the express provisions of the LLC agreement. In an M&A context, we consider this feature may be of particular interest for management buyout investors who may wish to have the right to appoint a representative as a director or manager of that vehicle. In a traditional exempted company, any investor representative (in a company context, as a director) has a duty to act at all times in the best interests of the company when participating in company decisions: the representative cannot solely consider the interests of the investor.
that has appointed him or her (to do so would expose him or her to potential personal liability). Contrast this with an LLC, where the members have the freedom to contractually agree in the LLC agreement the duty of care that the managers of the LLC owe.

Although dependent on the required structuring for particular deals, the vehicle is commonly used in a broad range of corporate and commercial applications, including acquisition and joint venture structures, acting as corporate blockers and holding vehicles, as preference share issuing vehicles (in a venture capital financing arrangements), employee incentive vehicles and in structured finance transactions.

iv Global transparency

Already recognised by the OECD, the International Monetary Fund (IMF) and other international bodies for its transparency and standards being consistent with those of other major developed countries, the Cayman Islands is acknowledged as a first-class jurisdiction for conducting international business. The government has also now implemented or confirmed a number of further transparency steps it is willing to take, including:

a the introduction in July 2017 of a beneficial ownership register regime, discussed further below;

b a willingness to commence discussions with those jurisdictions that are participating in the G5 initiative (for the exchange of beneficial ownership information with law enforcement agencies) on entering into bilateral agreements with the Cayman Islands, similar to the beneficial ownership regime now in place with the United Kingdom;

c the repeal of the Confidential Relationships (Preservation) Law and its replacement by the Confidential Information Disclosure Law, which offers more understanding of and definition with regard to the mechanisms in place for sharing confidential information with the appropriate authorities;

d acknowledging privacy as a basic human right, and introducing new data protection legislation (currently expected to come into force at the end of September 2019);

e abolishing bearer shares (completed in May 2016); and

f implementation in the Cayman Islands of the model legislation published pursuant to the OECD’s Base Erosion and Profit Shifting Action 13 Report (Transfer Pricing Documentation and Country-by-Country Reporting), and as discussed above, the introduction of the Economic Substance Law.

These measures demonstrate the Cayman Islands’ continued efforts to comply with and promote transparency through close collaboration and compliance with the relevant global regulatory bodies, tax authorities and law enforcement agencies in line with international standards, while simultaneously respecting the legitimate right to privacy of law-abiding clients.

The Cayman Islands has agreements to share tax information with authorities in more than 90 other countries, including the United States under the Foreign Account Tax Compliance Act, and is in the early adopter group for the Common Reporting Standard, the OECD’s global tax information exchange standard.

In July 2017, the Cayman Islands introduced a new beneficial ownership register regime (BOR Regime). Exemptions mean that certain Cayman Islands companies and LLCs are not in scope of the regime. If a company or LLC is in scope, it must take reasonable steps
to identify its beneficial owners and certain intermediate holding companies, and to maintain a beneficial ownership register at its registered office in the Cayman Islands with a licensed and regulated corporate service provider.

This register must generally record details of the individuals who ultimately own or control more than 25 per cent of the equity interests, voting rights or rights to appoint or remove a majority of the company directors, or LLC managers, together with details of certain intermediate holding companies through which such interests are held.

Corporate service providers must facilitate access to information extracted from the register through a centralised IT platform operated by a competent authority designated by the government. The information will not be held on a central register by either the government or the competent authority; nor will it be publicly accessible or searchable. Only Cayman Islands and UK authorities will have rights to request information, and then only as individual (and not automatic) requests. The information on the beneficial ownership register can already be requested by UK authorities under existing information exchange gateways, so in essence the new regime merely seeks to streamline the process to provide for quicker and more discrete search accessibility.

Legislation introduced at the end of 2017 now requires that Cayman Islands companies and LLCs that are exempt from the BOR Regime make a filing to that effect with their corporate services provider in the Cayman Islands.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

The vast majority of M&A activity involving Cayman Islands entities concerns foreign businesses and investors as a result of the offshore nature of the jurisdiction. These businesses and investors are based in a broad range of international jurisdictions.

A large number of M&A deals are still originating from the United States, while European deals continue to feature and Asian-related transactions continue to grow.

As at the end of 2016, according to statistics published by the United States Securities Exchange Commissions, there were 700 foreign companies (i.e., non-United States issuers) listed on the New York Stock Exchange and NASDAQ, of which 103 were Cayman Islands issuers, far ahead of any other traditional offshore jurisdiction. Only Canada had more companies traded on the main US public markets than the Cayman Islands.

The Asian growth can be evidenced by the popularity of the Cayman Islands exempted company as a listing vehicle in Asia: as at the end of 2018, 956 of the 1,926 companies listed on the Main Board of the Hong Kong Stock Exchange were Cayman Islands exempted companies.

The Cayman Islands continues to be an attractive jurisdiction for the structuring of offshore transactions for a number of reasons, including:

a the speed with which vehicles can be established (usually within one business day), and without the need for any prior governmental approvals;

b the laws of the Cayman Islands are substantially based upon English common law and a number of key English statutes. This gives Cayman Islands law and the legal system a common origin with those of many of the jurisdictions of its users, including the United States;

5 HKEx Fact Book 2018.
the Cayman Islands has a modern and flexible statutory regime for companies, limited partnerships and LLCs;

as described further below, the Cayman Islands has no direct taxes of any kind;

the lack of exchange control restrictions or regulations; and

there is no requirement that a Cayman Islands entity should have any local directors or officers. Nor is there any requirement for local service providers (except that for funds regulated under the Mutual Funds Law, where there is a requirement for their audited accounts to be signed off by a local firm of auditors). The appointment of local service providers, however, may assist entities with obligations under the Economic Substance Law to discharge those obligations.

As discussed above, the Cayman Islands is recognised by the OECD, the IMF and other international bodies for its transparency and standards consistent with those of other major developed countries.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The merger regime of Part XVI of the Companies Law continues to be a popular tool for facilitating mergers involving Cayman Islands companies, and we continue to see listed companies being the subject of take-private transactions led by private equity and management in addition to traditional strategic corporate acquisitions. The merger regime has also proven to be a popular mechanism for business combinations for special purchase acquisition vehicles.

Deals of note announced or closed during 2018 that involved Cayman Islands vehicles included:

a the US$6.7 billion acquisition of majority ownership of insurance claims and technology services firm Sedgwick by funds managed by The Carlyle Group Global;

b the US$2.7 billion acquisition of NASDAQ-listed Ocean Rig UDW Inc, an international contractor of offshore deepwater drilling services, by Transocean Ltd;

c the US$860 million acquisition of an oil and gas platform from Pampa Energía SA and Pluspetrol Resources Corporation by Vista Oil & Gas, SAB de CV;

d the acquisition of SI Group, a leading global developer and manufacturer of performance additives and intermediates, by SK Capital Partners, a private investment firm focused on the specialty materials, chemicals and pharmaceuticals sectors; and

e the US$232.5 million tender offer to Paragon Offshore Limited by international drilling contractor, Borr Drilling Limited.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

As a leading jurisdiction for the establishment of private equity funds, it is perhaps unsurprising that a significant number of Cayman Islands M&A deals are also financed by private equity. Traditional sources also continue to be a key provider of finance for M&A involving Cayman Island entities, including in respect of a number of the deals listed above.
VII  EMPLOYMENT LAW

A range of legislation and licensing requirements apply to companies seeking to carry on local business in the Cayman Islands and employ local personnel. In view of the nature of offshore business, the vast majority of Cayman entities do not have employees in the Cayman Islands, and these requirements are therefore often not relevant to Cayman Islands M&A deals.

Employment standards in the Cayman Islands are currently governed by the Labour Law (2011 Revision) (Labour Law), the Health Insurance Law (2018 Revision) and ancillary regulations (Health Law), the National Pensions Law (2012 Revision) (Pensions Law), and the Workmen’s Compensation Law (1996 Revision) and ancillary regulations. These laws establish minimum employment standards, but do not preclude an employer from setting conditions that are above the minimum.

The Labour Law includes provisions dealing with probation periods, employment termination, public holiday pay, sick leave, compassionate leave, maternity leave, severance pay and unfair dismissal.

The Health Law requires that health insurance cover is provided to employees, and to their uninsured spouses and children. The Pensions Law requires an employer to provide a pension plan or to make a contribution to a pension plan through an approved pension provider for every employee who is between 18 and 60 years old (an employer is not required to provide a pension plan for non-Caymanian employees who have been working for a period of nine months or less).

VIII  TAX LAW

i  Cayman Islands taxation

The Cayman Islands has no direct taxes of any kind: no income, corporation, capital gains or withholding taxes, or death duties. Under the terms of the relevant legislation, it is possible for all types of Cayman vehicle – companies, unit trusts, limited partnerships and LLCs – to register with and apply to the government for a written undertaking that they will not be subject to various descriptions of direct taxation, for a minimum period, which in the case of a company is usually 20 years, and in the case of a unit trust, limited partnership and an LLC, 50 years.

Stamp duty may be payable in connection with the documentation executed in or thereafter brought within the jurisdiction of the Cayman Islands (perhaps for the purposes of enforcement). In most cases, this duty is of a relatively de minimis fixed amount except in limited circumstances, such as when security is being granted over property in the Cayman Islands.

ii  Automatic exchange of information legislation

The Cayman Islands has signed an inter-governmental agreement to improve international tax compliance and the exchange of information with the United States (US IGA). The Cayman Islands has also signed, with more than 90 other countries, a multilateral competent authority agreement to implement the OECD Standard for Automatic Exchange of Financial Account Information – Common Reporting Standard (CRS).
Cayman Islands regulations have been issued to give effect to the US IGA and CRS. Cayman Islands financial institutions are required to comply with the registration, due diligence and reporting requirements of these regulations, except to the extent that they are able to rely on certain limited exemptions.

IX  COMPETITION LAW

There is no specific anticompetition legislation that is relevant to Cayman Islands M&A. Given the offshore nature of Cayman Islands M&A, competition law issues are usually a question of the relevant onshore jurisdictions where the underlying businesses that are the subject of the M&A are based.

X  OUTLOOK

In a recent Deloitte survey, 6 76 per cent of corporate executives and 87 per cent of private equity investors – a significant source of deals for the Cayman Islands – expected the number of deals to increase in 2019. Based on the year to date, 2019 is shaping up to be another strong year for Cayman Islands M&A.

The existing legal framework of the Cayman Islands, together with the continued focus on being at the forefront of global compliance developments and the ability to deliver new legal initiatives (such as the new Cayman Islands LLC), will continue to ensure that the Cayman Islands remains the offshore jurisdiction of choice for global M&A transactions in future years.

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Chapter 11

CHINA

Wei (David) Chen and Kai Xue

I OVERVIEW OF M&A ACTIVITY

The trade war between China and the US has flared even more dramatically compared to last year’s events. From US$34 billion in tariffs and retaliatory tariffs in July 2018, it is expected to envelop all merchandise trade between China and the US by the end of 2019. As a response to the intensifying war, China is continuing to open up foreign investment. A new Foreign Investment Law (FIL) goes into effect on 1 January 2020, building on top of similar liberalisation moves in 2017 and 2018.

The effect on outbound investment to the US has not been noticeable so far in 2019 because there was already little deal activity by Chinese buyers of American target companies in 2018, leaving limited space for deal volume to dwindle any further. Overall Chinese outbound M&A across the world declined from US$122.5 billion in 2017 to US$94.1 billion in 2018. The slowdown in outbound M&A activity is even more apparent when compared to 2016, when deal volume reached the record-breaking level of US$210.4 billion.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

There is no unified M&A law governing all M&A activities. Rather, specific M&A activities are subject to different sets of laws and regulations depending on the type of buyer, the target and specific legal issues implicated in the deal. Foreign investment in certain industries requires approval from the competent regulatory body (e.g., investment in banking is overseen by the China Banking and Insurance Regulatory Commission).

i Inbound M&A

In the context of inbound M&A, the laws and regulations applicable to foreign investment in China will generally apply.

1 Wei (David) Chen is a managing partner and Kai Xue is a counsel at DeHeng Law Offices. The authors would like to thank DeHeng colleagues Tong Yongnan, Wang Yuwei, Hu Tie and Zhang Xu for their assistance in preparing this chapter and summer 2019 interns Weize Tong and Lui Ka Yee for their contributions.
Investment vehicles

China recognises a wide range of business vehicles. The three basic forms are the limited liability company, the company limited by shares and the partnership. A business establishment that is the result of foreign investment will generally be referred to as a foreign invested enterprise (FIE). The most common forms of FIEs are:

1. Joint ventures (JVs) between domestic and foreign partners, including equity JVs and cooperative JVs;
2. Wholly foreign-owned enterprises;
3. Foreign-invested holding companies;
4. Foreign-invested companies limited by shares (FICLS); and
5. Foreign-invested partnerships.

Joint ventures will be impacted when the FIL comes into effect on January 2020. The FIL replaces the existing joint venture law. After the end of a five-year grace period from January 2020, joint ventures must make amendments to their corporate structure in accordance with the Company Law. The eventual result will be consolidated corporate governance rules applicable to both FIEs and domestic companies.

Foreign investment regulation system

Under the foreign investment regulatory system, foreign investment in industries that are encouraged are grouped under an encouraged industries list (Encouraged Catalogue). While foreign investments in industries subject to restriction or that are prohibited are placed under a general nationwide negative list (Negative List) or a negative list (FTZ Negative List) for the free trade zones (FTZ). The Encouraged Catalogue contains an extensive list of industries that are sought after by policymakers. If a target sector industry is outside of the Negative List or FTZ Negative List (in the case of investment within an FTZ), then the investment does not require a case-by-case approval and can undergo recording through the record filing system.

Negative List

The Negative List is a mechanism that restricts or prohibits foreign investment into certain domestic industries. The latest Negative List (which entered into effect in July 2019) reduces the number of items listed from 48 to 40. For non-Negative List items, all market participants are legally entitled to invest in the respective sectors without bias, and foreign investors will only need to go through the record filing system, rather than the case-by-case approval needed under earlier versions of the foreign investment regulatory system.

Foreign investors are now allowed to hold controlling shares in domestic shipping agencies, urban infrastructure networks (e.g., gas, heat and water drainage systems) that cater to a population of 500,000 and above, and movie theatres and performance management agencies. Changes were also seen in the agricultural, mining and manufacturing industries. Foreign investors are no longer prohibited from investing in the development of wild animal and plant resources, the exploration and development of certain natural resources (tungsten, molybdenum, tin, antimony and fluorite), or the development of petroleum and natural gas (when the investment occurs in the form of an equity or cooperative joint venture).
Negative List for FTZs

For investments within FTZs, a separate negative list is implemented under the FTZ Negative List. Here, the Negative List concept is used with a more experimental purpose, as successful economic reforms are then subsequently extended nationwide.

In the latest revision of the FTZ Negative List (entering into effect in July 2019), the number of restricted or prohibited industries was reduced from 45 to 37 items. Compared to its 2018 predecessor, the 2019 FTZ Negative List completely removes restrictions on foreign investment in fishing aquatic products, the printing of publications, smelting and processing of radioactive minerals, and the production of nuclear fuel. Foreign investors may also now hold minority shares in cultural and artistic performance groups. While such investments are still prohibited within the nationwide Negative List, it is expected that a number of the 2019 FTZ Negative List exemptions listed above will be implemented broadly in future issues of the Negative List.

It must be noted that in some sectors (e.g., finance, where there is a substantial similarity between the Negative List and the FTZ Negative List in terms of restrictions such as shareholding limits), companies operating in the FTZs can still enjoy more flexibility in their day-to-day operations. For example, FTZs have simplified procedures for controlling foreign capital. Foreign-invested companies in FTZs enjoy expedited processing in opening a foreign currency account and receiving payment in a foreign currency.

As for the number of FTZs, this stands now at 12 locations. During the G20 Summit of 2019, China announced that six new FTZs would be established in the near future. Besides newly established FTZs, the Ministry of Commerce (MOFCOM) is also focusing on improving the quality of the existing FTZs, and it has indicated it will deepen liberalisation in existing FTZs through concentrating on promoting openness in the areas of finance, education, culture, medicine and general manufacturing.

Record filing system

In parallel with adoption of the Negative List, a uniform record filing administration system was implemented to replace case-by-case approval under MOFCOM for investments in industries not on the Negative List. In general, the establishment of and most changes to existing non-Negative List FIEs, including the transformation of non-FIEs into FIEs through an acquisition, strategic investment by foreign investors in listed companies, mergers and other methods, is under the purview of record filing. However, exceptions include transactions on the radar of antitrust or national security review. Also not eligible for record filing are affiliated acquisitions, namely the acquisition of domestic entities through overseas entities that are established or controlled by affiliates of the target.

A strategic investment in a listed company not on the Negative List by a foreign investor is eligible for record filing. This is worthy of note since investments of this type are still subject to a number of legal requirements; however, it is commonly understood that the requirements – including qualification, lock-up period and shareholding ratio of foreign investors – may have been lifted (see ‘Inbound M&A transactions involving A-shares listed companies’).

All record filings are required to be carried out via a uniform online platform, largely eliminating the uncertainty of different interpretations by local officials.

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2 Special Administrative Measures for Foreign Investment Access to Pilot Free Trade Zones.
China

Encouraged Catalogue

The Encouraged Catalogue sets out the range of encouraged industries for foreign investment. The latest Encouraged Catalogue (which entered into effect in July 2019) expands to include 415 items that are encouraged nationwide, and in the less-developed hinterlands of Central and Western China there are 693 encouraged items. Examples of encouraged industries are engineering consultancy, accounting, tax, cold chain logistics, artificial intelligence and carbon capture.

M&A regulations

Inbound M&A transactions by foreign investors are primarily governed by the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (M&A Regulations) developed by MOFCOM.

The M&A Regulations mainly concern:

a. the acquisition of equity interest in and assets from Chinese domestic enterprises;
b. the establishment of offshore vehicles for the purposes of listing Chinese assets through an offshore initial public offering;
c. the establishment of FIEs by offshore entities set up or controlled by Chinese domestic enterprises and Chinese residents; and
d. the swapping of shares between a foreign company or its shareholders and the shareholders of a Chinese domestic enterprise.

The M&A Regulations also provide detailed procedures and rules regarding the acquisition of domestic companies by foreign investors, including approval procedures, acquisition prices and terms of payment. However, they are not comprehensive and do not apply to the following inbound M&A transactions by a foreign investor:

a. acquisitions of the equity or subscription of a capital increase of an existing FIE (covered by regulations on equity changes of the investors of FIEs);4
b. mergers between or acquisitions of a domestic enterprise through an existing FIE (this is the ambit of regulations for mergers and divisions of FIEs and reinvestment by FIEs);5 and
c. acquisitions of a domestic limited liability company and the transforming of the same into an FICLS (governed by regulations on the establishment of an FICLS).6

3 As last amended on 22 June 2009.
4 Mainly, Certain Regulations on the Change of Investors' Equities in Foreign Investment Enterprises promulgated by the former Ministry of Foreign Trade and Economic Cooperation (predecessor of MOFCOM) and the State Administration for Industry and Commerce on 28 May 1997.
6 Mainly, Provisional Regulations on the Establishment of Foreign Invested Companies Limited by Shares as last amended on 28 October 2015.
If a foreign investor’s acquisition of a domestic enterprise has a bearing on national security, the acquisition may also be subject to a national security review by a ministry-level co-chaired committee, generally involving MOFCOM, the National Development and Reform Commission (NDRC) and, if necessary, other governmental regulators.

**Acquisition of state-owned assets or equity**

Inbound M&A transactions aimed at acquiring state-owned assets or equity are subject to a rather complex legal regime and strict supervision by the Chinese authorities, including the State-owned Assets Supervision and Administration Commission of the State Council (SASAC). In general, sales of state-owned assets or state-owned enterprises (SOEs) (with few exceptions) must be approved by SASAC (or its provincial and local counterparts) or by the relevant SOEs that are empowered with approval authority. Acquisitions of state-owned assets or SOEs are also subject to a mandatory appraisal conducted by a qualified appraiser and, as a general principle, the actual transfer price for the state-owned assets or equity shall not be less than 90 per cent of the value determined by the appraiser, except if a price lower than the 90 per cent threshold is approved by the competent authority.

**Inbound M&A transactions involving A-shares listed companies**

PRC domestic stock exchange-listed companies currently issue two classes of shares, namely:

- A-shares, which are yuan-denominated shares reserved for Chinese investors, qualified foreign institutional investors (QFIIs), yuan-qualified foreign institutional investors (YQFIIs) and qualified foreign strategic investors; and
- B-shares, which are yuan-denominated shares traded in foreign currency (in US dollars on the Shanghai Stock Exchange and in Hong Kong dollars on the Shenzhen Stock Exchange) and available for purchase by both Chinese and foreign investors.

To qualify as a foreign strategic investment in a domestic-listed company, a foreign investor needs to purchase at least 10 per cent of the A-shares of a listed company, by way either of a private placement or a share transfer, and generally be subject to a three-year tie-in period and other prescribed conditions.

In addition, to purchase through QFIIs or YQFIIs, or through qualification as a strategic investment, a foreign investor may acquire A-shares indirectly through an existing FIE that holds or is eligible to hold A-shares of a listed company.

**ii Outbound cross-border investments**

A new regulatory regime for outbound investments, the Administrative Measures for Outbound Investments by Enterprises (the Outbound Investment Circular), came into effect on 1 March 2018, specifying filing or approval requirements for outbound investments. The Outbound Investment Circular is a framework of filing and approval requirements on both direct and indirect outbound investments based on the sensitivity of an investment. The Outbound Investment Circular, issued by the NDRC, cements the build-up of regulatory policy changes since late 2016 when authorities adopted practices to curb outbound investment in sensitive sectors. It also builds on the Guidelines on Further Guiding and Regulating the Directions of Outbound Investments issued in August 2017 (the Outbound Investment Guidelines), which divided types of outbound investments into the categories of encouraged, restricted and prohibited.
The Outbound Investment Circular also has the important consequence of bringing under regulatory coverage the sponsorship of, or investment in, offshore investment funds with outbound investments by Chinese entities, including offshore entities controlled by Chinese companies or individuals. This puts indirect investments under the purview of outbound approval regulation by the NDRC. Previously, if funds were transferred offshore for an indirect investment, the transaction, although subject to domestic foreign exchange regulations, was outside the regulatory approval of the NDRC.

Under the previous regulatory framework, it was necessary to file a project information report for projects exceeding US$300 million before ‘carrying out any substantive work’. This ‘small pass’ requirement at the early stage of a project has been eliminated. Approval, filing or reporting requirements under the NDRC under the new framework are timed at completion (financial closing).

**NDRC**

The approvals and registrations for outbound investment must be obtained or conducted through the NDRC, MOFCOM and the State Administration of Foreign Exchange (SAFE). For SOEs, there are additional reporting obligations and a required approval from SASAC (not covered in detail here).

Approval of a project before financial closing by the national level NDRC is required for sensitive projects. However, for a non-sensitive project undertaken by a non-central state-owned enterprise worth over US$300 million, a filing with, rather than approval from, the national level NDRC is necessary. For non-sensitive projects under US$300 million, conducting a filing is necessary with the provincial level NDRC. For indirect, non-sensitive investments made through an offshore investment fund that exceeds US$300 million in value, a report to the NDRC must be submitted before the financial closing; for such projects below US$300 million, there is no reporting requirement. The applications for filing, approval and reporting are done through the NDRC’s online platform.

Sensitive projects are outbound investments to sensitive countries or in sensitive sectors. The 2018 Catalogue of Sensitive Industries for Overseas Investment defines sensitive sectors as industries listed as restricted under the Outbound Investment Guidelines (i.e., real estate, hotels, cinemas, entertainment, sports clubs) and news media, among others. Sensitive countries are those that do not have diplomatic relations with China, are at war, or are barred by international treaties agreements or treaties to which China is a party.

**MOFCOM**

Following the execution of the definitive transaction agreements, an ‘application form of outbound direct investment’ should be submitted online to MOFCOM. The application package includes the application form, transaction agreements, the business licence of the buyer, an export permit for products or technologies (if applicable) and a statement from officers of the companies warranting the veracity of the proposed outbound investment. MOFCOM approval is typically received within 10 to 15 business days of the date on which the application satisfies the filing requirements, and culminates in the issuance of an enterprise overseas investment certificate.

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7 Guatemala, Honduras, Nicaragua, Paraguay, Belize, Eswatini, and several Caribbean and Pacific Island countries.
SAFE
After obtaining an enterprise overseas investment certificate from MOFCOM, an application for foreign exchange registration on an outbound direct investment is made to a commercial bank under the supervision of SAFE, which will include the business licence of the buyer and the enterprise overseas investment certificate, with a statement of foreign exchange funding sources. Following submission, an overseas investment foreign exchange registration certificate will be issued to the buyer.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Greater global participation in the financial sector gains traction
In 2018, a number of laws and measures eased or committed in the future to easing restrictions on foreign investment in the financial sector. Major steps that have been taken or are planned include the following:

a the removal of restrictions regarding the business scope of jointly funded securities companies in 2018;

b the cap on foreign ownership in companies in the securities, funds, futures and life insurance sectors was increased to 51 per cent, and all limits on ownership by foreign investors are due to be removed in 2020 (an acceleration was announced in 2019, moving up the initial 2018 timetable); and

c the removal of restrictions on the business scope of foreign-invested insurance brokerage companies.

Global investment banks have seized the opportunity to raise their shareholding to 51 per cent in their Chinese business ventures. UBS increased its shareholding in its securities joint venture to 51 per cent in December 2018. JP Morgan raised its shareholding in a local mutual fund business to 51 per cent in July 2019. Many more foreign investments in the local financial services industry are expected. Nomura and JP Morgan are expected by the end of 2019 to open Nomura Orient International Securities and JPMorgan Chase Securities (China) Co Ltd respectively, both 51 per cent held securities joint ventures with local investment firms.

ii New Foreign Investment Law
Coming into effect on 1 January 2020, the Foreign Investment Law (FIL) seeks to be a comprehensive overhaul of foreign investment law. The Law was passed against the backdrop of intensifying trade tensions with the US. The aim of the Law is to boost foreign investor confidence and remedy issues that may have previously deterred investors. While the FIL attempts to provide greater legislative and commercial certainty for foreign investors, the FIL is an overarching framework until more specific regulations and directives are issued.

The FIL replaced existing rules in relation to FIEs (i.e., the Sino-Foreign Joint Venture Law, the Sino-Foreign Cooperative Joint Venture Law and the Wholly Foreign-Owned Enterprise Law). The Law brings together in consolidated form rules many areas of foreign investment, including the administration system for market access, the Negative List, corporate governance and operations.

Chinese legislation has a reputation for vagueness of language and wording, and there are provisions in the FIL that set unclear legislative expectations for the behaviour of investors.
Premier Li Keqiang has announced greater clarification on the law with a ‘series of matching regulations and directives’. The ensuing regulations are each predicted to delve deeper into a specific segment of the FIL.

A salient feature of the FIL are IP protections responding to foreign investor complaints about Chinese industrial policies that compel the transfer of IP from foreign investors. The FIL prohibits theft of IP by Chinese joint-venture partners and commercial secrets from foreign partners through protections listed in Article 22. The protections include criminal liability for government officials for use of administrative means to pursue forced technology transfers.

IV SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i German investment screening and European sharing mechanism

Outbound Chinese investors also face difficulties and restraints by the countries of target companies. Most notably, the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA), an amendment to the CFIUS, was signed into law in August 2018, creating a more severe regime in the United States for the review and approval of foreign investment based on perceived national security threats. Based on FIRRMA and later regulations promulgated by CFIUS in October 2018, transactions in certain emerging technological industries are subject to a mandatory filing for review. The potential effect of a transaction on eroding the US’ technological leadership is an explicit factor adopted by CFIUS in determining whether a transaction would result in a threat to US national security.

European policymakers have shown similar national security-related concerns and protectionist sentiment towards China as a rising industrial competitor. The cumulative acquisitions of European high tech companies by Chinese enterprises has prompted a response in Germany. In December 2018, Europe’s largest economy amended its foreign investment regulations, expanding the ability of the German Ministry for Economic Affairs and Energy to prohibit those acquisitions of German enterprises that are perceived to threaten Germany’s national security. The screening threshold for the acquisition of companies deemed relevant to Germany’s security was lowered from 25 to 10 per cent, and certain media enterprises are also included as companies subject to screening.

Earlier instances of German governmental intervention in 2018 included preventing State Grid Corporation of China from obtaining a 20 per cent stake in 50 Hertz Gmbh, one of Germany’s four transmission grid operators, in the summer of 2018 (through KfW, the German development bank, the German government instead acquired the stake in 50 Hertz Gmbh), and again in the summer of 2018, the German government prohibited the acquisition by China Yantai Taihai Corporation of Leifeld Metal Spinning AG, a German machine tool manufacturer.

The European Parliament, Council of European Union and European Commission reached an agreement in 2018 on the introduction of a Europe-wide investment screening and sharing mechanism. The framework requires European Union Member States to inform the European Commission and other Member States of any transactions that are currently being screened by it. The European Commission will also have the power to issue opinions as to whether an acquisition will pose security risks to European nations, albeit these opinions are non-binding. For investors being screened, this means that the review procedure is likely to become even more lengthy and prolonged.
V FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Policymakers have sought to reduce the outflow of capital from China through stricter screening enacted in measures first announced and then formalised between 2016 and 2018. In response to the effect of these policies on curtailing financing for outbound M&A by NRDC, MOFCOM and SAFE, Chinese investors developed alternative modes of fundraising to minimise domestic regulatory scrutiny, including the use of:

a. a guarantee or security structure in which a Chinese onshore entity or individual grants a guarantee or security for a debt owed to an offshore creditor by an offshore debtor – usually a subsidiary or controlled entity of the guarantee or security provided;\(^8\)

b. cash deposited with an onshore financial institution by a Chinese onshore investor and a loan granted by an offshore branch of the onshore financial institution to an offshore debtor – usually a subsidiary or controlled entity of the Chinese onshore investor;

c. loans advanced by foreign lenders to overseas Chinese investors’ subsidiaries secured by assets located outside China; and

d. equity and debt issuance in overseas markets.

For option (a) registration with SAFE is required for the guarantee or security, and NDRC and MOFCOM filings are necessary for such registration. Absence of such registration affects the enforceability of the guarantee and security.

VI EMPLOYMENT LAW

M&A transactions have triggered labour disputes or strikes leading to collective labour arbitration, hindering the completion of deals. Labour relations are established in the form of employment contracts and, barring any change to the subject qualification of an employment contract,\(^9\) labour relations are usually not affected. According to Article 40 of the Labour Contract Law and Article 26 of the Labour Law, a target has the right to terminate an employment contract if a material change in the objective circumstances relied upon at the time of conclusion of the contract renders it impossible for the seller to perform and, after consultation, the employer and the employee are unable to reach an agreement on amending the employment contract. As such, unless the M&A transaction leads to a ‘material change of the objective circumstances’ or the ‘subject qualification’ of the seller being eliminated, the seller does not hold a unilateral right to terminate the employment contract.

Whether an M&A transaction has caused a change in either condition depends to a large extent on the type of transaction. In general, a share acquisition does not affect the change of the legal subjects of the parties. Nor is it a ‘material change of the objective circumstances’ to the employment contract, so this type of transaction has no basis in providing the seller with the unilateral right to terminate the employment contract. In the case of an asset acquisition or business reorganisation, if it involves a transfer of assets, then this may constitute a material change of the objective circumstances, and the seller may unilaterally terminate employment contracts with employees.

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\(^8\) Known as *neibaowaidai*.

\(^9\) According to the relevant provisions of the Labour Contract Law, an enterprise with the subject qualification of labour and employment means it is established in the territory of the PRC, has not been declared bankrupt according to law, and no business licence has been revoked, been ordered to close, been revoked or been decided to be dissolved ahead of schedule.
Even though there is a right to unilaterally terminate an employment contract, the seller must still hold good faith negotiations with the employee to work out a comparable position before exercising termination. If the employment contract is terminated, the seller must provide severance based on the number of years of employment. In the case of large-scale layoffs of employees, sellers must carry out negotiations with the employees’ labour union and the local government to formulate a plan that includes providing advance notice to the employees.

VII TAX LAW

The State Administration of Taxation (SAT) levies enterprise income tax (withholding tax) at a rate of 10 per cent on the taxable income obtained by non-resident enterprise (NRE) transferors through cross-border M&A.


VIII COMPETITION LAW

Sweeping changes that had been enacted in March 2018 saw the anti-monopoly enforcement functions of three agencies (the Anti-Monopoly Bureau of the Ministry of Commerce, the Price Supervision/Inspection and Anti-Monopoly Bureau of the National Development and Reform Commission, and the Anti-Monopoly and Anti-Unfair Competition Bureau of the State Administration of Industry and Commerce) being consolidated under the control of the State Administration for Market Regulation (SAMR), including the role of merger control review.

M&A transactions meeting statutory thresholds and circumstances constituting a concentration of undertakings (i.e., an acquisition of control over a target) are subject to the merger control provisions of the Anti-Monopoly Law. If in the preceding financial year (1) the combined global turnover of the undertakings (i.e., the buyer or the target) exceeds 10 billion yuan, and the turnover from the PRC of each of at least two of the undertakings exceeds 400 million yuan, or (2) the combined turnover from the PRC exceeds 2 billion yuan, and the turnover from the PRC of each of at least two of the undertakings exceeds 400 million yuan, then the transaction must obtain clearance from the enforcement authority.

The enforcement authority has strengthened enforcement to ensure compliance with the filing requirements. In 2018, 13 deals were punished for failure to file and obtain clearance before closing. Punishment amounts to fines of no more than 500,000 yuan, though MOFCOM has the authority to go further and order the unwinding of a transaction or divestiture of certain businesses or assets.

Over 81 per cent of cases in 2018 fell under the simple application procedure, a process designed to abbreviate the duration of the review time for merger control reviews. The following types of transactions are generally eligible for the simple application procedure: (1) horizontal mergers in which the combined market share of the parties is less than
15 per cent; (2) vertical mergers and conglomerate mergers in which each party’s market share is less than 25 per cent; (3) acquisitions of shares or assets of a non-Chinese company that does not conduct economic activities in China; (4) the establishment of a non-Chinese joint venture that does not conduct economic activities in China; and (5) changes in control of a joint venture whereby the joint venture becomes controlled by one or more of the previously jointly controlling parents.

Lastly, some statistical figures shed light on enforcement activity in 2018: 444 applications were approved without any condition, increasing significant compared to 325 applications in 2017. Four applications were approved with conditions in 2018 under the Anti-Monopoly Law. The average time for acceptance and clearance shortened to 16 days from 24 days in 2017. In addition, 99.4 per cent of simple cases were cleared at the first stage (within 30 calendar days following the acceptance of an application), demonstrating that the simple case procedure plays an active role in improving the efficiency of merger control review.
I OVERVIEW OF M&A ACTIVITY

In 2018, M&A activity in Colombia decreased by 8 per cent as compared to 2017. However, M&A activity in 2019 is increasing, with factors such as a newly elected President who promotes foreign investment, a new tax reform, Colombia’s admission as an OECD member, the stability of macroeconomic figures and a strong rule of law coming into play. Compared to the first quarter of FY 2018, the number of transactions in Colombia in the first quarter of FY 2019 grew by 14.58 per cent, although the total aggregate value of the transactions decreased by 28.81 per cent. The Cross-Border M&A Index published by Transactional Track Record sets forth the following highlights for Colombia during the first quarter of 2019:

a) a total of 55 transactions (M&A, private equity, venture capital and asset acquisitions) worth US$972 million;
b) of these 55 transactions, 40 correspond to M&A and are worth US$387 million. Twenty-two transactions are ongoing and are worth US$326 million, and 18 transactions worth US$60 million have been completed;
c) of the 55 transactions, a total of nine correspond to asset acquisitions worth US$551 million. Six transactions, worth US$551 million, are ongoing, and three transactions, whose value has not been disclosed, have been completed;
d) a total of 30 cross-border inbound deals into Colombia worth US$263.08 million; and
e) a total of seven cross-border outbound deals from Colombia worth US$108.5 million.

Moreover, some of the factors ensuring the continuing success of M&A activity in Colombia are the following:

a) the approval of a tax reform that provides clarity to anxious dealmakers;
b) lower valuations because of strong foreign currency exchange as compared to Colombian pesos, resulting in cheaper targets;

1 Alexandra Montealegre and Stefania Olmos are associates at Baker McKenzie.
Colombia’s adherence to key international treaties;
buyers interested in acquiring distressed assets;
favourable regulatory environment, including a flexible foreign investment regime;
well-established orthodox financial management practices;
low inflation;
strong rule of law;
foreign asset management willing to invest in Colombian infrastructure projects;
the biggest infrastructure programme in Latin America, worth 16 trillion Colombian pesos;
implementation of peace agreements; and
global economic recovery, which is enhancing expectations of growth.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Colombian Commercial Code is the principal legal framework that sets forth the legal vehicles that are available to foreign investors in Colombia and the rules related to corporate governance of Colombian companies, such as quorums, veto rights, fiduciary duties of members of boards of directors and legal representatives, and general rules applicable to foreign investors aiming to conduct businesses in Colombia. Acquisitions of public companies (public takeovers) have special regulations under Colombian law, and are regulated primarily by, inter alia, Law 964/2005, which is the general statute regulating the Colombian securities market, and Decree 2555/2010, which regulates public takeovers.

Nevertheless, many features of Colombian M&A are familiar to global businesses and are similar to international standards of other jurisdictions, especially to New York law standards and styles. In the past, the common law contractual model has influenced the way acquisition agreements are drafted and negotiated in Colombia. It has become common in the legal market that shareholders’ agreements, asset purchase agreements and share purchase agreements in Colombia are drafted in a manner similar to New York law-governed agreements, sharing similar provisions.

In fact, in the past couple of years, local arbitrators and case law have accepted pro-sandbagging provisions under Colombian law and the right of buyers to be indemnified via share purchase agreements due to a breach of sellers’ representations and warranties of the sellers and of the target company. Such judicial decisions by local arbitrators have clarified that concepts arising out of share purchase agreements, although not expressly regulated under Colombian law, do have a legal reasoning and support under Colombian corporate principles and rules.

Therefore, the increasingly sophisticated M&A market in Colombia is another trend and reason for foreign investors to have confidence in the Colombian market.

Some key provisions that are frequently incorporated into the Colombian agreements that are common to New York-style provisions are as follows:
purchase price adjustments, including working capital adjustments and cash-free, debt-free adjustments, and the use of locked box mechanisms;

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6 Arbitrator’s award dated 1 September 2011 (Baclin Investments SL, Altra Inversiones Ltda, Mauricio Camargo Mejía and Dario Durán Echeverry as the buyers and claimants v. Jairo Gutiérrez Robayo, Jimena Gross Mejía, Carlos Andrés Torres Robayo, Néstor Andrés Beltrán Algara and Monserrat Gross Mejía as the Sellers and Plaintiffs).
non-compete provisions and agreements, which now regularly include non-solicitation clauses for the protection of employees and existing commercial relations and which are legal in Colombia only in the context of an acquisition process in order to protect the buyer and the value of the company; and

escrow agreements (holdback provisions are less common, although they are becoming increasingly more common, depending on the target).

In connection with indemnity provisions, limitations of liability (caps) are typically heavily negotiated and may vary depending on the risk level of the target, although the cap typically ranges between 15 to 20 per cent of the purchase price. Carveouts to the cap are generally accepted for fraud, special indemnities and fundamental representations (such as capitalisation, due authority and organisation, and ownership of shares or quotas). It has become increasingly common to leave Foreign Corrupt Practices Act or anti-bribery carveouts as fundamental representations and uncapped, especially when private equity funds are involved in deals and for infrastructure deals.

The Colombian Arbitration Statute\(^7\) sets out provisions for domestic and international arbitration and includes flexible and modern regulations for the benefit of foreign investors. For instance, with respect to dispute resolutions, it is increasingly common that when an international party is involved in a deal and the assets are located in Colombia, the international arbitration has Bogotá as the seat of arbitration. The advantage to this is that an award issued within an international arbitration seated in Bogotá is treated as a national award, and is enforceable without any recognition procedure. By contrast, when an award is issued outside Colombia, recognition is required prior to enforcement. It is also possible to have Bogotá as the venue and for hearings to be held in a neutral place.

In addition to having Bogotá as the seat of arbitration, foreign investors might choose as the rules of arbitration either the rules of the International Chamber of Commerce or the rules of the Bogotá Chamber of Commerce, which allows the choosing of international arbitrators instead of local arbitrators.

In connection with shareholders’ agreements under Colombian law, provisions are commonly negotiated for minority rights protections, such as the appointment of members of boards of directors, information rights, veto rights with respect to certain matters, the appointment of executive officers of the company, preemptive rights and tag-along rights. In addition, controlling shareholders often negotiate strongly for drag-along rights and control of the day-to-day management of the company. In the past, the enforceability of tag-along rights and drag-along rights under Colombian law were widely discussed, as this was not clear among arbitrators, judges and legal academia. Nowadays, according to a thesis by the Superintendence of Corporations and the flexibility of the simplified stock corporation form, these rights are increasingly common under Colombian shareholders’ agreements.

\(^7\) Law 1563 of 2012.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Tax reform

The Colombian tax system underwent a large-scale reform in 2018 as part of efforts to obtain the income required by an unbalanced governmental budget. This tax reform reduces companies’ taxation by reducing their income tax rates, progressively eliminating the presumptive income rate and excluding companies from wealth tax. Furthermore, the tax reform includes the following key changes, which are particularly important in the M&A area:

a it includes direct sales of shares, rights or assets located in Colombia as taxable events as if such shares, rights or assets were sold directly;
b it modifies the general rule to determine the fair market value (FMV) of direct sales of assets to include special rules designed to prevent tax avoidance; it also extended said rules to rendered services;
c it includes a withholding tax of 7.5 per cent applicable to the dividends payable to national legal persons, transferable to a foreign investor or to a local individual shareholder;
d it modifies the tax regime applicable to dividends payable to individuals; and
e it creates the Colombian holding regime (CHC) to grant certain tax benefits to companies created with the purpose of investing in other companies.

Withholding tax: dividends

A special 7.5 per cent withholding tax rate applies to dividends distributed as non-taxable income to resident companies (increased from 5 per cent in the original finance law bill). The withholding tax is payable only when an initial distribution is made to a resident company, and is treated as an imputed tax credit on a subsequent distribution to a Colombian resident (individuals) or an investor resident abroad. Dividends paid out of profits that were not taxed at the corporate level are subject to the general income tax rate (33 per cent for taxable year 2019). In this last case, the 7.5 per cent withholding tax also applies after deducting the tax paid at the general rate, resulting in an effective rate of 38.025 per cent for taxable year 2019. These rates also apply to dividends distributed to non-resident individuals and foreign entities, subject to certain exceptions.

Indirect transfers

The indirect transfer of shares or assets in Colombian entities are taxed in Colombia as if the underlying Colombian asset had been directly transferred. If a seller fails to report the deemed income arising out of an indirect transfer as taxable income or capital gain on the income tax return, the subordinate Colombian company would be jointly and severally liable

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8 Special thanks to Carlos Espinoza, group director of the tax team at Baker McKenzie Bogotá, for his contributions to and comments on this section.
for such applicable tax, as well as for any associated interest and penalties. The purchaser
also would be jointly and severally liable if the purchaser becomes aware that the transaction
constitutes abuse for tax purposes. These rules do not apply where:

a the underlying Colombian assets are shares that are listed on a stock exchange recognised
by a governmental authority, and no more than 20 per cent of the shares are owned by
a single beneficial owner; or

b where they represent less than 20 per cent of both the book value and the FMV of the
total assets held by the foreign entity being transferred.

These measures will certainly discourage indirect transfers of shares. However, if an indirect
transfer of shares were to be performed, the following contractual measures shall be taken
into account from the M&A perspective as per joint and several liability:

a a fundamental representation and warranty, probably on the seller’s side, shall be
included in the share purchase agreement stating that the transaction does not
constitute abuse for tax purposes. Such fundamental representation shall survive as per
the applicable statute of limitations and shall not be subject to any limitation of liability
included in the share purchase agreement (i.e., cap, basket, de minimis); and

b a covenant on the seller’s side shall be included in the share purchase agreement stating
that the seller will comply with the obligation to report the deemed income arising
from the indirect transfer.

**Tax incentives**

The CHC regime is introduced for resident companies whose main activities are holding
securities, investing in foreign or Colombian shares, or administering such investments, and
that comply with certain additional requirements. The following rules apply under the CHC
regime:

a dividends received by a CHC from a non-resident entity are exempt from tax in
Colombia;

b dividends distributed by a CHC to a non-resident individual or foreign company are
considered foreign-source income and therefore not taxed in Colombia (but dividends
distributed by a CHC to a resident individual or Colombian entity are taxed at the
normal rate, and are subject to the general income tax regime); and

c the distribution of premiums for the placement of shares is subject to the same
treatment as ordinary dividends: that is, as exempt income when the beneficiary is
a CHC, as foreign-source income if distributed by the CHC to a non-resident, or as
taxable income if distributed to a Colombian resident.

**Private equity funds**

The rules for the realisation of income by capital funds have been amended so that in certain
cases, and subject to the fulfilment of strict conditions, income from such funds will be
deemed to arise or to be realised for income tax purposes when the profits are effectively
distributed or paid to the beneficiary.
ii Foreign exchange rules

The government has been introducing important changes concerning the applicable foreign exchange procedures to increase Colombia’s competitiveness in foreign markets, internationalise the domestic economy and increase the investment of Colombians abroad. In response to Decree 117/2017 containing the rules governing foreign investments in Colombia and Colombian investments overseas, the Colombian Central Bank issued secondary legislation. Highlights include the following:

a Financial investments and investments in assets abroad made by Colombian investors exceeding US$500,000 do not need to be registered if the investment was paid with cash that does not need to be transacted through Colombian financial intermediaries; however, the rule requiring registration when cash is remitted from Colombia remains in place.

b While not directly related to foreign investments in companies, the Central Bank also issued new rules governing in a clear manner the purchase of local, Colombian peso-denominated A/Rs by non-Colombian investors seeking to become creditors of Colombian obligors under commercial transactions. This included rules on the acquisition of A/Rs held by local oil and gas companies subject to the special foreign exchange regime. These new regulations solved the controversy of whether Colombian peso-denominated A/Rs could be converted into foreign-currency assets held by offshore creditors.

c Regarding financial derivatives products, during 2018, the Central Bank modified certain restrictions to Colombian and foreign counterparties, eliminating the requirement for Colombian financial entities to enter into credit default swaps with foreign counterparties only whenever there was a related foreign investment operation. However, the Central Bank has maintained the provision mandating that local financial entities may only act as protection buyers and not as protection providers.

d Local financial entities may now enter into commodities derivatives with foreign counterparties. Furthermore, the Central Bank has removed the limited list of derivatives products that local counterparties may enter into. Finally, restrictions on the settlement (delivery or non-delivery) have been lifted.

These reforms undoubtedly bring more flexibility to the market and its participants.

iii New private equity regulation

To boost the development of the private equity funds industry in Colombia and attract new investors, the government recently issued Decree 1884 2018, which is aligned with international standards and best practices. The most important developments of the new Decree are as follows:

a allowing private equity funds to issue bonds (the issuance of bonds is restricted to private equity funds that grant credits);

b allowing private equity to grant credits to individuals and corporations and to buy receivables;

c units of private equity funds can be negotiated in the secondary market;

11 Special thank you to Sebastian Boada and Daniel Botero, senior associates in the banking and finance team at Baker McKenzie Bogota DC, for their contributions to this section.
private equity funds and their compartments are able to merge or spin-off, and are able to be assigned to an authorised manager; and

e new rules related to corporate governance have been introduced. For instance:
  • principles related to management;
  • the prevalence of the interest of investors in all the decisions to be made by a manager;
  • private equity funds shall have the obligation to prepare a conflict of interest policy; and
  • the investment committee shall meet at least once every three months.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Since 2010, US-based companies have been the most acquisitive in the Colombian market. Internet and technology companies have been the most attractive to foreign investors by deal volume.12 Among the main transactions that took place in 2018, the following rank as the biggest:

a Grupo Argos increased its participation in Odinsa from 54.7 to 99.8 per cent for 2,578,139 Colombian pesos;

b the acquisition of ExxonMobil’s distribution in the region by Terpel for 2.146 million Colombian pesos;

c the acquisition from the municipality of Bogotá of its 10.4 per cent shares in Grupo de Energía de Bogotá by AFP and other investors for 1.920 million Colombian pesos;

d the acquisition from Spain’s Gas Natural Fenosa by public tender offer of a controlling stake in Gas Natural SA ESP, one of the main gas distribution and retail supply companies in Colombia, by Brookfield Asset Management for 1.12 million13 Colombian pesos; and

e the purchase of Distribuidora Andina de Combustibles by Inversiones Primax and Primax Holdings for US$231.9 million.14

Furthermore, some of the largest transactions during the first quarter of 2019 included the following:

a Empresa de Energía del Pacífico’s (EPSA) purchase of the power generation assets, including hydropower plants and wind and solar projects, from Celsia for US$222.61 million;

b EPSA’s purchase of the electric energy distribution and commercialisation business of Enertolima for US$532.01 million;

c Gran Tierra Energy Colombia, Southeast Investment Corporation and Gran Tierra Resources’ purchase of Vetra Southeast (Spain) for US$102 million;

d Smurfit Kappa’s purchase of Smurfit Kappa Cartón de Colombia for US$101.72 million;


Financial and Insurance: Glenoaks Investments’ purchase of GNB Sudameris for US$60.4 million; and Tecnoglass’s purchase of Vidrio Andino for US$45 million.¹⁵

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Infrastructure

The fourth generation (4G) road infrastructure programme in Colombia involves 30 toll roads financed by local and foreign lenders. To date, financial closing has been reached for 14 of such 30 4G toll roads, and the financial closing for eight 4G toll roads is expected to occur this year.¹⁶ From 2016 until the first half of 2018, Colombia awarded 17 public–private partnership (PPP) infrastructure projects for an amount of US$8.4 billion. Fifteen out of the 17 projects focused on roads, with investment of US$8.4 billion; the remaining two projects focused on electricity, with investment of US$78 million. Furthermore, the President has established a taskforce within the Ministry of Transportation to facilitate PPPs for roads, and is promoting that more than US$4 billion be invested in Bogota’s first subway line as a municipal PPP.¹⁷ We expect M&A infrastructure activities to continue to grow in Colombia, primarily for the following reasons:

- the sale of the participation interests of some of the concessionaires of the 4G infrastructure projects;
- the appetite of international investors (Chinese, Brazilian, Spanish and Canadian investors, among others) in infrastructure projects; and
- the government’s promotion of foreign investment and the development of the country’s infrastructure.

Because of advances on the regulation and the strengthening of institutions for PPP initiatives in the infrastructure industry, Colombia is considered the second most favourable country in the region to develop such businesses. Reassurances provided by Law 1882 of 2018 include an enhancement of transparency in public procurement, and an increase of the possibilities for regional and municipal governments and state-owned companies to engage in PPPs. As regards the adequacy of the Colombian PPP agency’s staff, the National Infrastructure Agency received an award for its performance in 2018. Furthermore, the President has promoted transparency mechanisms as a response to the Odebrecht corruption scandals.

However, a challenge remains regarding Colombia’s investment and business climate score, which has been affected by bribery and corruption scandals. It is not certain that the measures imposed by Law 1882 of 2018 will be able to restore confidence after this reputational damage.¹⁸

¹⁷ The Economist, Intelligence Unit, Inter-American Development Bank, The 2019 Infrascope – Evaluating the environment for public–private partnerships in Latin America and the Caribbean.
¹⁸ The Economist, Intelligence Unit, Inter-American Development Bank, The 2019 Infrascope – Evaluating the environment for public–private partnerships in Latin America and the Caribbean.
ii New decision of the Constitutional Court related to infrastructure

To grant legal certainty to the infrastructure sector and to support the fight against corruption, the Constitutional Court conditioned Article 20 of Law 1882 of 2018 through a recent court ruling.19 Before being conditioned by the Constitutional Court, such article of Law 1882 stated that investors in a PPP shall be compensated for all the costs, expenses, investments and interest if such PPP agreement were to be annulled. This means that such compensation could be paid to investors whose unlawful conduct led to the annulment of a PPP, which ended up not penalising bribery and corruption, and infringing constitutional dispositions such as public morality, good faith and public interest.

In its decision, the Court considered that those who finance such projects (banks, funds, etc.) assume the major part of the capital risk, and therefore restitutions arising from the annulment of a PPP agreement are intended to pay a project’s debt. Moreover, no compensation shall be paid to a contractor or its members (for such purpose, the corporate veil may be lifted) if their unlawful conduct led to the annulment of a PPP agreement.

Furthermore, the Court stated that the government shall no longer pay for sanctions arising from the early termination of the applicable credit agreements of a PPP, given that the payment of the penalty clauses or the early termination sanctions agreed on by a contractor and lenders may not be justified against the public interest.

The decision of the Court is key for the development of infrastructure in Colombia, considering that this decision protects lenders and third parties that have invested in infrastructure projects and that have acted in good faith. Such court ruling shall reactivate the financial closings of the 4G toll road concessions given that the lenders will have their resources protected.

iii New infrastructure fund

The country’s biggest private equity fund for infrastructure started to operate with more than US$1 million provided by pension fund administrators and the Financiera de Desarrollo Nacional (FDN).20 This fund will co-invest with Caisse de dépôt et placement du Québec21 through a platform whose objective is to make capital investments in infrastructure projects and companies. The primary focus of the fund is to invest in roads. However, the fund also intends to purchase power and to invest in social infrastructure through work in the health and education sector, either through PPPs or privately, as well as in water, sanitation and waste management. In addition, the fund intends to invest mostly in brownfield projects and less in greenfield projects.22

iv Representation and warranties insurance

The increased use of representation and warranties (R&W) insurance in transactions has become a trend that reduces risks for buyers and investors in Colombia. Buyers increasingly

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19 Decision issued by the Constitutional Court on 16 May 2019.
20 FDN is a financial corporation that specialises in infrastructure. Its focus is on project finance and structuring.
21 Caisse de dépôt et placement du Québec is a long-term institutional investor that manages funds primarily for public and parapublic pension and insurance plans.
are willing to use R&W insurance in acquisition proposals to make their bids more attractive and competitive to sellers. In Colombia, this is still an emerging trend that is being analysed by buyers and sellers, and the insurance policies that are available are also being scrutinised.

The terms of the typical indemnity packages differ substantially between transactions that use or do not use R&W insurance. For example, the indemnity escrow amount and indemnity cap size are typically drastically lower in transactions using R&W insurance as compared to transactions that do not use such insurance. Therefore, from a seller’s perspective, R&W insurance may help expedite the sale process and improve sellers’ return on their investments. A seller may also attract superior bids, because R&W insurance may offer broader indemnification rights (particularly for a private equity or financial sponsor seller). Thus, by purchasing R&W insurance at a fixed cost, a seller may significantly reduce or eliminate contingent indemnification obligations. This protection is especially important for minority or passive sellers who have minimal knowledge or control over a target company.23

From a buyer’s perspective, R&W insurance mitigates the risk of not being able to enforce indemnity provisions where inter-jurisdictional legal processes may complicate matters. R&W insurance policies can also be greatly customised: they can provide protection beyond a limited indemnity cap, extend the duration of indemnification rights or replace indemnification altogether, providing a sole remedy for breaches of representations and warranties.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

i Legal security for lenders of PPP projects
See Section V.i in respect of the Constitutional Court’s ruling stating that restitutions arising from the annulment of a PPP agreement shall pay a project’s debt.

ii Issuance of green, social impact and project bonds
The local issuance of green and social impact bonds in 2017 and 2018 increased financing options, especially for sustainability focused projects. Colombia’s social impact bond was issued with the support of the Inter-American Development Bank in May 2018 for US$133.3 million with three-year and five-year maturities.

Since 2016, more than US$500 million-worth of green bonds have been issued in Colombia with the participation of banks, energy companies, multilaterals and local investors. According to the Climate Bonds Initiative, green bond issuance grew a steady 4 per cent year-on-year to US$162 billion in 2018.

Bancolombia SA24 took a performance-based approach to satisfy investors and pivot the construction market towards a more sustainable future, focusing its efforts on green buildings (above other areas that it also finances, such as clean production and agribusiness). The bank provides variable loans for green construction financing from 0.5 to 2 per cent less than conventional market rates by using its own resources alongside the proceeds of the green bonds. The more measurably green a project is, the better the financing rate. Qualified projects must receive a preliminary design certificate from an approved green buildings rating system such as LEED or the International Finance Corporation’s EDGE.

24 Colombia’s largest commercial bank.
The success of these early examples, and the support they have received from multilaterals and other organisations, could encourage their implementation in other countries in the region, opening up alternative forms of financing that could be applied to infrastructure and PPP investments.

As to project bonds, nearly US$2 billion has been issued from Colombia since 2015, mostly related to the 4G toll road programme. The 4G-related US dollar project bond size has been constrained by the fact that the projects under the 4G programme are substantially reliant on local currency revenues through user pay tolls, complemented by the availability of payments and certain revenue top-ups made directly by the National Infrastructure Agency (ANI).

Issuances related to the 4G programme have been able to attract international institutional investors anchored by ANI’s payment obligations and on external credit enhancement provided by Colombia’s development bank, FDN, in the form of subordinated revolving liquidity facilities.

VII EMPLOYMENT LAW

i Legislation relevant for M&A

The labour legislation relevant for M&A in the Colombian jurisdiction varies depending on whether a transaction is conducted as an asset transfer or as a purchase of shares. When a business is acquired by means of a stock purchase agreement, the transaction will not involve a change of employer. Therefore, employees and their conditions, benefits and entitlements are unaffected.

However, if a deal is structured as an asset deal that involves the transfer of personnel, and if the parties involved in the transaction do not previously assign or terminate their employment agreements, this would be considered to be an employer substitution. Pursuant to Colombian law, this would operate automatically upon the execution of an asset purchase agreement and the transfer of personnel.

The main effects of employer substitution under Colombian law are the following:25

a Employment agreements of employees are not modified, suspended or terminated, and all risks, duties and liabilities will be transferred to the buyer.

b The buyer must therefore match the salaries and benefits that the employees are already receiving.

c If the incoming employees have enjoyed different employment benefits compared with those of the purchaser’s existing employees in similar job roles, the purchaser might be forced to match these by offering all employees the most favourable conditions (unless otherwise agreed with all the employees, both old and new).

d All employees’ seniority must be preserved for all legal purposes.

e The pension liabilities of the seller will be transferred to the buyer.

f The former and new employers would be considered jointly and severally liable for all labour obligations relating to the employment agreements existing at the time the employer substitution takes place, and the new employer will be responsible for the obligations that come into effect after the substitution occurs. If the new employer


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assumes payments regarding labour obligations that the old employer was forced to recognise, then the new employer can recover them from the old employer, unless agreed otherwise.

VIII TAX LAW
See Section III.i.

IX COMPETITION LAW

i Competition law relevant for M&A
As per the Colombian competition rules, M&A are subject to antitrust clearance by the Superintendence of Industry and Commerce (SIC) when the following criteria are met:

a objective criteria: total assets or joint operating income of the parties involved in the transaction during the fiscal year prior to the closing date, individually or combined, exceed the annual thresholds established by the SIC. For transactions undertaken in 2019, the threshold is equivalent to approximately US$14.4 million; and

b subjective criteria: the parties involved in the transaction are engaged in the same economic activity and therefore establish a horizontal relationship (horizontal mergers); or participate in the same chain of value, establishing a vertical relationship (vertical mergers) in one or more markets in Colombia regardless of the legal structure used for such purpose.

However, if the subjective criteria set forth above are met but the combined market share of the parties involved in the transaction is under 20 per cent, the parties can apply for a fast-track (implied) approval by submitting a simplified form (notice) before the SIC. The SIC, however, does not issue any opinion or ruling confirming such approval, and the notice is answered by a letter whereby the SIC acknowledges receipt of such notice, within 10 business days counted from the day of the filing before the SIC. Nevertheless, if the combined market share of the parties is equal to or above 20 per cent, the parties must obtain clearance from the SIC through a full filing from which the SIC has the right to approve, or oppose the proposed transaction, or to impose remedies on the proposed transaction. The time frame for clearance depends on the complexity of the competition issues triggered by a transaction, and usually takes from four to eight months.

26 Special thank you to the antitrust team of Baker McKenzie Bogotá: Carolina Pardo, principal partner, Angélica Navarro, senior associate and Mariana Camacho, junior associate for their contributions and analysis to this Competition law section.
28 A chain of value is a set of activities performed pursuant to which the product delivered is input for another product.

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ii Gun jumping

In Colombia, during the past year the SIC has become increasingly active in regulating pre-closing behaviours and transaction structures, and this is a trend we expect to continue. Gun jumping relates to the unlawful coordination between the parties of an M&A deal pre-acquisition or pre-merger.

Specifically, gun jumping may occur during the negotiation or due diligence process, between signing and closing, or before the closing of a transaction when:

- the parties take (or participate in) concrete decisions in relation to the other party’s business affairs, customer relationships, marketing programmes, pricing, price setting, price-related decisions, suppliers or supply-related decisions, or any other commercial decision;
- the parties exchange competitively sensitive information between the parties involved in the transaction, absent additional safeguards;
- one party intervenes in another party’s business decisions or operational management decisions (e.g., by way of a consent mechanism as part of the share purchase agreement covenants);
- one party provides access to another party’s IT systems or other support functions; and
- there is any other action that could be construed as contributing to one party having control over the activities of the other or others before gaining clearance by the antitrust authority and before the transaction is closed.

To mitigate the risk of gun jumping, it is advisable to take certain measures and implement them until closing, especially in the due diligence and negotiation phases of a transaction.

Such measures include designating specialised teams in each of the parties involved, with such members being the only individuals on each side of the negotiation with access to the other parties’ competitively sensitive information. Clean team members should only have access to this information to the extent they do not have influence over the commercial decisions of the company that they represent and pursuant to certain confidentiality protocols.

Parties may also agree on interim operating covenants that do not grant them any decision-making power or control over the other party (including veto powers) but that reflect the purchaser’s interest in preserving the value of the investment. Parties should implement these covenants through clean team protocols.

Clean team covenants should avoid situations where either party can:

- influence the appointment of the senior management of the other party;
- influence the other party’s pricing policies;
- influence commercial decisions of the other party (e.g., through vetoing of tax filings);
- influence the target while entering into, terminating or modifying commercial contracts or agreements; or
- access commercially sensitive information of the other party during the period before signing and closing.

The design of the protocols should guarantee that should the transaction not close, the parties will continue to act as independent competitors within the relevant market.
I OVERVIEW OF M&A ACTIVITY

Costa Rica is a development success story in many respects. There has been steady economic expansion for more than a quarter of a century, and a stable democracy has been in place since 1949, allowing the country to enjoy growth for several years thanks to a strategy of outward-oriented growth based on openness to foreign investment and gradual trade liberalisation.

Costa Rica is also a global leader with regard to its environmental policies and accomplishments, which have helped the country to build its green trademark by promoting forest and biodiversity conservation and the use of renewable energy sources.

The Costa Rican Investment Promotion Agency (CINDE) is a private, non-profit and non-political organisation appointed by the government to promote foreign investment. It has attracted more than 200 companies since it was formed more than 30 years ago, including worldwide leaders such as Intel, Hewlett-Packard, Procter and Gamble, to name but a few. More recently, Amazon, McKinsey & Co and Microsoft have announced that they intend to expand their operations here.

The Social Progress Imperative global index ranked Costa Rica 33rd out of 146 countries in 2018. Of all the Latin American countries included in the report, Costa Rica ranks first as the country with the greatest social progress in the region, well ahead of some of the major regional players.2

According to the Global Competitiveness Report of the World Economic Forum, Costa Rica was catalogued as an economy transitioning from Stage 2 (efficiency-driven economies) to Stage 3 (innovation-driven economies). The country was ranked 55th out of 140 countries on the Global Competitiveness Index for 2018, third in Latin America after Chile and Mexico and ahead of Panama.3

Costa Rica’s gross domestic product (GDP) per capita has tripled since 1960, and its growth averaged 4.5 per cent between 2000 and 2013, as compared to the regional average of 3.8 per cent for the same period. According to World Bank information, the country’s GDP in 2017 was US$57.29 billion, with economic growth of 3.3 per cent. Inflation for 2017 was at 2 per cent.

Costa Rica’s economy is predominantly services-based. The services export industry includes business process offshoring (BPO), information technology offshoring and shared services. BPO itself covers a wide range of services. There are many large corporations with

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1 John Aguilar Quesada and Marco Solano are partners at Aguilar Castillo Love.
2 Data from www.socialprogressimperative.org.
3 Data from http://reports.weforum.org/global-competitiveness-index/competitiveness-rankings/.
BPO operations in Costa Rica, including Hewlett-Packard, Intel, Bridgestone, Amazon, Procter and Gamble, Western Union, Emerson Electric and IBM. Some companies combine BPO services with manufacturing or repair facilities. Costa Rica's economy also has a thriving medical device manufacturing industry that includes Baxter, Covidien, Abbot, Boston Scientific, Allergan and St Jude Medical.

According to data from the World Bank, exports of goods and services in Costa Rica represent 33 per cent of the country's GDP. In 2017, exports to European and Asian countries thrived, with countries of both regions experiencing significant growth.

In 2017, 40.5 per cent of exports from Costa Rica were to the United States, followed by Belgium (6.5 per cent), Panama (5.6 per cent), the Netherlands (5.5 per cent) and Nicaragua (5.3 per cent).

The Costa Rican M&A market was equally as active in 2018 as in 2017 (based on data available at the Commission for Competition Promotion (Coprocom)). Consumer and service sectors were the main drivers.

During 2018, multinational firms continued to purchase medium-sized companies to position themselves in the Central American market. There were also cases of local and Central American groups buying competitors to strengthen their market presence. Transactions during 2018 continued to focus on medium-sized enterprises.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Costa Rica is a civil law country. Case law is only relevant in the interpretation of the law.

The Commerce Code\(^4\) regulates mercantile (commercial) companies in general. From a corporate law standpoint, M&A are contemplated in the Commerce Code.

Costa Rican competition law is set out in the Law for the Promotion of Competition and Effective Consumer Protection (CR-LPC).\(^5\)

Chapters 3, 6 and 7 of the First Book of the Commerce Code regulate the two most common corporate forms: corporations and limited liability companies. These Chapters include company acquisition-related regulations, but there is no specific acquisition title or chapter. The regulations mainly concern the transfer of shares or equity participations and associated requirements.

The purchase of ongoing businesses is different from a company acquisition, and is regulated in Chapter 3 (Title 1) of the Second Book of the Commerce Code (Articles 478 and 489). Chapter 3 establishes requirements for the transfer of ongoing businesses, including publication (for three consecutive days) in the official newspaper and giving notice to the enterprise's creditors so that they have an opportunity to oppose the acquisition or exercise their rights for a period of 15 days. Payment of the purchase price, according to Article 480, is not to be made before the 15-day period expires and until liquidation of accounts payable is made. Escrow of funds is commonly used for this purpose.

If the formalities established in Chapter 3 are not met, the transaction will be absolutely void (for any eventual rights of third parties or creditors of the acquired ongoing business) and payments made to the creditor will not be considered valid.

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\(^4\) The Commerce Code (Law No. 3284 of 30 April 1964).

Regarding mergers, Chapter 10 of the First Book of the Commerce Code, ‘Mergers and transformations’, includes a very basic set of regulations regarding the legal nature of a merger and the formal requirements to complete it. Merging entities may either form a new company or be merged via absorption (acquisition), in which only one of the entities survives.

From a corporate law standpoint, the requirements to complete a merger are simple: a pre-merger project or agreement, approval via extraordinary shareholders’ meetings (of all entities involved) and publication of an extract of the merger approval in writing or in a deed in the official newspaper. The merger will be effective a month after its publication and registration if no third party opposes it. In principle, recordable assets will be transferred to the resulting or surviving entity.

Competition law requirements to complete mergers, company acquisitions and purchases of ongoing businesses are described in the next section.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

As indicated, Costa Rican competition law is set out in the CR-LPC.

Preliminary merger control for transactions of a certain volume (over a threshold of US$15 million) or of special relevance to the national market is mandatory.

A merger or acquisition may be considered a concentration under Article 16 of the CR-LPC, so even though parties are free to consolidate a merger or an acquisition, they are required to file a notification or previous communication to the Coprocom if meeting the criteria established in the CR-LPC.

M&A control in Costa Rica uses a short authorisation proceeding. If the preliminary merger control notice is not sent, the Coprocom may challenge a merger proven to qualify as a concentration by opening a penalising proceeding.

Mergers or acquisitions involving regulated entities (banks, public companies, financial entities, pension funds, companies managing funds of third parties and insurance companies), in addition to the previous communication to the Coprocom, must obtain the applicable approvals of the Securities Supervisory Agency (SUGEVAL), the Private Pension Funds Supervisory Agency (SUPEN), the General Insurance Supervisory Agency (SUGESE), the General Telecommunications Supervisory Agency (SUTEL) or the Financial Entities Supervisory Agency (SUGEF), as appropriate.

According to the amended version of Article 16 CR-LPC, a concentration is defined as:

[a] merger, sale of business premises, or any other act or contract by which companies merge, form partnerships, acquire shares, share equity, form trusts, merge or combine management, representation or general assets; made between competitors, suppliers, customers or other operators who have been independent in respect to each other, and result in the acquisition of economic control by one over the other or others, or in the formation of a new economic agent under joint control of two or more competitors, and any transaction in which any natural or legal person, public or private, acquires control of two or more independent economic agents, actual or potential competitors.
The enactment of the Tax Collection and Management Act and the General Tax Procedure Regulations are discussed below. Although specific M&A regulations are not contained in either set of Regulations, there are indirect applications or consequences to mergers, company acquisitions and the purchase of ongoing businesses.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Acquisitions, expansions and ventures took place in Costa Rica in several sectors during 2018. While US companies and European multinationals were the main participants, Latin American groups were also involved.

Costa Rica continues to pursue high-quality foreign investment. CINDE and the Procomer lead Costa Rica’s investment promotion efforts. CINDE has focused on creating clusters of related businesses, successfully targeting potential investors in the areas of medical devices, services (shared services, BPO, global in-house centres) and advanced manufacturing.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The following is a summary of relevant 2018 transactions, expansions and projects in Costa Rica:

<table>
<thead>
<tr>
<th>Acquirer</th>
<th>Transaction</th>
<th>Target or targets</th>
<th>Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capitales Moonriver</td>
<td>Acquisition</td>
<td>Go Pato</td>
<td>Delivery application</td>
</tr>
<tr>
<td>ABB Ltd</td>
<td>Acquisition</td>
<td>General Electric Industrial Solutions</td>
<td>Electric products</td>
</tr>
<tr>
<td>Banco Davivienda</td>
<td>Acquisition</td>
<td>Grupo Kineret</td>
<td>Financial</td>
</tr>
<tr>
<td>KKR &amp; Co LP</td>
<td>Acquisition</td>
<td>Unilever (spreads division)</td>
<td>Consumer</td>
</tr>
<tr>
<td>Grupo CCR</td>
<td>Acquisition</td>
<td>Aeris Holdings/Airport Worldwide</td>
<td>Airport</td>
</tr>
</tbody>
</table>

Of special note during 2018 was a transaction involving Corporación de Supermercados Unidos (CSU or Walmart), as a potential buyer of Grupo Empresarial de Supermercados (GESSA), as seller. The Coprocom denied approval of the transaction on the grounds that CSU boasted a condition of substantial power in the markets under investigation and that the increase in shareholdings and power resulting from the proposed merger with GESSA would have increased and strengthened the substantial power position already held by CSU. Although CSU appealed the decision, it is unlikely that the Coprocom will change its criteria on the basis of the power position that would be boasted by CSU, but the case is still pending final resolution.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Acquisition financing is available for transactions. The most common funding structures, regardless of the acquirer, are bank lending, corporate debt, capital increases (private placement of shares of stock), and securitisations or security trust agreements.6

6 http://latinlawyer.com/jurisdiction/1003113/costa%20rica.
Withholding taxes are an important issue to take into account in establishing funding structures and schemes, as these may apply if interest is paid to a bank domiciled abroad.

M&A financing has mainly come from abroad. As has traditionally been the case, M&A are still financed in the acquirer’s market or through regional or global banks. However, regional banks are becoming more involved in M&A transactions.

VII EMPLOYMENT LAW

No recent relevant amendments or modifications to Costa Rican labour regulations affecting mergers or acquisitions have been issued. The only applicable regulation in the Code of Labour Law is still the employer substitution rule, according to which both parties involved in an acquisition (or employer substitution) will be jointly liable for six months after the substitution is completed or verified regarding employees’ termination rights and benefits. Once this period expires, the new employer remains solely liable for termination rights and benefits.

VIII TAX LAW

Except for a few exceptions discussed below related to tax auditing, the tax system has not been recently amended. The country’s tax regulations establish that residents and corporations are taxed only on income earned in Costa Rica. The following is a summary of the main applicable taxes.

i Income tax
This applies to individuals as well as legal entities for income originating from a Costa Rican source. Taxable income is based on net income. Capital gains are generally not subject to income tax, except when the transfer activity is regular or when transferring assets that were subject to depreciation. In the latter case, the applicable rate is 30 per cent on the capital gain. Withholding taxes apply, inter alia, to dividends (15 per cent), interest (15 per cent), royalties (25 per cent) and fees (25 per cent).

ii Annual property tax
Property tax is rated at 0.25 per cent of the value of a property, and may be paid annually, by semester or by quarter depending on the procedures established by the local government (municipality).

iii Transfer taxes
There is a 1.5 per cent real property transfer tax and a 2.5 per cent vehicle transfer tax. This tax is based upon the higher of the registered value or the deed value at the time of sale.

iv Stamp duty
This applies to all contracts and agreements at a rate of 0.5 per cent of the documents’ economic value.
v Sales tax
This is imposed on certain taxable transactions at a rate of 13 per cent and is paid monthly.

After the enactment of the Tax Collection and Management Act in October 2012, the General Tax Procedure Regulations were approved. Although specific M&A regulations are not contained in them, the Regulations are broad and complex, and they contain stricter rules and new capacities for the Tax Administration that should orient acquisition or merger processes during due diligence and implementation.

The rule contained in the amended Code of Policies and Procedures Tax is that assets will be subject to companies’ enforceable tax debts even after a transformation, merger or company acquisition process, or the transfer of ongoing businesses. For assets to be subject to companies’ enforceable tax debts after a transformation, merger, acquisition process or the transfer of ongoing business process, the debt has to be enforceable prior to the process.

Also important to take into account is that the Tax Collection and Management Act also imposes transfer tax (as described above) on indirect transfers (when a company holds real properties and vehicles, and the company is transferred to new group of shareholders as a whole). In principle, transfer tax does not apply to mergers: the application of transfer tax has not been yet been interpreted by the Tax Administration in connection with acquisitions.

No other recent relevant amendments or modifications to the Costa Rican tax regulations affecting mergers or acquisitions have been issued.

IX COMPETITION LAW
As outlined in Section III, Costa Rican competition law is set out in the CR-LPC. Mergers, company acquisitions or the purchase of ongoing businesses may be interpreted by the Coprocom as a concentration under Article 16 of the CR-LPC, so preliminary merger control for transactions of a certain volume or special relevance is mandatory.

Other agencies may also exercise control over mergers, acquisitions or other relevant transactions in connection with public companies, financial entities, pension funds, companies managing funds of third parties and insurance companies, based on the regulations issued by Conassif, the National Council of Supervision of the Financial System. These agencies are Sugeval, Supen, Sugese, Sutel and Sugef.

X OUTLOOK
Costa Rica has continued to experience economic growth during the past year. The country presents a winning combination of skills and opportunities that are appealing to export and services-oriented foreign investment. Costa Rica’s attractiveness for foreign investment has started shifting to emerging areas such as, inter alia, IT, knowledge processes, finance and accounting, which require sophisticated skills and technological infrastructure.

Experts consider recent developments in the Costa Rican services market to be part of its natural evolution.7 Other developments include the establishment of shared service

centres and manufacturing facilities outside the Greater Metropolitan Area, as well as the establishment of energy, infrastructure and tourism projects, creating continuous M&A opportunities for sophisticated investors and investment banking firms.

Costa Rica continues to evolve as a destination for investors with strong promotion and protection programmes and friendly policies. Even though the size of the Costa Rican and Central American market is not as significant as other countries in Latin America, in terms of retail operations, its pursuit of growth will continue drawing multinationals that feel comfortable with the above-mentioned mixture of skills and opportunities.
I OVERVIEW OF M&A ACTIVITY

During the past few years, we have seen important M&A activity taking place. The Dominican economy continues to outperform most economies in the Latin American and Caribbean region (averaging 7 per cent GDP growth over the past three years), and major foreign investment continue to develop and grow in the Dominican Republic, together with strong levels of M&A activity.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A deals occur through a merger by incorporation of a new entity or absorption of one or more of the companies merged, a share transfer or an asset purchase.

Law No. 479-08 of General Companies and Limited Liability Individual Enterprises was enacted in December 2008 and later modified by Law No. 31-11 (Companies Law). This statute repealed the provisions effective until the current date of the Commercial Code regarding companies (Articles 18 to 64 inclusive), introduced important legal modifications concerning the incorporation, life and dissolution of companies, and, in addition to the existing corporate vehicles, introduced three new corporate vehicles: the limited liability company (LLC), limited liability individual enterprise and simplified company.

Moreover, Chapter IV of the Companies Law provides a definition for the term merger and establishes a process for its fulfilment from a corporate standpoint. It defines a merger as a transfer made by one or more companies of their assets and liabilities, either to an existing company or to a new one, whereby the shareholders of the company that makes the transfer receives shares in the company or companies that receive the assets and liabilities, and eventually, a liquid amount that cannot exceed one-tenth of the nominal value of the shares.2

The merger must be approved by a shareholders’ extraordinary meeting of all the companies involved, and will entail the following consequences: the dissolution without liquidation of the companies that disappear, and the transfer of all their assets and liabilities in the state in which they are present on the date of final completion of the transaction to the beneficiary companies. Simultaneously, the shareholders of the disappearing companies become shareholders in the recipient companies. When a new company is incorporated as a

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1 Georges Santoni Recio is a partner and Laura Fernández-Peix Pérez is a senior associate at Russin, Vecchi & Heredia Bonetti.

2 Article 382 of the Companies Law.
result of a merger, its by-laws must be approved by an extraordinary general meeting of all the companies that will cease to exist, and the new company must confirm and acknowledge those approvals. The companies involved must execute a merger agreement.

Before the approval of the merger, the companies involved in the transaction must appoint one or more commissioners, who must render a written report with the particulars of the merger, and who shall verify that the value attributed to the shares of the participating companies are adequate and that the rate of change is equitable. Additionally, the report must include the estimated value of in-kind contributions and particular advantages, if there are any. The report will be made available to the shareholders prior to the meeting, and must be taken into consideration during the meeting before the approval of the merger.

Commissioners must have a bachelor’s degree in accounting, business administration, finance or economics, and at least three years’ experience in their profession. There are certain conditions that prohibit individuals from being appointed as commissioners:

\[ a \] conviction for criminal offences or bankruptcy (fraudulent or not) by an irrevocable judgment;
\[ b \] disbarment, by virtue of a judicial or administrative decision, from the practice of commercial activities;
\[ c \] the individuals are public officers with duties related to the activities of the company;
\[ d \] the individuals are the founders, in-kind contributors, beneficiaries of particular advantages, directors of the company or its subsidiaries and their relatives up to the fourth degree;
\[ e \] the individuals are directors (and their spouses) of other companies that own one-tenth of the paid capital of the company in question; and
\[ f \] the individuals are any person (or his or her spouse) who directly or indirectly receives a salary or compensation from the company for undertaking permanent activities different from those assigned to the commissioner.

Commissioners may require the delivery of all useful documents related to the merger from all the companies involved, and will provide the necessary confirmation of their content. Likewise, depending on the types of companies involved, the boards of directors of the companies must render a written report on the merger project.

Within 30 days of the execution of the merger agreement, the companies involved in the process must file it along with the meeting minutes that approved the agreement before the corresponding chamber of commerce. Additionally, an extract with the main terms of the merger agreement must be published in a newspaper with national circulation.

In contrast, a shareholders’ meeting is not always required when an acquisition is made through an assets purchase; this will depend on the types of assets being purchased and the by-law requirements. If a company is selling all its assets, a shareholders’ meeting must approve the sale. Nonetheless, the law and principles that govern the agreement itself will be those of the Civil Code. Notwithstanding this, the parties are free to choose the jurisdiction that will govern the agreement.

Regarding acquisitions made by share transfer, depending on the type of entity that is selling the shares and the provisions of the by-laws, existing shareholders may have the right of first refusal or right of first offer and, in some cases, tag-along rights. The Companies Law governs shared transfers.
The Restructuring Law\(^3\) was enacted on 12 August 2015 and came into effect in February 2017. Its Ruling for application was also enacted in February 2017. Under the Restructuring Law, if any company or merchant is in cessation of payments over a certain period,\(^4\) or if at least one of the other scenarios provided in Article 29 of the Law occurs, the affected party or the debtor can request the restructuring of the company. If the formalities for requesting a restructuring process have been met, a verifier will be appointed who will confirm whether there are grounds for the debtor to undergo a restructuring process. If so, a conciliator will be appointed, and the process should end in a restructuring plan that is approved between the majority (60 per cent or more) of the acknowledged and registered creditors and the debtor. If it is not feasible for the debtor to undergo a restructuring process, the liquidation of the company could be ordered by a court. If this occurs, a liquidator will be appointed and will perform all actions related to the sale of the company as a whole (running business) or the company's assets. Once a restructuring request has been filed at court by the debtor, or the debtor has been notified by the creditor or creditors of a filing at court of a restructuring request, the debtor must inform the court and the verifier, among other actions, of any act that represents a direct or indirect merger of the debtor.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Regarding takeover provisions, the Companies Law provides that in every company, except LLCs, any shareholder (individual or legal entity) that achieves a participation of more than 10 per cent of the voting shares must notify the company, via a bailiff's act, within a 15-day period counted from the acquisition of shares that amounted to 10 per cent or higher, indicating the number of shares owned and the votes it has in a shareholders' meeting. LLCs are excluded from this requirement, presumably because the Law specifically provides for their shareholders and the company itself rights of first refusal, whereas in other companies those provisions are only in place if they are included in the company's by-laws. Thus, because of its \textit{intuitu personae} nature, an LLC always knows the intention of its shareholders to transfer shares in advance, and the number of shares being transferred, and can therefore take action on the transaction should it wish to do so.

The Law also provides that a corporation cannot have investments in another company if the latter holds 10 per cent or more of the capital of the former. Likewise, there is a similar provision for any other type of company that has a corporation among its shareholders.

Even though the Securities Law\(^5\) regulates the stock market, and the Companies Law provides certain provisions applicable to corporations whose shares are publicly traded, to date there is not a single company that is publicly traded; thus, the probability of a hostile takeover occurring on a Dominican company is very remote.

\(^3\) Law No. 141-15 on the restructuring and liquidation of companies and merchants.

\(^4\) This will vary depending on the obligation that was unpaid; for example, two months of employees' salaries, or payments overdue to a creditor or creditors for 90 days.

\(^5\) Securities Law, Law No. 249-17.
IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

The vast majority of M&A transactions that have occurred in the Dominican Republic have been from foreign investments and from different countries. As a result of the financial crisis, the number of business synergies, mergers and consolidations keeps increasing as a way to cope with the difficult economic conditions.

Banking institutions, both local and foreign, have a prominent influence on M&A transactions.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The number of M&A has risen during recent years. While there might not be a significant difference in the volume of the transactions taking place, the settlement of transactions, and the high-profile entities that have merged or that have been acquired, have increased exponentially.

The most relevant M&A during the past few years are as follows:

\[a\] in 2016:
- a French group acquired the majority (70 per cent) of a fund that owns approximately 130 petrol stations throughout the Dominican Republic from a US parent company;
- a Japanese company acquired 50 per cent of the shares of a local cigar company. The deal is said to have amounted to around US$14 million; and
- an American hotel group acquired a hotel group that had several hotels in the Dominican Republic. The deal was concluded in September 2016;

\[b\] in 2017:
- a Spanish hotel group acquired three hotels in the Dominican Republic for approximately US$100 million. The deal was concluded in December 2017;
- a Japanese company, the leader in the sanitary industry, acquired a local factory in the same market. The deal was announced in November 2017;
- a Lithuanian airline that owned 65 per cent of the shares of a Dominican airline sold its shares in June 2017; and
- other M&A deals mainly happened abroad but affected the Dominican Republic: for example, a Dutch–British multinational signed an agreement to acquire the personal care and house cleaning line brands from a Colombian multinational, both of which have a presence in the Dominican Republic;

\[c\] in 2018:
- the largest Brazilian company in the brewery industry increased its ownership (to 85 per cent) in the main local brewery by acquiring an additional 30 per cent of the shares. The deal is said to have amounted to around US$926.5 million. The deal was announced at the end of 2017 and finalised at the beginning of 2018; and

\[d\] to date in 2019:
- a Canadian independent supplier and marketer of fuel and petroleum products acquired 75 per cent of the shares of the company that indirectly owned one of the top petrol stations in the Dominican Republic; and
- a Canadian bank acquired 97.44 per cent of an important local bank. The deal is said to have amounted to around US$330 million. The deal was announced on August 2018, and finalised at the beginning of 2019.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Typically, M&A are financed through loans that are guaranteed by assets of the buying company or one or more of its subsidiaries, debt finance or private equity funds.

When financed through loans, several banks are usually involved in the lending. In the case of Dominican banks, solvency ratio restrictions are determined by Monetary and Financial Law No. 183-02, which places certain boundaries on the lending bank with regard to the amount that can be lent to a single entity or economic group. Moreover, while Dominican banks are participants in the financing of different mergers taking place in the Dominican Republic, the main lenders are almost always foreign banks, particularly US banks.

As indicated above, when a bank grants a loan, usually certain assets of either the parent company or one or more of its subsidiaries are given in guarantee. If the assets placed in guarantee are located in the Dominican Republic, depending on the type of assets, there are filings and recording processes to be fulfilled. Typically, tangible assets (such as machinery, equipment, vehicles) are given in chattels without loss of possession, as governed by the Law of Agriculture Foment. There are certain formalities and restrictions surrounding chattels without loss of possession; for example, a borrower cannot grant a chattel over assets that have already been pledged unless the previous lender renounces its rights. In addition, the contract must be executed before a justice of the peace or a notary public, and it must be recorded by the justice of the peace of the domicile of the borrower in order to make it opposable to third parties and in this way safeguard the privilege that the creditor is entitled to with the subscription of this type of contract. Furthermore, if the assets are vehicles, in addition to the chattel without loss of possession recordation, a transfer opposition is recorded before the Tax Office to avoid the transfer of the registration of the vehicles.

When the guarantee is real property, it must be recorded before the corresponding title registry of the real property, and a 2 per cent lien over the value of the property must be paid to the Tax Office.

Furthermore, local financing institutions typically require that the borrowing company executes a promissory note, which is a form of security that is invested by the prerogatives provided for by Article 545 of the Civil Procedural Code, and it will be considered a title of enforcement, without the need for a court ruling, in the event of the debtor’s default. The promissory note has very specific and mandatory rules as to the form of the document, and must be drawn up by a local notary public. Among the requirements of the promissory note are that it must be in Spanish, and be validated and executed by the borrower in the presence of a notary public. Stamp tax and recording fees apply.

Regarding debt finance, since acquirers are mainly foreign, bonds and other forms of securities are rarely placed in the Dominican Republic. However, if a public offer is made in the Dominican Republic, then Dominican law, as per the terms of the Securities Law, will govern it.

Private equity as a financing method, from both local and foreign sources, is growing steadily.

Finally, considering how volatile the local currency is, foreign currency, mainly the US dollar, is used for any financing options.

6 Law of Agriculture Foment, Law No. 6188.
VII EMPLOYMENT LAW

Employment is governed by the Labour Code, which was enacted on 29 May 1992.

The relevant matters to consider in a merger transaction with regard to employees are labour contingency (severance), acquired rights and joint liability.

Dominican laws are very protective of employees’ rights, and the lawfully provided severance payment derived from the unilateral decision of an employer to terminate a labour contract can be quite high. Because of this, in some mergers, the labour contingency at the time of the merger is deducted from the price.

In accordance with Articles 76, 79, 80, 184, 203, 221 and 223 of the Labour Code, the severance payment and other benefits to be paid to an employee upon liquidation (when the employer unilaterally terminates a contract without justified cause) comprise:

- advance notice: this is the notice of termination of the contract. The number of days in advance on which an employee must be notified of the termination of his or her contract will vary depending on the length of time that the employee has worked for the company. If this period is one year or more of continuous work, the advance notice will be of 28 days. If the company fails to give this advance notice, then it must pay the employee 28 days’ salary;
- severance: the payment of an amount equal to 21 days’ salary for each year of service given;
- any outstanding wages;
- holidays, if the employees have not taken their holidays during the past year;
- a proportion of the Christmas salary, depending on the date of the termination; and
- a portion of the company’s profits in the past year, if applicable.

The severance amount to be paid, and any other benefits related to it, are made proportionally to the amount of time the employer has worked in the company, which means that until the labour contract is terminated and the employees are paid, the amount to be paid in connection with severance and employees’ acquired rights will increase over time.

On the other hand, the acquired rights of employees are those benefits given to them in addition to those lawfully provided for: for example, life insurance policies, petrol payments and funeral expenses. Any modification or elimination of the acquired rights of employees constitutes a breach of the terms of the labour contract, which entitles the employee to dismissal with just cause and triggers the severance compensation indicated above.

Finally, the third scenario (joint liability) refers to the shared responsibility that is created when a company, a branch or an agency thereof is transferred or assigned, or employees are transferred to other companies, including those rights and obligations of the employees that have been the subject of a lawsuit and are pending verdict, and in no case will void the acquired rights of the employees, whereby the new employer is jointly liable with the substituted employer for all the obligations resulting from the labour contracts or the law before the date of substitution.

In that vein, in an acquisition by share transfer, all the employees’ acquired rights must be preserved, because the company continues its operation without there being any change in

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7 This occurs, for example, when the employees of the company that ceases to exist work for the surviving or newly created entity.
the terms of employment. Likewise, in a merger by absorption, the surviving entity assumes all the labour liabilities of the company that ceases to exist; if a new company is created, it assumes the liabilities of the companies that cease to exist.

In an asset purchase acquisition where there is no transfer of employees, in principle there are no labour liabilities to consider. However, if an employee transfer takes place, or a company sells all its assets to another company and the first one terminates the labour employment with the employees who are then hired by the company that purchased the assets within a period of less than two months, it can be presumed that the seniority of the employee continues in the labour contract with the buying company, and as such the employee will have the legal remedies to oblige the companies to comply with Dominican law. Nonetheless, the severance payment paid by the company that sold the assets may be deducted from future severance payments made by the acquiring company to the employees.

VIII TAX LAW

The fiscal impact of a merger is covered mainly by the Tax Code, the Ruling for the application of Title II of Income Tax enacted by Decree No. 139-98 and Decree No. 408-10 of Business Reorganisation.

Prior to going through the merger process, and as per the terms of Article 94 of Decree No. 408-10, it is mandatory to inform the Tax Office of the intention to merge and request its approval to proceed with the merger.

Mergers, as stated in the above-cited three legal texts, are considered to be a form of reorganisation of companies, and as such the results that could arise as a consequence of the reorganisation are not taxed, and the rights and fiscal obligations that correspond to the entities that are reorganised will be transferred to the continuing entities. Notwithstanding, Article 287, Paragraph III of the Tax Code states that the losses that come from other entities as a result of a reorganisation process are not tax-deductible.

It is also important to note that the surviving entity in a merger, or the new entity created as a result of the merger, is liable for the obligations and taxes owed by its predecessor and for the penalties for the infringements of the companies that have ceased to exist, and it cannot oblige another entity to assume them.

On the other hand, acquisitions either by share transfer or by asset purchase are taxable transactions, with consequences for both parties (buyer and seller).

If a company decides to purchase the assets of an entity, to avoid acquiring the liabilities it would have to pay the corresponding taxes for all the assets, and the tax rate to be applied to the transfer would depend on the type of asset that is being transferred. The tax on the transfer of real property amounts to 3 per cent of the sale price of each property or of the value of the property registered in the records of the Tax Office, whichever is higher. The same principle applies to the transfer of vehicles, but the tax rate here is 2 per cent. In both scenarios, the tax described lies on the buyer.

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8 Even if the buyer does not acquire the shares of the business, in some scenarios the Dominican Tax Code holds him or her jointly liable (before the Tax Administration) for certain tax payments of the seller, such as those that affect the assets acquired, proportionally to the tax debt of the seller, and VAT taxes that are paid by the seller but collected by the buyer to be paid to the Tax Administration. In addition, if the buyer acquires what the Tax Administration defines as a permanent establishment, the Tax Administration could hold the buyer jointly liable for all the tax obligations of the contributor (seller).
For the seller, the corresponding taxes that arise out of a transaction are paid on the yearly income tax, and will be the difference between the acquisition price (adjusted by inflation) and the sale price if it is a real property. For other types of tangible assets, the seller will pay income tax on the difference between the book value of the asset and the sale price. In both cases (sales of real property and sales of tangible assets), the tax rate is 27 per cent.

The purchase price (except when transferring real property or shares) should also include 18 per cent VAT for the sale of assets (other than real estate) that must be reported, collected and paid by the seller.

With regard to the transfer of shares, it is the seller who bears the tax burden. In accordance with Article 289 of the Tax Code, capital gains tax, which applies currently at a rate of 27 per cent, applies to sales, swaps, and other allocation acts of capital assets such as share transfers, in which the applicable tax is calculated by deducting from the price or the value of the transfer of the shares the cost of its acquisition adjusted by inflation (as per the multiplying factor published yearly by the Tax Office).

Moreover, Norm 07-2014, issued by the Tax Office, allows the Tax Office to estimate a minimum transfer value (sale price), regardless of the transfer value that the parties agree to in the agreement (sale price), and it takes into consideration the equity of the company whose shares are being transferred by dividing the result of the values for the paid-in capital, admitted reserves, accumulated benefits or losses at the time of the sale, revalorisation of the company equity and the surplus from the number of shares transferred. With this reasoning, the Tax Office determines whether there has been a capital gain or loss.

Norm 07-2011 of the Tax Office also requires that any company that acquires shares withholds 1 per cent of the price paid to the seller for the purchase of the shares regardless of whether the seller is an individual, a legal entity, a resident or a foreign national. Said payment is credited to the tax on capital earnings that has to be paid by the seller, generated on the occasion of the sale, if applicable.

IX COMPETITION LAW

On 16 January 2008, the Dominican Republic enacted Law on the Defence of Competition. This Law prohibits the abuse of a dominant position and disloyal acts, such as agreements between competitors’ market players, and promotes free competition. However, it does not regulate the concentration of capital between the different players in a market.

Notwithstanding the above, several regulated markets require the authorisation of certain government dependencies, such as:

a Telecommunications: Law No. 153-98 and the Rules of Free and Loyal Competition of the Telecommunications Market require that any transfer, assignment, lease or grant of the right to use any title or lien granted on concessions or licences must be carried out with the previous authorisation of the Dominican Institute of Telecommunications (Indotel). In that vein, the sale or assignment of shares resulting in the loss by the seller or transferor of social control will require the authorisation of Indotel. Furthermore, mergers and market concentrations in telecommunications are expressly subject to the previous approval of Indotel, which can challenge a transaction or request and instruct correction measures in order for the transaction to be within the boundaries of the Law and the Rules.

9 Law on the Defence of Competition, Law No. 42-08.
Banking: the Monetary and Financial Law requires that the authorisation of the Monetary Board is acquired in advance, as per Articles 9 and 35 of the Law, in cases of mergers, share transfers of 30 per cent or more of the paid-in capital, absorption, and substantial asset and liabilities transfers of any financial intermediation entity. The authorisation of the Monetary Board is also required in advance for currency exchange institutions.

Securities: as per the terms of Articles 386 and 157 of the Companies Law, a corporation that had ventures in the securities market must submit the merger agreement to the Securities Superintendence, which will accept or reject the project within 15 days. The merger agreement is submitted for the approval of the bondholders’ meeting, unless the companies involved allow that the bondholders can be offered a refund as the sole requirement. Moreover, the Securities Law sets out several provisions to avoid concentration.

Insurance: Articles 174 to 184 of the Dominican Insurance and Bonds Law allow insurance and reinsurance companies to merge between each other with the previous authorisation of the Dominican Insurance Superintendence. The Superintendence can also recommend that an insurance company merges if the financial statements or the verifications made by the Superintendence reflect that the insurance company is not in a position to guarantee the fulfilment of its obligations before the insurers.

Electricity: Paragraph II of Article 12 of the Ruling for the Application of the Electricity General Law, enacted by Decree No. 555-02, states that the Electricity Superintendence, before authorising the transfer of generation concessions, mergers or sales of shares where generation companies are involved, must investigate whether the petitioners, either by themselves or through related parties, are owners of generation centres with a total capacity that represents, in its opinion, a significant percentage of the maximum demand of the national interconnected electric system that, in accordance with the criteria established by the National Commission of Energy, constitutes a threat to free competition in the electric wholesale market. Article 82 of the Law establishes a similar prohibition on the transfer of concessions of generation and distribution.

Pension funds: Article 93 of the Law of Social Security and Article 50 of Decree No. 969-02, which establishes the Pension Ruling, require that mergers are approved by the Pension Superintendence before completing matters of common law, and in that sense, a meeting approving a merger project together with the merger plan must be submitted. The Superintendence can require amendments to the merger project or reject it.

Health risk administrators: similarly to pension funds as described above, Article 153 of the Law of Social Security states that health risk administrators and the National Health Insurance Scheme must obtain the express authorisation of the Health and Labour Risks Superintendence before merging with another entity.

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10 Monetary and Financial Law, Law No. 183-02.
11 Dominican Insurance and Bonds Law, Law No. 146-02.
12 Ruling for the Application of the Electricity General Law, Law No. 125-01.
13 Law of Social Security, Law No. 87-01.
OUTLOOK

Significant modifications to the Labour Code and Civil Code are being discussed, which could affect certain aspects of M&A. However, it is not known when these modifications to the existing laws, and the enactment of new laws, will be approved by Congress, considering that some bills have been submitted for years.
Chapter 15

ECUADOR

Boanerges H Rodríguez Velásquez

I  OVERVIEW OF M&A ACTIVITY

During the past year, the Ecuadorian economy has changed course and begun attracting foreign direct investment (FDI); the FDI registered by the Central Bank of Ecuador in fiscal year 2018 totalled US$1.401 million, which reflects an increase of 126.5 per cent compared with the FDI received in 2017. During 2018, FDI was invested in the following industries:

a  mining (US$742 million);
b  services (US$187.3 million);
c  commerce (US$182.7 million);
d  manufacturing (US$103 million);
e  construction (US$86.8 million);
f  agriculture (US$59.3 million);
g  transportation; and
h  storage and communications (US$38.7 million).

The new government came into power in May 2017, and has been working on policies to improve FDI. At the end of December 2017, for example, the government defined the promotion of investments as a key state policy, for which President Lenin Moreno created, through Executive Decree 252, the Strategic Committee for the Promotion and Attraction of Investments.

On 2 April 2018, President Moreno presented the general outline of his economic plan, which consists of four main axes and 14 measures. The most important of these in relation to M&A are measures 6, 7 and 8, which are intended to grant income tax and foreign exchange tax benefits for new investments. The government will work on a new regulatory framework to encourage the financing of investment credits by international banks; this will undoubtedly help reactivate the local M&A market. The government will also seek to rationalise both the costs of stock transactions and the statute that holds the shareholders of a company responsible for the actions of its administrator, all as a means of strengthening the stock market. These measures will help strengthen the concept of limited liability in mercantile companies – a key concept that was harmed by the abusive application of the Organic Law for the Defence of Labour Rights, the negative impact of which was notorious in the stock market.

In March 2019, the Directory of the International Monetary Fund (IMF) approved a financing agreement with Ecuador of up to US$4,200 million. The agreement requires

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Ecuador to implement several legal amendments to its framework and change several policies, including, among other things, a reduction of the country’s overall foreign debt, a reduction of the public sector deficit, tax reforms, privatisations, returning its autonomy to the Central Bank and labour reforms.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Generally, an M&A transaction will be governed by the Civil Code (Private Law Rules), the Companies Law, the Organic Law of the Internal Tax Regime and its regulations and, when applicable, the Organic Law for the Regulation and Control of Market Power.

For M&A purposes, the Companies Law regulates the merger procedure. Pursuant to the Companies Law, there are two types of mergers: when two or more companies join to form a new one that acquires their rights and obligations (Article 347 of the Companies Law), commonly known as a merger; and when one or more companies are absorbed by an existing one, commonly known as a merger by absorption.

In a merger, tangible or intangible assets can be transferred at their book value or at their market value. The market value of the tangible and intangible assets is determined by a shareholders’ meeting, based on an independent appraisal.

Generally, a merger involves the following steps:

a) summons to the extraordinary general shareholders’ meetings for both the absorbed and the absorbing entities;
b) issuance of resolutions by the extraordinary general shareholders’ meetings regarding the merger of the company, in the case of the absorbing entity, and the dissolution, in the case of the absorbed entities. The shareholders approve the merger and the amendment of the by-laws;
c) filing the public deed of merger before the Superintendency of Companies, Securities and Insurance (SCSI), which will include the approved merger balance sheet;
d) an opposition period (six working days) starting with the publication of announcements for three consecutive days to allow for the opposition of any party that might consider itself affected by the dissolution;
e) registration of the SCSI’s merger approval resolution at the Mercantile Register and annotations with notaries;
f) other publications and actions related to the finalisation of the approved dissolution;
g) cancellation of the absorbed entity’s tax identification number and its registrations at other government agencies; and
h) other publications and actions related to the finalisation of the approved merger, including updating the information regarding the absorbing entity’s capital at the Internal Revenue Service and other government agencies.

The acquisition of an existing business can be sought through different contractual vehicles, but generally, these contracts will either agree to the acquisition of the shares (in the case of a corporation or public limited company) or share interests (in the case of a limited liability company); or the acquisition of business assets and liabilities.

These contracts will generally be governed by the Private Law Rules and, depending on the industry or sector, will add additional regulatory conditions as required by the relevant law.
i Acquisition of shares

If stocks are listed on the stock market, they can only be negotiated in the stock exchange through brokers. The only exceptions are transfers of shares made by virtue of mergers, demergers, inheritance, legacies, donations and liquidations of community properties or de facto business associations.

In general terms, unless a shareholder agreement is in place, a transfer of non-listed shares must comply with the Companies Law as follows:

a The assignee must receive the stock certificates that contain the shares being transferred, with the respective assignment signed by the assignor. The assignment notice can be delivered in a separate document attached to the stock certificate.

b Both assignor and assignee must inform the legal representative of the local company whose shares are being transferred about the respective share transfers by means of a joint communication signed by both or through separate communications.

c The legal representative of the local company must register the respective share transfers on the company’s shares and shareholder ledger.

d The local company’s legal representative must electronically notify the SCSI about the share transfers that have been carried out.

e The local company must issue new stock certificates at the request of the assignee. For that purpose, the stock certificates that are transferred shall be handed in for their annulment. The assignee can also choose not to request the issuance of new stock certificates and to keep the assigned stock certificates.

f Compliance with the applicable rules for the declaration and payment of income tax on the transfer of shares or participations.

g When Ecuadorian residents and effective Ecuadorian beneficiaries make direct or indirect disposals through non-resident companies, they must declare the income obtained, the expenses attributable to said income and the profits or losses produced by said operations.

h In the case of operations carried out by non-residents of Ecuador, it is the substitute’s obligation, namely the company whose shares are being negotiated, to declare and pay the income tax for the sale of shares.

i When a purchaser of shares or rights representing capital is a tax resident in Ecuador and at the same time a withholding agent, he or she is liable for withholding tax on the payment he or she makes.

j The lack of presentation of this information (or the presentation of erroneous data) is sanctioned with a fine of 5 per cent of the real value of the transaction.

The share participations issued by limited liability companies are not freely assignable or transferable as is the case for stocks issued by corporations. They can be transferred to another partner in the company or to third parties only with the unanimous consent of the partners. The transfer must be executed through a public deed and registered in the company’s ledger.

ii Acquisition of assets

The acquisition of business assets and liabilities may or may not generate the payment of various taxes. For example, if what is acquired is real property, the operation will be highly taxed by municipal and state taxes. On the other hand, if the operation only involves movable property and intellectual property rights, it will not be taxed.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

On 28 December 2017, the Organic Law for the Reactivation of the Economy was enacted, which includes certain measures to reactivate the economy. The Law amends the Companies Law and introduces the procedure for the transfer of the legal domicile of a foreign company to Ecuador; it also approves the validity of shareholders’ agreements, which establish conditions for a transfer of shares.

On 21 August 2018, the Law for Productive Promotion, Investments Attraction and Generation of Employment was enacted with the main purpose of making the economy dynamic, and promoting investment and employment as well as long-term fiscal sustainability.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Buyers in the process of acquiring companies in Ecuador are often subsidiaries of foreign companies. Many of the large transactions that take place in Ecuador are financed by the purchasers or by foreign banks; it is not common for local banks to be involved in M&A processes.

In the World Bank’s Doing Business 2019 publication, Ecuador is ranked as the 123rd country out of 190 economies as regards the ease of doing business. Foreign investors often struggle with bankruptcy proceedings, for instance, which can be complex and lengthy.

Players in markets such as the food, animal products, agricultural goods, banking and insurance, beer and beverage, and cement and steel-producing markets have been the main recipients of foreign investment through M&A transactions in recent past. During the past year, manufacturing was the sector that received the most foreign investment.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The most significant transactions during the past few years include the following:

a Nutreco Investments BV and Hendrux Genetics BV acquired 80 per cent of Macrobio SA, a laboratory dedicated to shrimp farming;

b Socofar SA, a subsidiary of Fomento Económico Mexicano, SAB de CV (FEMSA), acquired 100 per cent of one of the key players in the retail pharmaceutical business, Corporación Grupo Fybca SA GPF;

c Grupo Familia, through its subsidiary Productos Familia Sancela of Ecuador SA, acquired 100 per cent of Industrial Papelera Ecuatoriana SA for approximately US$36 million. This operation required the authorisation of the Superintendency of Market Power Control;

d Compañía de Petróleos de Chile Cope SA acquired the lubricants and fuels business of Exxon Mobil Ecuador through its subsidiary, Organización Terpel SA;

e Zurich Insurance Group signed an agreement with QBE Insurance Group Limited to acquire the operations of the latter in Argentina, Colombia, Ecuador, Brazil and Mexico for US$409 million;

f Nestlé SA acquired the majority of the social capital of Terrafertil;

g InRetail Perú Corp acquired the pharmaceutical distributor Quicorp SA for US$583 million;

h Heineken International BV acquired the majority of Biela y Bebidas del Ecuador SA, a company dedicated to the production of beer products, including key brand Biela;
i Dicomtriz SA acquired the Amazonas Gas Station for US$10,561,332 million; and
j on 24 August 2017, the sale of the production plant of Ambev Ecuador SA, a subsidiary of AB InBev, to the Ecuadorian consortium CEREC Holding Company SA was approved by the Superintendency of Market Power Control (SCPM) as part of the divestment process that AB InBev must complete for its global merger with SABMiller.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

M&A transactions are generally funded either by companies’ own funds when multinationals are involved, or international private banks and multilateral development banks, together with their private branches, such as IDB-Invest. The agreement with the IMF will encourage more foreign lenders to participate in these transactions.

VII EMPLOYMENT LAW

M&A transactions generate labour issues that must be addressed during negotiations. If a transaction is made through the purchase of shares, there is no change of employer and the working relationship is maintained with the employees; however, some legal scholars consider that Article 171 of the Labour Code is also applicable, and that employees have the option to terminate their contractual relationship as well; this is a much-debated subject. If, after the purchase, the buyer terminates the contracts of certain workers, the company is obliged to provide compensation in the form of severance payments.

On the other hand, if a transaction is made through the acquisition of assets or business units of a company, Article 171 of the Labour Code comes into effect, and the buyer must assume the responsibility of its predecessor as employer with respect to the workers at the business unit. Note that if a worker decides not to continue the employment relationship with the new employer, the employer must compensate him or her with a severance payment.

In merger processes, all labour contracts are maintained, and the absorbing company will be the new employer of the workers of the absorbed company. If two merging companies are liquidated and a new company is created, the new company will be the new employer of the workers of the two companies that have merged.

Generally, once an employment agreement is terminated unilaterally by the employer, a severance payment is due to the employees. The amount of the severance payment will depend on the last compensation and the seniority of each employee.

Another important aspect regarding employment legislation is that there are specific contractual modalities that apply for certain industries, such as banana production, tourism and floriculture.

The IMF agreement requires major amendments to the employment framework. There are ongoing talks regarding the depth of such amendments; however, it is expected that these amendments will make the current rigid labour regime more flexible.

VIII TAX LAW

Nearly all payments made by corporations and individuals are subject to withholdings on account of taxes. The payer is responsible for withholding the appropriate amount, providing tax withholding certificates to the payee, filing a report of withholdings and paying the amounts withheld within the following month. Payments made abroad – with some
exceptions, such as dividends and interests – are subject to withholding at a rate of 25 per cent pursuant to Article 39 of the Internal Tax Regime Law. For instance, royalties paid abroad are subject to a withholding of 25 per cent unless they are reduced under a tax treaty, or increased to 35 per cent if the recipient is in a tax haven or low-tax jurisdiction.

Dividends paid to a resident or non-resident corporation from another resident corporation out of profits that have been subject to corporate income tax are exempt, provided that the recipient does not reside in a low-tax jurisdiction or tax haven; otherwise, a withholding of 10 per cent has to be made.

Payments made abroad for interest on foreign loans registered at the Ecuadorian Central Bank (ECB) are tax-deductible, but are not subject either to income tax or to withholdings on account of taxes in Ecuador as long as that interest does not exceed the interest rate fixed by the board of directors of the ECB as of the date on which a loan was registered or registration was renewed. If the interest rate of the loan exceeds the ECB’s interest rate, a withholding of 25 per cent must be made on the excess.

Income (capital gains) generated by the direct or indirect transfer of shares is no longer tax-exempt, since the tax laws were amended in 2015. However, share transfers are exempt from VAT.

Transfers of assets and liabilities that take place as a result of a merger are exempt from income tax. The increase or reduction in the value of the shares that may take place as a consequence of a merger is also tax-exempt but not deductible. Any personal property transfer taking place as a result of a merger would not be subject to VAT. Likewise, the transfer of real property would not be subject to VAT or municipal taxes.

One tax implemented since 2008 that still discourages foreign investment is the overseas remittance tax. This is levied on the value of all monetary operations and transactions carried out towards any other country, with or without the intervention of institutions belonging to the financial system. The tax base is the amount of the currency transfer, or of the credit or deposit, or the amount of the cheque, wire transfer or draft abroad. The current tax rate is 5 per cent, and there are few exemptions.

In the past, Ecuador has not only imposed higher taxes on transactions involving persons located in tax havens, but in general it has been combating tax havens. One of the most recent examples, in February 2017, saw Ecuadorians vote to bar politicians and civil servants from having assets, company interests or capital in tax havens.

Ecuador has been part of the global trend towards greater tax transparency and the fight against tax evasion. In May 2017, Ecuador joined G20 countries, OECD members and other developing countries as a member of the Global Forum on Transparency and Exchange of Information for Tax Purposes. In May 2018, the Director of the Internal Revenue Service announced that Ecuador had become a party to the Convention on Mutual Administrative Assistance in Tax Matters. As a party to the Agreement, Ecuador will be able to exchange financial information with 117 countries.

Ecuador has concluded tax treaties with several countries (including Belgium, Canada, Chile, France, Germany, Mexico, Singapore and Spain) to avoid the double taxation of income.

Several tax incentives are set forth in the Production Code, the Organic Law for the Reactivation of the Economy, and the Law for Productive Promotion, Investments Attraction and Generation of Employment, all aimed at attracting both domestic and foreign investment in certain priority sectors (logistical services, biotechnology, tourism, forestry,
A five-year tax moratorium on corporate tax applies to new investments that comply with certain requirements and are located outside the main cities of Quito and Guayaquil. A tax exemption of 10 years applies for investments in some industries.

As previously stated before, the IMF agreement also requires major tax reforms. While none have been approved yet, the President has already announced the elimination of the green tax because it had not fulfilled its tax purpose.

IX  COMPETITION LAW

Starting from 13 October 2011, Ecuador’s competition regime was implemented through the enactment of the Organic Law for the Regulation and Control of Market Power (LORCPM). The SCPM is the entity in charge of overseeing compliance with the LORCPM.

The SCPM, as provided in the LORCPM and its regulations, has broad powers, including:

- investigating and imposing sanctions related to antitrust matters and violations, restrictive practices and market power abuse;
- approving conditioning or rejecting economic concentrations (mergers); and
- investigating and imposing sanctions related to unfair trade practices.

Operations of economic concentration are those operations that have the potential to affect the structure of a market by limiting the number of competitors or the means of production.

i  General legal regime applicable to mergers

The LORCPM determines that operations of economic concentration include but are not limited to the following:

- mergers;
- full transfers of the assets of a merchant;
- the direct or indirect acquisition of the property or of any other right over the shares or interests in the capital or securities that grant any type of right to be converted into shares or interests in the capital, or to have any type of influence in the decisions of the person that issues them, when such acquisition grants to the acquiring party the control of or a substantial influence over that person;
- economic concentrations through the appointment of common managers or directors; and
- any other agreement or act that transfers to a person or to an economic group the assets of an economic operator, or that grants such person or economic group decisive control or influence in the adoption of the decisions of the ordinary or extraordinary management of an economic operator.

ii  Thresholds and conditions

Certain operations of economic concentration require prior approval from the SCPM before taking effect. Prior approval is required in the following cases:

- when the total business volume in Ecuador of all the transaction participants, considered jointly, in the previous fiscal year of operation exceeds the amount of unified basic remunerations (RBU) set forth by the Regulating Board as follows:
  - for operations involving financial institutions and stock market entities, 3.2 million RBU, which in 2019 represent US$1.260 million;
ii for operations involving insurance and reinsurance companies, 214,000 RBU, which in 2019 represent US$84,3 million; and

iii for operations involving economic operations not included in (i) and (ii), 200,000 basic unified salaries (US$78,8 million); and

b when a transaction involves economic operators with a combined market share of 30 per cent or above in the relevant market of products or services.

If the conditions described above are not met by the parties to a transaction, or by the transaction itself, no prior approval by the SCPM is necessary. Nevertheless, the SCPM, may, *ex officio* or at the request of an interested third party, review the transaction.

Depending on the markets in which the M&A transaction is taking place, the approval of specific regulatory agencies (such as the Superintendency of Companies, the Superintendency of Banks, the Hydrocarbons Regulatory and Control Agency, the Mining Regulation and Control Agency, the Telecommunications Regulatory and Control Agency) must be obtained.

As previously indicated, the enactment of the LORCPM has completely changed the landscape in Ecuador with respect to large M&A transactions. The need for regulatory approval under many circumstances has increased both the time and cost of closing transactions of economic significance. In addition, a perceived sense of unpredictability that clearance will be granted will remain until there has been sufficient and consistent practice by the regulator.

Violations of the Antitrust Law are severely penalised. Monetary fines range from 8 to 12 per cent of the turnover in the fiscal year previous to the one when an infraction is determined. There are also substantial monetary fines for the legal representatives, directors and officers of a company involved in an infraction.

During 2018, the SCPM investigated 31 cases, 24 of which were opened during the course of the year and seven of which were originally opened in 2017. Of the 24 cases opened during 2018, 15 ended with an authorisation of the transaction without any type of remedies.

**X OUTLOOK**

The following, among other measures, will undoubtedly contribute to an increase in M&A activity in the next few years in Ecuador:

a the Organic Law for the Reactivation of the Economy, the Law for Productive Promotion, Investments Attraction and Generation of Employment, and the IMF agreement, the laws that are expected to be sent to the National Assembly to attract FDI;

b the government’s economic plan;

c the campaign announced by the Minister of Foreign Trade and Investment to make Ecuador a new investment destination; and

d the liberalisation of air transport.

The strengthening of the principle of limited liability will undoubtedly be an incentive for both local and foreign investors, as will be the guarantee of the continued dollarisation of the economy, which is perceived to bring much-needed stability for long-term investment.

We also expect that the labour and tax reforms required by the IMF agreement will also pave the way for more M&A transactions in Ecuador.
Chapter 16

EGYPT

Omar S Bassiouny and Maha El-Meihy

I OVERVIEW OF M&A ACTIVITY

Egypt’s M&A value increased by 285.6 per cent, reaching US$1.5 billion in 2018 compared to US$389 million in 2017.²

M&A deal value grew due to increased interest by foreign investors in the energy, mining, education and utilities sectors. Landmark M&A transactions in 2018 included Mubadala’s US$935 million and Rosneft US$1 billion acquisition of parts of the Zohr oilfield from Eni, Dr Oetker’s acquisition of Tag Al Melouk and Soco International’s acquisition of Merlon Petroleum El Fayoum Company.

Egypt’s share of M&A deals in the Middle East and North Africa region has increased to 6.3 per cent in 2018, compared to 2.5 per cent in 2017.³

For the past 12 months, the Egyptian market and international investors have been monitoring the progress of the implementation of the government’s economic and social development plan in light of the US$12 billion Egypt–International Monetary Fund (IMF) loan agreement, which was associated with a number of important measures including changes in the deposit and lending interest rate announced by the Central Bank of Egypt (CBE) and, most importantly, the removal of all FX controls and the free flotation of the Egyptian pound, which was followed by a severe currency devaluation. The severe devaluation of the pound saw Egyptian assets and securities lose more than 50 per cent of their value and, in conjunction with the positive performance of the government insofar as the IMF loan programme is concerned, as publicly noted by the IMF, had a major positive impact on M&A activity in Egypt.

The CBE has modernised its monetary policy framework, focusing on inflation under a flexible exchange rate regime. Its monetary policy stance has been appropriately calibrated, helping to reduce inflation from 33 per cent in July 2017 to 13 per cent in April 2019 despite occasional supply-side shocks and excessive volatility in some food prices.⁴

Overall, 2018 was a progressive year for M&A in Egypt. Private equity, investment managers and financial institutions become more active in terms of the number of deals and their value. M&A transactions were closed in several sectors including:

a media;

b education;

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c oil and gas downstream;
d petrochemicals;
e telecommunications;
f renewable and traditional energy;
g manufacturing;
h food processing;
i education;
j fintech; and
k healthcare.\(^5\)

In 2019, M&A is likely to continue in the same positive manner in the Egyptian market, and to rank third in terms of combined value in the region, whereby M&A business is expected to reach US$1.372 billion in 2019, while trans-border M&A are likely to stand at US$2.93 billion and rise to US$3.14 billion in 2020.\(^6\)

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Egyptian legal system is a civil law system, which is influenced mainly by Islamic shariah and the French civil code. Hence, it is based on written legislation, rather than depending on judicial precedents as in common law countries. That said, the Egyptian Civil Code\(^7\) plays an prominent role in the legal framework since it governs and regulates all the general principles pertaining to contract law, including but not limited to all types of sale and purchase transactions. In other words, in the case of M&A transactions governed by Egyptian law, the Civil Code is one of the main pillars regulating such transactions.

In addition to the general rules stipulated under the Civil Code, M&A transactions are regulated in Egypt by diverse specific legislation depending on whether a transaction is public or private.

Key rules pertaining to M&A can be particularly found under the Egyptian Companies Law\(^8\) and its Executive Regulations, as amended, the Capital Market Law\(^9\) and its Executive Regulations, as amended, and the Egyptian Exchange Listing Rules, as amended.\(^10\)

Furthermore, decisions and decrees issued by the following concerned key regulatory authorities constitute an integral part of the regulatory framework: the Egyptian Stock Exchange (EGX), the Financial Regulatory Authority (FRA) and the General Authority for Investment and Free Zones.

Subject to the specific activity of a target company, other regulatory bodies might be involved such as the CBE and various key ministries.

As a general rule, acquisitions involving transfer of title of shares of joint-stock companies and quotas of limited liability companies are the most common acquisition structures in Egypt. The transfer of unlisted shares is conducted over the counter (OTC) through an accredited broker registered with the EGX and appointed for such purpose.

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\(^7\) No. 131 of 1948.

\(^8\) No. 159 of 1981.


\(^10\) The Board of Directors of the Financial Regulatory Authority Decree No. 11 of 2014.
OTC transactions are not subject to the same level of regulation as public transactions. Any transaction exceeding 20 million Egyptian pounds must be, inter alia, pre-approved by each of the EGX Pricing Committee, which convenes on a weekly basis to study and resolve on each envisaged transaction; and the FRA.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

2018 witnessed several legislative amendments that have impacted the M&A market, including an increase of the mandatory tender offer trigger from 2 to 5 per cent in the shareholding of a public company. Further, the FRA introduced numerous specific regulations regarding the acquisition of notable stakes in financial services companies.

The legislative amendments that have impacted the M&A market include an amendment of the Companies Law in relation to shareholders’ agreements and preferred shares.

i Shareholders’ agreements

Legal provisions exist to govern the concept of the shareholders’ agreement. Shareholders’ agreements are typically concluded between the founders and shareholders of a company in order to organise the relationship between the partners that are not contained in the articles of association that is ratified by the General Authority for Investments and Free Zones on a designated form. Although there is no legal requirement to conclude agreements between sellers, buyers and target companies for share acquisitions, it is however customary in large acquisitions that parties conclude transaction agreements such as share purchase agreements and shareholders’ agreements, as long as such shareholders’ agreements do not include any contractual restrictions on the free tradability of the listed shares, since otherwise the same would be null and void.

Egyptian law does not explicitly regulate or recognise the concept of the drag-along right. There are no publicly available Court of Cassation judgements addressing the validity or enforceability of drag-along or similar rights. In addition, in practice, the General Authority for Investments and Free Zones does not accept the inclusion of drag-along right provisions in a company’s articles of association. Accordingly, drag-along right provisions fall under the scope of application of the general provisions of the Civil Code and the Executive Regulations of the Companies Law, and qualify as a conditional contractual obligation. Hence, the drag-along right is valid under Egyptian law since the fundamental conditions that trigger the drag-along right (i.e., a third-party bone fide purchaser wishing to acquire a majority or all of the capital of a target) do not conflict with the Civil Code. However, its enforceability remains untested.

It is worth noting that the same is applicable to put option provisions. Accordingly, put option provisions fall under the scope of application of the general provisions of the Civil Code and the Executive Regulations of the Companies Law and arguably qualifies as a promise to contract.

In light of the foregoing, the introduction of a regulated shareholders’ agreement will give parties to M&A transactions further comfort, since rights such as drag-along rights and put option rights will be incorporated into such shareholders’ agreement.
ii Preferred shares

In the past, a company was not allowed to issue preferred shares unless its by-laws contained a provision allowing that at incorporation. In this respect, the new amendments to the Companies Law allow companies to issue preferred shares, even if such was not provided for in their by-laws at incorporation, so long as an extraordinary general assembly of such company vote representing three-quarters of the company’s capital is obtained. At the outset, preferred shares were assumed to be incorporated with no limitations. However, shortly after the issuance of the new amendment of the Companies Law, GAFI issued a circular to limit the voting powers of holders of preferred shares to be capped at two to one. Preferred shares are advantageous for parties who wish to enjoy more voting and financial rights and contribute with the same capital, as opposed to ordinary shareholders.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Investing in Egypt was subject to a period of instability following the 2011 and 2013 revolutions. Although the devaluation of the Egyptian pound against the United States dollar in 2016 should have increased foreign investment into the country, political instability throughout the Middle East and North Africa have had a greater negative influence. Another problem that slowed down foreign direct investment was the high level of bureaucracy. However, several steps have been taken to enhance public service delivery and the domestic investment environment, and to re-attract significant foreign direct investment inflows.¹¹

Egypt was one of the African countries that received some of the largest amounts of foreign direct investment inflows in 2018. According to the Central Bank of Egypt, foreign direct investment inflows increased to US$10.2 billion, while outflows stood at US$4.2 billion, which led to an increase of net foreign direct investment inflows to US$6 billion between July 2017 and March 2018. In parallel, total foreign investment reached US$14.9 billion due to portfolio investments. Further, the discovery of the largest gas reserves in the Mediterranean Sea, first in the country’s western desert and then in the Zohr offshore field, has positively affected inflows into Egypt. As a result, Egypt saw around 1.6 per cent of growth in inflows in relation to the oil industry in less than a year.

Foreign investments mainly come from countries with which Egypt has signed a bilateral treaty, including EU and Arab countries, and the United States. Notwithstanding this, the United Kingdom remains by far the largest investor in Egypt. Such direct investments mainly target the oil sector, followed by the construction, manufacturing, real estate and financial services sectors.

The countries that have been key players in M&A deals in Egypt include the United Arab Emirates, which currently enjoys very strong diplomatic and economic ties with Egypt; a large number of UAE public and private companies have been consolidating their presence in the Egyptian market via M&A.

Egypt is a party to more than 100 bilateral investment agreements with, inter alia, the majority of the European Union Member States, the United States, and some African, Middle Eastern and Asian countries. In addition, Egypt signed an agreement with the Mercosur bloc of Latin American nations in 2010.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

Regional, international and local private equity and financial institutions are empowering the Egyptian economy. The renewable energy sector, and consumer-focused sectors such as food and drink, healthcare and education, have been the most active sectors.

The past year witnessed the acquisition by Mubadala Petroleum of a 10 per cent stake in the Shorouk concession in Egypt’s Zohr gas field for US$934 million as well as SOCO International’s acquisition of Merlon Petroleum El Fayum Company.

Further notable transactions were:

- EFG Hermes’ acquisition of a Cairo-based elementary schools’ portfolio from Talaat Moustafa Group Holding, Egypt’s largest listed real estate developer, for 1 billion Egyptian pounds;
- Tag El Melouk (a market leader in the production of baking powder, vanilla and salt, among other products) selling 100 per cent of its shares to Dr Oetker; and
- Solvay Alexandria Sodium Carbonate (CCI) selling 100 per cent of its shares to three state-owned companies in a US$15 million buyout of CCI by state-owned companies Egyptian Ethylene and Derivatives Company, Sidi Kerir Petrochemicals Company and the Egyptian petrochemicals holding company, ECHEM.12

While 2019 will be more focused on government IPOs, the first two quarters of 2019 witnessed some notable transactions.

Bank Audi announced through its acquisition to the National Bank of Greece in Egypt (NBG). This acquisition included a book of ‘mostly of Egyptian-risk loans, deposits and securities (total assets of around €110 million), a branch network of 17 branches and c.a. 250 employees’. The exit of NBG from the Egyptian market is in accordance with a wider restricting plan for reducing its overseas presence.

Cleopatra Hospital Group has also acquired the real estate assets of El Katib Hospital, and is currently finalising the business transfer agreement. El Katib Hospital is expected to add around 100 beds to the existing capacity and introduce of a new urology centre of excellence.

New challenges have been seen due to a more difficult external environment, given the constricted global financial conditions. Egypt has successfully weathered recent capital outflows. Nevertheless, further strengthening of the policy buffers, including by containing inflation, enhancing the exchange rate’s flexibility and reducing the public debt will all be essential.13

According to CBE monthly inflation developments, the nationwide annual inflation declined to 12.5 per cent in April 2019 as the rural annual inflation declined to 11.9 per cent, from 13.8 and 13.4 per cent in March 2019, respectively.14

According to the IMF review, the continued reinforcement of tourism and construction, and the rising production of natural gas are expected to increase GDP growth to 6 per cent due to the ongoing implementation of structural reforms, and should translate into stronger private investment. Inflation is expected to reach single digits in 2020. The current account

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13 IMF, ‘Arab Republic of Egypt: Fourth Review Under the Extended Arrangement Under the Extended Fund Facility—Press Release; Staff Report; and Statement by the Executive Director for the Arab Republic of Egypt’.
14 https://www.cbe.org.eg/en/MonetaryPolicy/MonthlyInflationNoteDL/IN_April%202019_EN.PDF.
deficit is projected to gradually narrow from 2.4 per cent of GDP in 2017 and 2018 to under 2 per cent of GDP in the medium term, and general government gross debt is expected to continue to decline to 74 per cent of GDP by 2022 or 2023.¹⁵

In parallel, the significant investment liberation measures that are currently being undertaken by the government – by way of example, the introduction of a new law for the setting up of a natural gas regulatory authority charged with licensing – aims at opening the gas market to competition.

Furthermore, the issuance of the New Industrial Law¹⁶ has made the establishment of manufacturing facilities easier through the introduction of a one-stop shop mechanism as an addition to the current practice of the General Authority for Investment and Free Zone, under which the same concept is applied to establishing companies. These have encouraged local investors to establish companies or manufacturing facilities, or to expand their existing facilities, without being concerned about regularising the status of such facilities.

The free float of the Egyptian pound has affected inbound foreign investments through the contributions of non-residents’ purchases into real estate, and the net purchase by non-residents of companies and assets. Although purchases by non-residents have increased foreign direct investment into real estate, the real estate sector is still mostly being affected because of the increase in price of all the raw materials involved, which has affected costs and purchase prices, leading to stagnation.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

M&A are typically financed through equity, third-party financing, which includes credit financing, or a combination of equity and financing. Buyers tend to provide sellers with a warranty, or documentary evidence, or both, confirming the availability of the acquisition financing. Typically, the payment of the purchase price is a condition precedent to a transfer of shares. Hence, if finance is not available, a transaction will never be closed.

There are no typical seller’s assistance obligations. However, there are some regulatory restrictions under Egyptian law that could impact the financing structure, including the CBE regulatory instituted limitations and regulatory framework regulating acquisition financing; and financial assistance rules that under Egyptian law restrict a company from lending or guaranteeing the obligations of any of its board members.

Furthermore, in the case of a mandatory tender offer, a proposal submitted to the FRA must include a confirmation from a licensed bank in Egypt evidencing the availability of the financial resources to fund and cover an offer. Accordingly, short of a financial solvency confirmation, the FRA should not accept an offer proposal.

Subject to the parties’ commercial agreement, financing may be structured as a condition (among other conditions) in asset-based transactions, where the transaction documents may reflect procurement of financing as a condition as supported by guarantees, warranties and the provision of evidence confirming the availability of financing.

It is, however, not customary to enshrine a seller’s obligations to assist in relation to a buyer’s financing in the transaction documents.

¹⁵ See footnote 9.
¹⁶ No. 15 of 2017.
Private equity, investment managers and financial institutions recently become more active in terms of the number of deals and their value. 2018 witnessed a deal flow of 30 per cent in favour of strategic investors and 70 per cent for private equity firms. Hence, private equity firms still dominate the private M&A scene in the Egyptian market.

VII EMPLOYMENT LAW

The relationship between employers and employees is governed by the Egyptian Labour Law and decrees of the Ministry of Manpower. Generally, the Employment Law favours and protects employees as supported by several court precedents issued in favour of employees. Although Egyptian law does not oblige employers to obtain approval of or consult employees during an acquisition process, the law has still restricted an employer’s ability to make changes to the workforce during this process. In an acquisition, employees’ rights (including their acquired rights) remain protected and may not be discretionally limited or changed by the employer. Employees’ dismissals take place by virtue of court orders and are limited to specific major events. Further, any redundancies during acquisitions must take place in coordination with the Ministry of Manpower and subject to its approval.

The Labour Law obliges buyers to have all the employees of the seller remain with the target company or transfer to the buyer in the case of an asset deal. The application of such transfer varies whether an acquisition is for assets or shares. In a share transfer, employees do not transfer, since they remain with the target company; hence, an acquisition of shares does not involve an employee transfer process.

In an asset sale, pursuant to the Labour Law, in the event an establishment is transferred from one employer to another, employees of the transferred establishment are transferred automatically to the new employer. Both the former and new employers will be jointly liable for the fulfilment of their entire obligations as set out under the employees’ employment contracts. Article 9, Paragraph 2 of the Labour Law states the following:

> merging the establishment with another or transferring it by inheritance, bequeath, donation, or sale – even by public auction – or by assigning or leasing it or other such disposing actions shall not terminate the employment contracts of the existing employees. The successor employer shall be responsible jointly with the former employers for implementing all obligations arising from these contracts.\(^{18}\)

Based on Article 9, the Labour Law neither defines an asset sale nor sets out parameters to include a sale of business, whether in whole or partial. Hence, some sellers tend not to apply the conservative approach and have employees transferred. Although the Labour Law recognises the concept of employees’ automatic transfer in the event of an asset sale, practically the transfer of employees cannot automatically be implemented before the Social Insurance Authority due to bureaucracy.

That said, it should be also noted that in transfer of assets constituting a business, employees’ and tax-related liabilities will remain shared, from a statutory standpoint, by both the purchaser and the seller. A new labour law has been discussed in the Parliament since

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\(^{17}\) No. 12 of 2003.


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2017, and the draft of that law has kept a provision to the same effect. Other provisions that are irrelevant to the M&A have been either amended or introduced to grant employees more benefits (e.g., four months of maternity leave instead of three months\(^\text{19}\)).\(^\text{20}\)

**VIII TAX LAW**

Taxation in Egypt is governed by a number of pieces of legislation mainly comprising the Income Tax Law\(^\text{21}\) and the Value Added Tax Law.\(^\text{22}\)

Recently, capital gains realised from the sale of listed Egyptian shares by both resident and non-resident shareholders have been taxable at a rate of 10 per cent.\(^\text{23}\) For listed securities, the application of this tax was suspended for two years as of 17 May 2015. Such suspension was extended for an additional period of three years that ends on 16 May 2020. Accordingly, no capital gains tax shall be collected or withheld before 17 May 2020 with respect to shares listed on the EGX.

On the other hand, the sale of unlisted Egyptian shares by both resident and non-resident shareholders is subject to capital gains tax at a rate of 22.5 per cent on the gain realised.

Another applicable tax on sales of securities, whether listed or unlisted, is the newly introduced stamp duty tax whereby the purchase and sale of shares representing less than 33 per cent of a company’s issued capital (during a consecutive period of two years) up to 31 May 2019 was subject to stamp duty at a rate of 0.3 per cent of the total consideration, while as of 1 June 2019 the rate increased to 0.35 per cent. As per the Stamp Duty Law,\(^\text{24}\) stamp duty should be borne equally by the seller and the buyer. If the transferred shares represent 33 per cent or more of a company’s issued share capital (as bulk in one transaction), the buyer shall pay stamp duty at a rate of 0.3 per cent and the seller shall also pay 0.3 per cent.

Further, although value added tax may seem irrelevant to M&A activities, its application is crystallised in the acquisition of assets – in the context of asset deals rather than stock deals – since a sale of assets is subject to value added tax at different rates according to the sold assets.

Further, Article 107 of the Income Tax Law stipulates that if the Tax Authority finds that the rights of the public treasury are liable to be lost, the President of the Authority may request the competent summary matters judge to issue a warrant on petition for levying an attachment on the funds or assets deemed adequate for collecting rights that may be lost, whatever the holders of such funds.

Additionally, as per Article 1139 of the Civil Code, sums due to the state treasury for taxes, duties and any other dues are privileged in accordance with the conditions laid down by the laws and regulations issued in this connection. These sums shall be paid out of the proceeds of the sale of a property charged with this privilege, in whosever’s hand they may be, and before all other rights, whether privileged by a lien or secured by a mortgage, except the costs of legal proceedings.

\(\text{19}\) Article 91 of the Labour Law.
\(\text{20}\) https://drive.google.com/file/d/0B7TbC7kyvm9KVThUU1Jva09NZTA/view.
\(\text{21}\) No. 91 of 2005.
\(\text{22}\) No. 67 of 2016.
\(\text{23}\) Article 46 bis 5 of the Income Tax Law.
\(\text{24}\) No. 11 of 1980.
By virtue of the above, the Tax Authority the right to trace the assets of a target in whosoever’s hands they may be to satisfy any sums due on the target to the state treasury, even if those assets have been transferred to, and are now owned by, the target. Although the privileged right of the Tax Authority is deemed to be a general privileged right that shall not entail, as a rule, tracing rights, this specific privileged right of the Tax Authority exceptionally entails the latter’s right to trace the assets of the target, in whosoever’s hands they may be, as indicated in above-mentioned provisions.

Further to the above, it should be additionally noted that the Tax Authority may have another legal basis for claiming the amount of taxes due on any target from any purchaser jointly with the target if a transfer of assets is considered to be a transfer of the target’s business.25

Recently, there have been studies and recommendations to improve the current tax regime through, among other things:

a. the presence of a progressive tax, which shall be in accordance with social justice and eliminate the burden on people with limited incomes;

b. incentivising taxpayers that delay paying their taxes, thereby expediting the process of receiving tax and increasing Egypt’s financial sources;

c. imposing a tax on inheritance; and

d. imposing a tax on net wealth, which shall be paid only one time.26

IX  COMPETITION LAW

In 2018, the Egyptian Competition Authority (ECA) began adopting a new approach in its interpretation of the Competition Protection Law and its Executive Regulations that has materially impacted M&A transactions. The ECA, via its novel interpretation of the law, deems that M&A transactions between dominant companies (defined as companies that control over 25 per cent of a specific market) must obtain the prior approval of the ECA prior to concluding a transaction, even if the transaction is concluded offshore. On the legislative front, the ECA is trying to introduce an amendment to the Competition Protection Law in Parliament to give it greater power in controlling mergers, and explicitly legalising its above-mentioned new approach and interpretation.

In that context, the ECA regards the potential merger between Uber and Careem (two of the biggest ride hailing app transportation companies) to be a horizontal agreement, which as such violates Article 6(a) and (d) of the Competition Law.27 In this regard, the ECA issued decision No. 26 of 2018 on 23 October 2018. This decision obliges the two companies and their related parties, including the companies participating in their shareholding, to obtain the ECA’s pre-approval prior to concluding any agreement related to the merger, establishing joint ventures, or the purchase or sale of shares or assets of either company, either directly or indirectly.

Based on the above, if the buyer is a competitor of the seller, whereby both will have a significant share covering almost the whole market, the prior approval of the transaction by the ECA will be required. Otherwise, failure to procure approval will be subject to the penalty

25 Article 80 (3) of the Egyptian Income Tax.
27 Law No. 3 of 2005.
stipulated in Article (22) of the Competition Law: each party to the horizontal agreement shall be punished by a fine ranging between 2 and 12 per cent of the total revenue of said party that was generated from trading the product or products that are the subject of the horizontal agreement during the violation period. In the event the competent court is unable to determine the aforementioned revenue, each party shall be punished by a fine amounting to no less than 500,000 Egyptian pounds and not exceeding 500 million Egyptian pounds. Such fines will be doubled in the case of recurrence.

The Cabinet and the President have recently approved draft amendments to the Competition Law, including a provision by virtue of which the penalty for failure to serve post-closing notifications upon acquiring, inter alia, assets, usufruct rights, shares or the joint management of two or more parties in the event that the combined annual turnover of the concerned parties in Egypt exceeds 100 million Egyptian pounds) according to their latest financial statements, will be calculated on a daily basis and until the required notification is made. However, such amendments have not yet entered into force.

X OUTLOOK

Considering that Egypt achieved an economic GDP growth rate of 5.5 per cent for the second half of 2018 (the highest growth in the Middle East according to the IMF), implemented the vast majority of the medium-term reform plan agreed upon with the IMF, stabilised the Egyptian pound foreign exchange rate, secured the relative availability of foreign currency within banking channels and realised a notable increase in the forex reserves at the Central Bank, a large number of analysers and practitioners remain optimistic insofar as foreign direct investment and M&A activity are concerned.

In an attempt to reduce Egypt’s increasingly large foreign currency debt (which is close to US$100 billion), a wave of privatisations of public sector assets, including power stations, financial institutions and infrastructure, is expected, whether in the form of direct sales or flotations on the stock exchange.

It is also envisaged that further reforms in connection with the regulatory framework for antitrust will take place, and it is expected that these will strengthen the role of the regulator. The sectors that will see the vast majority of M&A transactions in the coming 12 months include:

- renewable energy;
- oil and gas;
- petrochemicals;
- education;
- food processing;
- financial services;
- telecommunications;
- real estate; and
- with a population of just over 100 million, sectors that will be impacted by Egypt’s demographic power and potential.

All of the above evidence Egypt’s commitment to a strong investment environment.\(^{28}\)

I OVERVIEW OF M&A ACTIVITY

Building on a solid performance in 2017, the Finnish M&A market had a very strong year in 2018, reaching a level close to the peak seen in 2006 and 2007 prior to the 2008 financial crisis, both in terms of the number of deals and deal value. The second half of 2018, with 101 announced deals according to data compiled by Mergermarket, showed strong growth compared to the 69 deals announced in the second half of 2017. The aggregate disclosed deal value for announced acquisitions of Finnish targets was approximately €9.3 billion in the second half of 2018 (second half of 2017: €5.8 billion), including the largest ever tender offer for a Finnish company, namely the €5.6 billion offer for Amer Sports Oyj, the Finnish sporting goods company, by a consortium led by Chinese ANTA Sports Products Limited.

Strong growth in the Finnish economy, following a sustained period of low and even negative growth, continued to support optimism in the Finnish M&A market. The availability of financing remained relatively good.

However, there have been signs of a market slowdown in the first half of 2019, with 66 deals announced. The aggregate disclosed deal value for announced acquisitions of Finnish targets was approximately €3.7 billion in the first half of 2019, compared to €2.8 billion in the first half of 2018, attributable mainly to Telenor’s €3.1 billion acquisition of DNA Plc, the Finnish telecom operator, announced in April 2019. There is uncertainty as to whether the market will regain momentum or whether the slowdown will be more persistent, linking to general concerns about slowing growth in the Finnish economy.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Finnish legal system derives from the Nordic legal tradition, which itself is based on the German civil law tradition. Historically, agreements have been relatively brief, leaving room for interpretation in accordance with contract law principles and market practice. However, during the past few decades, agreements (and in particular acquisition agreements) have become more detailed and have started to resemble Anglo-American acquisition agreements.

The manner of carrying out a takeover of a Finnish company depends primarily on its ownership structure and whether the company’s shares are listed or unlisted.

The ownership of most Finnish private companies is concentrated. Even in many listed companies, the majority of shares are held by a relatively small group of shareholders.

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1 Jan Ollila is senior partner, Wilhelm Eklund is a partner and Jasper Kuhlefelt is a senior associate at Dittmar & Indrenius.
Therefore, negotiations with the majority shareholders are often important in both public and private takeovers, and irrevocable undertakings from major shareholders may be decisive for the success of a public offer.

The legal framework applicable to public takeovers varies considerably from the regulation of private transactions. Contrary to private deals, takeovers of listed companies are subject to fairly detailed rules.

Regulation of Finnish public takeovers essentially consists of the rules applicable to public takeovers included in Chapter 11 of the Securities Markets Act (SMA), regulations and guidelines on takeover bids and the obligation to launch a bid (Regulation 9/2013) issued by the Finnish Financial Supervision Authority (FSA), which entered into force on 1 July 2013 and replaced the FSA Standard 5.2c, as well as the revised Helsinki Takeover Code issued by the Takeover Board of the Securities Market Association, which entered into force on 1 January 2014 and replaced the Takeover Code of 2006. The current SMA entered into force at the beginning of 2013.

Chapter 11 of the SMA sets out, inter alia, the general requirement to treat holders of each class of securities subject to the offer equally, the general structure of the offer procedures, rules on publication of an offer and disclosure obligations, the requirement to make a mandatory offer, pricing of offers and rules on competing offers.

There is a dual mandatory offer threshold, which is exceeded when the bidder, and its affiliated parties, obtains more than 30 or more than 50 per cent of the voting rights in the target. No mandatory offer will be required if the relevant thresholds are exceeded as a result of a voluntary offer made for all shares and securities entitling to shares in the target.

Public offers are monitored by the FSA, which is authorised to interpret the relevant statutory provisions and issue regulations and guidelines. Regulation 9/2013 supplements the statutory rules and sets forth the FSA’s interpretation of the relevant provisions of the SMA. Regulation 9/2013 contains more detailed rules on matters such as the takeover procedure, disclosure obligations and pricing.

Furthermore, the rules and regulations of NASDAQ OMX Helsinki regulate, inter alia, the trading in securities in connection with public transactions.

If a consideration consists of securities, the rules of the SMA relating to public offerings and the listing of securities may also become applicable. Under the EU prospectus regime, an EU listing prospectus may be used in exchange offers in Finland if the consideration consists of securities listed in Finland or in another EU Member State. In such cases, the offer document will also have to comply with the EU prospectus regime.

Another source of law is the Companies Act, which sets out general principles of company law and provides the regulatory framework for corporate reorganisations and squeeze-outs.

Under the Companies Act, a squeeze-out procedure can be initiated by a shareholder holding, either directly or indirectly through a group company, more than 90 per cent of the shares and votes of a company. A shareholder whose shares can be redeemed also has a right to require that the majority shareholder redeems that shareholder’s shares.

The redemption price in a squeeze-out is the fair price. If the 90 per cent threshold is exceeded as a result of a voluntary or mandatory public offer, the offer price is regarded as the fair price unless there are special reasons for deviation from that price. If the bidder intends to exercise the squeeze-out right upon reaching the legal threshold through a tender offer,
that intention should be disclosed in the offer document. The squeeze-out is effected through arbitration proceedings, which are usually initiated by the majority shareholder against all other shareholders.

Whereas the takeover of a listed company follows a rather rigid statutory procedure, the acquisition of a private company can be structured more freely.

With regard to private transactions in particular, there are few processes involving notaries and government officials. As a result, few formal requirements exist concerning documentation governing the transfer of a business regardless of whether it is transferred through an asset or a share deal.

Regarding defensive actions, the board of a target company has a general obligation under Finnish company law to act in the interests of the target company, with particular regard to the interests of the shareholders. In line with this general obligation, Chapter 11 of the SMA provides that the board is generally obliged to seek shareholder approval for defensive action that may frustrate a tender offer.

Finland has resolved to opt out of the breakthrough rule contained in Article 11 of the Takeover Directive. Breakthrough rules may, however, be voluntarily adopted by listed companies in their articles of association. To date, these provisions have not been adopted by any listed company.

Finnish law severely restricts financial assistance. Under the Companies Act, a Finnish limited liability company may not grant any loan or any security for a loan, give any guarantee or assume any other liability the purpose of which is to finance an acquisition of the shares in the company or the shares in its parent company. A breach of the financial assistance rule may lead to, inter alia, personal liability for the members of the board of directors. In practice, alternative structures, such as merging the target company into the acquirer after the initial transaction, are used to facilitate intragroup financing arrangements in connection with acquisitions.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

The current SMA entered into force at the beginning of 2013. It includes certain rules applicable to public offers for securities.

The amendments introduced in the 2013 SMA derive mainly from the Takeover Directive. Among the key amendments, a revised definition of persons acting in concert was introduced into law, mirroring that included in the Takeover Directive. Accordingly, natural or legal persons are regarded as acting in concert if, on the basis of an agreement or otherwise, they cooperate with a shareholder, the bidder or the target company with a view to exercising or acquiring significant influence in the company or frustrating a public offer. In addition, related parties such as group companies are regarded as persons acting in concert. A bidder's obligation to promote the fulfilment of a public offer is also now expressly stated in the SMA, in line with the general principles of the Takeover Directive. Under this rule, the bidder may not prevent or substantially hamper the fulfilment of the bid or its conditions.

The FSA has the right to impose on a potential bidder a deadline for launching a public offer (‘put up or shut up’). Such a deadline can be imposed on the target company’s application in a situation where a potential bidder has publicly stated that it is considering launching a public offer. In cases where the potential bidder does not launch a bid, it can be prevented from doing so during the following six months.
To ensure sufficient protection of target shareholders, shareholders have the right to withdraw their acceptance until the bidder has announced that all the conditions of the bid have been fulfilled or waived. With regard to unconditional bids, the acceptance can be withdrawn if the bid has been valid for 10 weeks and the purchase transactions have not been effected.

The SMA provides for two exceptions from the obligation to launch a tender offer for all shares in the company. First, significant shareholders are permitted to launch a conditional consortium bid: if the mandatory bid obligation is triggered merely as a result of shareholders acting in concert in launching a voluntary offer, the shareholders are exempted from the mandatory bid obligation, provided that their acting in concert is limited to the voluntary bid. Second, no mandatory bid obligation will arise if a shareholder, or a party acting in concert, disposes of the number of voting rights exceeding the mandatory bid threshold within one month of the mandatory bid obligation arising.

Furthermore, following an amendment to the SMA implementing the EU resolution and recovery regime, no mandatory bid obligation will arise if the threshold for a mandatory bid obligation is exceeded as a result of the Financial Stability Authority having exercised its resolution implementation authority.

The SMA requires all listed companies to be members of a common organisation, the purpose of which is to develop good securities market practice.

In connection with the entry into force of the SMA, the former Takeover Panel was closed down, and as of January 2013, the renewed Securities Market Association has taken care of issuing recommendations and opinions to promote compliance with good securities market practice. The Association has also established the Takeover Board to promote good securities market practice in connection with takeover bids. Furthermore, an application can now be made to the Takeover Board for a statement regarding the interpretation of the Helsinki Takeover Code, compliance with good securities markets practice and individual company law issues.

In December 2013, the Takeover Board issued the new revised Helsinki Takeover Code, which entered into force on 1 January 2014 and replaced the Takeover Code of 2006. Compliance with the Takeover Code is based on a comply or explain principle; in a tender offer, both the target company and the bidder have an obligation to confirm whether they comply with the Takeover Code, and to publicly explain if they are not committed to complying with the Takeover Code or some of its individual recommendations.

**IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS**

The private M&A market is an integrated part of the Nordic and international private M&A market. This is reflected in Finnish market practice and the procedures followed in Finnish private transactions. Even purely Finnish transactions are often prepared, negotiated, drafted and executed in ways that are similar to those in the international marketplace.

A large number of Finnish transactions have a cross-border element, as foreign ownership of Finnish businesses continues to increase. The financial crisis significantly decreased the use of structured sales and auctions in the Finnish market, but in recent years structured sales have regained their prominence, although broad auctions have remained less common.

As the Finnish market is relatively small, Finnish companies frequently engage in M&A transactions abroad, both as sellers and buyers. Foreign buyers are, on the other hand, frequently involved in the Finnish market on the buy side.
As in other Nordic countries, the legal advisory market concentrates on domestic firms. The same goes for domestic or Nordic banks, which handle a large share of the financial advisory mandates. However, the largest transactions frequently involve large international investment banks, complemented by local Finnish players.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Finnish activity abroad

Finnish activity abroad generally comprised smaller acquisitions with a few exceptions, such as the acquisition by Stora Enso Oyj, the Finnish pulp and paper company, of Swedish forest asset Bergvik Väst AB, valued at €1 billion (announced in November 2018). Other notable deals included the following acquisitions:

a Sanoma Oyj, the Finnish media company, acquired Iddink Group BV, a Netherlands-based educational platform and service provider, for €227 million (announced in December 2018);

b Ramirent Plc, the Finland-based provider of machinery and equipment rentals for construction and industrial use, acquired Stavdal AB, a Sweden-based construction equipment rental company, for €158 million (announced April 2019); and

c Valmet Oyj, the Finnish developer and supplier of technologies, automation and services for the pulp, paper and energy industries, acquired GL&V Inc, a Canada-based provider of technologies and services to the pulp and paper industry, for €113 million (announced February 2019).

In general, acquisition activity abroad by Finnish companies has remained relatively high during the past 12 months, with Finland-based companies actively seeking international growth, mainly through smaller acquisitions.

ii Private equity

Private equity (PE) investors’ activity showed some strong growth during 2018 and the first half of 2019. The amount of PE and venture capital (VC) investments into Finnish companies reached approximately €203 million in 2018 in the aggregate, according to data from the Finnish Venture Capital Association. The total number of investments by PE and VC funds into Finnish companies in 2018 was 154.

Notable PE transactions included the acquisition of Parmaco, a Finland-based provider of modular buildings, by a consortium led by Terra Firma, a UK-based PE investor, for an estimated €400 million, from MB Funds, a Finnish PE investor (announced in October 2018), and the acquisition of OpusCapita Solutions, a digital payment solutions provider, by Providence Equity Partners, from Finnish Posti Group (announced in February 2019). In addition, there were a number of smaller transactions.

PE investors have generally remained active, and many are expected to exit portfolio companies already beyond their planned investment horizon and to invest committed capital. In recent years, the trend in sales processes has moved towards a higher level of differentiation in terms of structure, with the popularity of large-scale controlled auctions decreasing, and the focus remaining on more concentrated efforts with a limited number of bidders.
iii Public-to-private activity

Public-to-private transactions during 2018 and 2019 to date included several notable transactions, including the following:

- a consortium led by ANTA Sports Products Limited’s €5.6 billion tender offer for Amer Sports Oyj, the Finland-based sporting goods company, being the largest ever tender offer for a Finnish company (announced in December 2018);
- Telenor’s announced acquisition of a controlling stake in DNA Plc, the Finnish telecommunication company, to be followed by a mandatory tender offer, valuing DNA at €3.1 billion (announced in April 2019); and
- Kildare Partners’ €1.6 billion tender offer for Technopolis Oyj, a Finland-based company engaged in the provision of workspaces and services related to the technology industry (announced in August 2018).

Other notable transactions were ÅF AB’s tender offer for Pöyry, the Finnish consulting and engineering firm, for €586 million (announced in December 2018) and Orkla ASA’s tender offer for Kotipizza Group Oyj, the Finnish pizza and fast food restaurant chain, for €158 million (announced in November 2018).

No major hostile offers have been seen on the Finnish market since Nordic Capital’s unsuccessful €1.1 billion offer for TietoEnator (currently Tieto) in 2008. However, one minor unsuccessful hostile offer occurred in November 2016 when Sistema Finance, a subsidiary of the listed Russia-based diversified holding company AFK Sistema, announced its offer to acquire Honkarakenne, the listed Finland-based housing construction company, against a cash consideration of €7.8 million.

iv Sector-specific trends

After a strong and active period in the healthcare sector, activity in the sector showed some signs of slowing down, mainly due to the failed social and healthcare reform, which resulted in the government resigning in March 2019 just four weeks ahead of the general elections, and a scandal involving private sector care service providers gaining extensive media coverage in February 2019. Following strong activity during the first half of 2018 (including the acquisition of Mehiläinen, the Finland-based provider of healthcare and social care services, by CVC and Finnish institutional investors for an estimated €1.8 billion, announced in May 2018), the only notable transaction in the sector was the acquisition of Coronaria Hoiva Oy, the Finland-based social care provider, by Humana, the Swedish social care provider, for €71 million (announced in January 2019). There was also a number of smaller transactions.

Deal activity in the information technology and telecommunications sector has remained high during 2018 and 2019. The most significant transaction in the information technology and telecommunications sector was Telenor ASA’s €3.1 billion acquisition of DNA Plc announced in April 2019. Other major transactions included the acquisition of Small Giant Games Oy, the Finnish mobile game developer, by Zynga, Inc, a US-based online gaming company, for €490 million (announced in December 2018), and Technology Crossover Ventures’, a US-based PE firm, acquisition of a minority stake in RELEX Solutions, the Finland-based computer software developer, for €175 million (announced in February 2019). There was also a significant number of smaller transactions.

Activity in the energy and infrastructure sector was lower compared to the previous year, driven by the absence of large transactions. The largest transaction in the energy and
infrastructure space was the acquisition of 33.9 per cent of Loiste Oy, a Finland-based energy company, by Mirova SA and Infranode, for €200 million (announced in April 2019). There were also some smaller transactions in the sector.

Transaction activity in the Finnish real estate and construction sectors remained active, the biggest transaction being Kildare Partners’ €1.6 billion tender offer for Technopolis Plc, the Finland-based company engaged in the provision of workspaces and related services to the technology industry, announced in August 2018.

In May 2016, the government announced its renewed ownership steering strategy, the main objective of which is to use invested capital to increase growth through, inter alia, the disposal of all or part of the government’s stake in certain wholly or majority owned companies. The government has carried out further disposals of stakes in certain companies, including Neste, the listed oil refining company.

The industrial products and services sector also witnessed fairly strong activity. In addition to Norwegian NRC Group ASA’s acquisition of VR Track Oy, the Finnish railway track maintenance company, for €225 million (announced in October 2018), there were several smaller transactions. The consumer and retail sector received a notable boost with the ANTA Sports Products Limited-led consortium’s acquisition of Amer Sports Oyj, the Finnish sporting goods company, for €5.6 billion (announced in December 2018), the largest ever tender offer for a Finnish company.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Domestic and Nordic banks have traditionally provided acquisition finance for Finnish transactions. However, large international banks are regularly involved in larger deals and have returned to the Finnish market, although not yet to the extent seen before the financial crisis. While Nordic banks may face lending constraints in the future because of increased bank regulation, the current market sentiment seems to be that they have a fair amount of capacity to finance transactions and that there is actually too little demand for financing. The 2018–2019 period indicates that Nordic banks are still willing to provide financing, at least for mid-sized transactions, in particular for deals in hot industries. In terms of covenants, however, the Finnish market has not to date witnessed a proliferation of covenant-lite loans without maintenance-based financial covenants.

High-yield and other corporate bonds have generally increased in importance as a financing source for larger companies. Recently, bonds have been issued in a number of refinancing transactions and for general corporate purposes. In the future, more PE sponsors are expected to tap the high-yield bond market, particularly as a source of refinancing for existing portfolio company debt. The absence of maintenance-based financial covenants is often cited by PE sponsors as a key benefit of high-yield bonds, although it should be noted that, with the exception of a few bonds issued by PE-backed companies, Nordic high-yield bonds’ terms tend to contain maintenance-based financial covenants.

Finally, there is a trend towards an increasing number of non-bank loan investors in the leveraged buyout market, including asset managers, hedge funds and collateralised loan obligations. The majority of those investors are from outside the Nordic countries.
VII  EMPLOYMENT LAW

A transfer of business under the Finnish Employment Contracts Act corresponds to the transfer under the Acquired Rights Directive. The basic requirement for a transaction or arrangement to constitute a transfer of business is that the subject of the transfer is an economic entity (i.e., an organised grouping of resources that has the objective of pursuing an economic activity) and that it retains these characteristics after the transfer. Supplementary operations may also be subject to a labour law business transfer.

The transfer is mandatory and automatic. It does not require the entry into new employment contracts or other agreements with the transferring personnel, and they cannot effectively object to the transfer.

The employees transferring to the transferee are those at the service of the business concerned at the time of the transfer.

According to the Finnish Cooperation Act, which applies to companies regularly employing at least 20 employees, the transferor and the transferee have a joint obligation to provide the employee representatives concerned with information regarding the timing of the transfer, the grounds for the transfer, the legal, financial and social consequences of the transfer to employees, and the planned measures concerning the employees. The information shall be provided well in advance of the transfer of business; generally, one to two weeks before the transfer is deemed sufficient, depending on the size of the transaction and its impact on the personnel.

After the transfer, the transferee needs to make sure that the transferred personnel have been provided with the requisite information within a week of the transfer. It should also be determined whether the transfer has effects on the personnel that should be handled in full-scale cooperation consultations. If there are no such effects, the transferee has no further transfer-related consultation obligations towards the personnel.

The procedure is the same irrespective of how many employees will transfer.

VIII  TAX LAW

An important driver for choosing the form of transaction is taxation. Finland has implemented the provisions of the Merger Directive and, accordingly, certain transactions such as share-for-share acquisitions can be carried out without triggering capital gains taxation.

An asset deal is typically preferable from the buyer’s tax perspective, since the buyer may obtain a step-up in tax basis and depreciate the acquired assets (including goodwill). However, losses cannot be transferred in an asset deal. Sellers typically prefer share deals, as a capital gain is often tax-exempt in a share deal. An asset deal may be preferred by a seller with carry-forward tax losses, or if the sale resulted in a loss. A buyer cannot depreciate the acquisition cost (including goodwill) in a share deal. Tax loss carry-forwards of the target can frequently be preserved in a share deal.

Transfers of shares and other securities in Finnish companies are subject to a transfer tax of 1.6 per cent of the sale price (2 per cent for transfers of securities in a real estate company). The sale price is deemed to include any payments made, or obligations assumed, by the

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Transferees to or for the benefit of the transferor. Transfers of securities between non-residents are generally exempted from the transfer tax unless the securities are issued by a Finnish real estate company. In addition, transfers of securities in a foreign real estate holding company are subject to the transfer tax if the assets of the foreign company mainly comprise real property (directly or indirectly) located in Finland, and either the transferor or transferee is Finnish. In addition to securities, a transfer tax at a rate of 4 per cent is levied on the transfer of real property. Where the consideration consists of securities, other than newly issued shares, the transfer tax is levied on the transferred assets and the consideration. Certain corporate restructurings, such as the transfer of a business against share consideration, are exempt from the transfer tax. Certain transfers of listed shares on the stock exchange are also exempted from the transfer tax.

An asset deal is not subject to VAT if it is treated as a transfer of a business as a going concern, the transfer is made to the buyer and the buyer starts using the assets in a business subject to VAT. No VAT is payable upon a transfer of shares in a share deal.

Acquisitions are typically carried out through a local, newly established and leveraged acquisition vehicle (a limited liability company). Specific interest limitation rules limit the deductibility of net interest expenses on both intragroup loans and third-party loans to the extent that the total net interest expenses exceed 25 per cent of the borrower’s fiscal earnings before interest, taxes and depreciation (EBITD). The limitation does not apply if total net interest expenses for the year do not exceed €500,000 (including third-party interest expenses) or the company’s equity ratio is at the level of or higher than the equity ratio of the group. The Finnish Supreme Administrative Court (SAC) confirmed in a ruling that a comparison is to be made regarding the consolidated financial statements of a foreign ultimate parent company as opposed to the Finnish subgroup parent company even if the foreign ultimate parent company is not obliged to prepare consolidated financial statements pursuant to an exception under local law. Interest expenses on third-party loans are deductible up to €3,000,000 regardless of the taxpayer’s fiscal EBITD. In addition, interest expenses on third-party loans that have been concluded prior to 17 June 2016 are fully deductible. Financial institutions and certain other companies are outside the scope of the interest limitation rule.

The SAC has issued two rulings in which the right to deduct interest costs within a group of companies was limited pursuant to the general anti-avoidance rule. In both cases, the Finnish branch of an international group was not able to deduct interest costs on a loan related to an intragroup share acquisition paid by the branch to a foreign group entity. The rulings have affected the interpretation of branch structures used in intragroup share acquisitions. Otherwise, arm’s-length interest expenses on acquisition debt are generally tax deductible. There is generally no withholding tax on interest payments made to non-residents.

When certain conditions are satisfied, one group member can transfer profits to another member by way of a tax-deductible group contribution, which constitutes taxable income for the recipient. The preconditions include a minimum ownership by the (common) parent of 90 per cent of the share capital in the subsidiary (or subsidiaries) that has lasted the entire fiscal year, the fiscal years ending simultaneously as well as both parties carrying out business activities. Group contributions to foreign group members are generally not deductible.

Capital gains are generally taxable for resident individuals at 30 per cent, or 34 per cent for taxable capital income exceeding €30,000. In the case of corporations, capital gains are generally included in the taxable income. The general corporate income tax rate is 20 per cent. Capital gains from transfers of shares classified as fixed assets are tax-exempt for...
corporate shareholders, as a general rule, provided that the shares represent at least 10 per cent of the share capital of the target and have been held for at least 12 months. However, PE investors have been excluded from the scope of the capital gains tax exemption. Capital gains realised by non-resident shareholders are generally not taxable in Finland under domestic rules, unless the shareholding relates to a business carried out in Finland, for example through a permanent establishment, or if the shares are shares in a real estate company.

Dividends received by corporate shareholders are generally tax-exempt. The exemption applies to domestic dividends, dividends from resident companies of other EU Member States referred to in Article 2 of the Parent–Subsidiary Directive4 and dividends from other EEA-resident companies, provided that the company is subject to a minimum of 10 per cent tax on its income. Specific rules apply to financial, insurance and pension institutions. Furthermore, dividends received by an unlisted company from a listed company are fully taxable at 20 per cent, unless the unlisted recipient company directly holds a minimum of 10 per cent of the capital of the distributing listed company. Dividend income is fully taxable at 20 per cent in cases other than the aforementioned if no exemption is provided under a tax treaty. However, dividend income is fully taxable if the dividend has been deductible for tax purposes for the distributing company, or if it relates to arrangements that are not genuine and have been put in place for the purpose of obtaining a tax advantage.

Dividend income received by resident individual shareholders from domestic listed companies is partly taxable (85 per cent) and partly exempt (15 per cent). The taxable dividend income is taxed as capital income at 30 per cent, or at 34 per cent when taxable capital income exceeds €30,000. The taxation of dividend income received by resident individual shareholders from domestic unlisted companies is determined based on an annual return of 8 per cent of the net value of the shares. As a general rule, within the 8 per cent annual return, dividend income is partly taxable (85 per cent) as capital income and partly tax-exempt (15 per cent). However, up to an amount of €150,000, only 25 per cent of the dividend income is taxable as capital income. To the extent that the dividend income exceeds the 8 per cent annual return, 75 per cent of the dividend income is taxable as earned income at progressive rates and 25 per cent is tax-exempt.

Foreign corporate shareholders are generally subject to a withholding tax at a rate of 20 per cent on dividends. However, dividends are not subject to withholding tax if paid to a corporate recipient covered by Article 2 of the Parent–Subsidiary Directive5 that holds more than 10 per cent of the distributing company’s share capital, or an EEA-resident corporate recipient that cannot obtain a credit for the withholding tax, and the dividend, if paid to a Finnish-resident corporate recipient, had been tax-exempt. Further, the level of withholding tax is generally reduced to between zero and 15 per cent under Finland’s tax treaties.

As a general rule, losses can be carried forward and used up to 10 years after the year in which they arose. However, losses incurred by a company are not carried forward if a change of more than 50 per cent in the ownership occurs. The rule also applies in the case of an indirect ownership change. An exemption may be granted by the tax authorities.

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IX COMPETITION LAW

Merger control rules are set out in the Finnish Competition Act, which entered into force in November 2011. If the EU Merger Regulation does not apply, a transaction must be notified to the Finnish Competition and Consumer Authority (FCCA) if the aggregate worldwide turnover of the parties (i.e., usually the acquirer and the target) exceeds €350 million and each of at least two of the parties has a Finnish turnover of at least €20 million. Finnish turnover means sales to customers located in Finland irrespective of whether the seller has any physical presence in Finland. Notification must be submitted after entering into a concentration agreement, acquisition of control or an announcement of a public offer, and in any event before closing the transaction. It is also possible to notify the transaction as soon as the parties have, with a sufficient degree of certainty and sufficiently specific terms, proven their intention to conclude the transaction: for instance, with a signed letter of intent. A notified transaction may not be implemented before clearance unless the FCCA grants an exemption.

The FCCA applies the significant impediment to effective competition test in line with the Merger Regulation. The Market Court of the Federation may, if proposed by the FCCA, prohibit a transaction, order it to be cancelled or impose conditions if the concentration would significantly impede effective competition in Finland or in a substantial part thereof, particularly as a result of the creation or strengthening of a dominant position.

The FCCA will decide within one month of submission of a notification to either approve the transaction or begin an in-depth investigation. The in-depth investigation may last for three months (but may be extended by two months). The FCCA can extend the investigation period if the parties to a transaction do not submit the required information to the authority, or if the information is significantly incomplete or inaccurate. If the FCCA wishes to prohibit the transaction, it is required to make a proposal to that effect to the Market Court, which will decide on the issue. The Market Court’s decision can be appealed to the SAC. The notifying party, however, is not entitled to appeal a conditional approval decision of the FCCA to the Market Court.

The Competition Act was amended effective as of June 2019, extending the time period of Phase I proceedings from one month to 23 working days. Consequently, the time period for Phase II proceedings was amended from three months to 69 working days, and the extension period from two months to 46 working days. The new provisions also grant the FCCA a right to obtain confidential information necessary for the investigation of merger control from other authorities, such as the tax authority and the Grey Economy Information Unit.

X OUTLOOK

The general short to medium-term outlook is somewhat mixed, with significant uncertainty as to whether the slowdown during the first half of 2019 will prove more persistent or whether the market will regain its momentum. In any event, it seems unlikely that M&A activity will return to the level seen in 2018.

Financial sponsors have been more active in the markets than at any time since the financial crisis and are expected to remain active. The amount of the funds already raised...
but not yet invested continues to be significant. Many financial sponsors also continue to remain under pressure to dispose of portfolio companies already held beyond the planned investment horizon. Many potential industrial buyers continue to be in a strong financial position and to seek investment targets.

After a lengthy process, the government’s reform of public social and healthcare services lapsed in March 2019 and caused the government to resign. As part of the reform, the responsibility for organising social and healthcare services would have transferred from municipalities to counties and partially opened up the public social care and healthcare market to private providers. The new government has just been formed, and it is expected to continue to work on a reform of the social and healthcare reform system. There are, however, many uncertainties surrounding the reform, and the new government has announced that it is not contemplating a reform that would open up the social care and healthcare market to private players to a significant extent. Over the medium to longer term, consolidation in the social care and healthcare sector is expected to continue.

After a few active years, the initial public offering market showed clear signs of slowing down. The NASDAQ OMX Helsinki had 14 listings in 2018, six on the main list and eight on the First North Finland list. In 2019 to date, NASDAQ OMX Helsinki has seen only three new listings.

The stock market is currently facing a number of uncertainties, including the US–China trade war, Brexit and a weak economic outlook for leading eurozone countries. Generally, investor confidence still appears to have remained at a fairly good level, and stock market valuation levels remain fairly attractive. The overall development of the share prices of Finnish companies listed on NASDAQ OMX Helsinki has been positive since early 2016.
I OVERVIEW OF M&A ACTIVITY

Despite Macron’s agenda to promote investments in France, French M&A activity in 2018 recorded its lowest level in terms of aggregate value since 2014 as material deals announced in France reached €54.5 billion against €99 billion in 2017. The number of material transactions reached 875, which is lower than the number seen in the past two years, with 932 deals announced in 2016 and 922 announced in 2017. Compared to 2017, when five deals worth over €5 billion were announced, France did not attract jumbo deals in 2018, and all transactions targeting French companies announced in 2018 were valued below €3.5 billion.

This decrease in value and volume of M&A activity can be explained by factors such as a lack of significant deals and investors’ caution following the 2017 presidential election, as a great number of reforms were implemented and others have been adopted since then. As expected, 2018 was a significant year in terms of economic regulation: the government has notably reformed and simplified certain corporate and financial market rules applicable to French companies and the provisions related to their funding. It has also strengthened the control regime of foreign investments in French companies. Such decrease may also be explained by the uncertainty arising out of the conditions of Brexit and unforeseen social instability in the second half of 2018: these required an urgent political response from the government the economic consequences of which were difficult to predict.

The only sector that has not been affected by this decline is private equity. Indeed, private equity transactions, which reached their highest annual value since the financial crisis at €24.2 billion, amounted to 44.4 per cent of the aggregate value of the deals announced in 2018.

M&A activity was driven by a few large cap deals, including the €2.6 billion bid made by Total SA for Direct Energie SA, with a view to enhancing Total’s market share in electricity distribution activities. The largest transaction in 2018 was the acquisition by Merck & Co of Antelliq for €3.25 billion from a UK private equity firm.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The French Commercial Code and the French Civil Code – in respect of which the provisions relating to contract law were reshaped in October 2016 and clarified in April 2018 – provide the statutory framework and form the legal basis for the purchase and sale of assets or legal
entities. Additionally, the French Monetary and Financial Code and the General Regulations of the French Financial Markets Authority (AMF) provide the regulations relating to takeovers. As a general rule, French takeover rules apply if a target is a French or EU public company whose securities are listed in France and, in some instances, if the company is dual-listed.

Rules relating to the financial services industry, the listing and public offering of securities and the prevention of market abuse are set out in the Monetary and Financial Code and in the General Regulations of the AMF.

French merger control rules are mainly contained in the Commercial Code. These rules apply to cross-border mergers having effects on the French market (as currently defined in accordance with worldwide and France-wide turnover thresholds) but with no EU dimension. Mergers with an EU dimension (i.e., involving companies whose turnover exceeds the thresholds set by the EU Merger Regulation) are instead subject to the review of the European Commission.

Within the framework of the applicable laws and the General Regulations of the AMF, NYSE Euronext operates the three French regulated markets, one stock market (Euronext Paris) and two derivative markets (Monep and MATIF), and some organised markets (such as Euronext Growth).

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i New additional regulations regarding the use of Blockchain technology

Further to and as required by an ordinance dated 8 December 2017, France adopted an implementation decree on 24 December 2018 that authorises and regulates the effective use of blockchain technology to record and operate the transfer of certain securities. This regulation governs the registration and transfer of securities issued in France and governed by French law that are not listed on a regulated market or on a multilateral trading facility. The French provisions do not impose a specific share electronic recording device, therefore granting total freedom to issuers and parties regarding the selection of such devices.

In practical terms, non-listed French issuers may decide to issue their securities on shared electronic recording devices (i.e., a blockchain) instead of the current book entry. Such shared electronic recording device shall guarantee the registration and integrity of entries and enable holders of securities to be identified, together with the number of securities they hold. In this regard, any holder may ask to be provided with a certificate setting out its transactions. Registration in a shared electronic recording device, such as registration in a buyer’s account in the book entry system, entails a transfer of securities. Similarly, a pledge over securities registered in a shared electronic recording may be constituted under the same terms and conditions as a pledge over securities registered in a book entry.

ii Promoting the growth and transformation of companies

On 11 April 2019, a law relating to an action plan for corporate growth and transformation of French companies (also known as the PACTE law) was adopted. The PACTE law aims to simplify corporate law and promote corporate financing. It also aims to instil a new vision of capitalism by allowing (but not requiring) French commercial companies to define in their bylaws not only their objects, but also their own objectives.
This reform entails the following main practical developments:

- **a** decrease of the squeeze-out threshold (from 95 to 90 per cent) in order to facilitate the delisting process;
- **b** the possibility offered to non-listed companies to issue preferred shares with multiple voting rights attached and preferred shares that are redeemable on the holder's request;
- **c** facilitating the access of companies to diversified funding (both public and private funding) through a simplification of the rules applicable to public offerings and a new initial coin offering (ICO) legal framework. This new framework will provide investors with certain safeguards and guarantees that French-based ICO issuers will have the possibility of requiring the approval (visa) of the Financial Markets Regulator certifying a set of requirements concerning the security and transparency of the token issued, and the creation of rules with respect to the secondary market for tokens;
- **d** a simplification of the rules applicable to mergers. While French merging companies used to be required to file with the commercial registry a statement in which they state that and acknowledge that they have performed the merger in accordance with the applicable rule, French companies will now be exempt from the requirement to perform such a compliance declaration. The PACTE law also introduces the possibility for a French SA to implement a merger by using a delegation of powers;
- **e** strengthening the rules governing gender balance in the corporate governance of French société anonymes and French SCAs. First, decisions taken by a board of directors or a supervisory board that do not comply with the rules relating to gender balance may be deemed void. Secondly, appointment procedures for new executives in French société anonymes shall now endeavour to achieve a balanced representation of women and men; and
- **f** privatisation of certain state-owned companies, and notably Aéroport de Paris (ADP), la Française des Jeux and Engie. The privatisation of ADP is, however, currently on hold due to political opposition.

### iii Simplifying corporate law

A law to simplify, clarify and update French corporate law was adopted on 10 July 2019, with immediate effect. This law notably contains the following main reform proposals:

- **a** the extension of the scope of the simplified merger regime, which allows the implementation of a merger without a shareholder decision approving the merger and without any report from special auditors, to mergers between sister companies wholly or 90 per cent owned by the same parent company;
- **b** the removal of the obligation to submit every three years a draft resolution on a capital increase to the benefit of employees; and
- **c** abstentions in general meetings of shareholders will no longer be counted as negative votes.

### iv Protection of trade secrets

A law on the protection of trade secrets was adopted on 3 July 2018 and is currently in force. This law implements Directive 2016/943 on the protection of undisclosed know-how and business information (trade secrets) against unlawful acquisition, use and disclosure into French law.
France

Under this new regime, any information known by a limited number of people with a commercial value and being subject to reasonable protective measures shall be regarded as trade secrets. The secrecy alone of information is not sufficient to benefit from the protection provided by law, as companies will have to prove that protective measures were put in place (e.g., confidentiality rules or restrictions on access rights) for that information.

The acquisition, use and disclosure of a trade secret is unlawful when it is carried out without the consent of its legitimate holder and arises from unauthorised access or unfair access in a way contrary to the normal course of trade.

v Strengthening the foreign investment control regime

Like most G20 countries, France has recently revised its foreign investment regulation to widen the scope for scrutiny of foreign investments by expanding the list of business sectors deemed sensitive to public order, public safety or national defence interests. The new business sectors falling within the scope of the foreign investments regime are notably:

a. activities related to operations in space;

b. activities related to electronic and IT systems that are required for the performance of police or customs duties;

c. activities related to cybersecurity, artificial intelligence, robotics, additive manufacturing and semiconductors; and

d. activities related to data hosting.

The scope has also been extended to the provisions of services related to business sectors that were already within purview (e.g., war materials or activities performed pursuant to an agreement entered into with the French Ministry of Defence).

Furthermore, it is also now possible in France for target companies to ask the French Ministry of Economy whether a contemplated investment is subject to the French foreign investment control regime. Such extension stems from a suggestion made by French tech companies to facilitate their fundraising, as the business sectors subject to foreign investment control have been correlative extended to the activities they may pursue.

As part of the PACTE law, France has also introduced a potentially more widespread use of golden shares in certain strategic companies in which the state has a stake if it becomes necessary to protect national essential interests relating to public order, public health, public security or national defence. Golden shares will grant the state with blocking powers (e.g., the right to block asset disposals or transfers of intellectual property or know-how outside France) and information rights regarding the exercise of the rights attached to a golden share. In any case, one ordinary share held by the state may be converted into a golden share by decree, and the rights attached to such golden share may also be increased or reduced by decree.
IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In 2018, French companies (as bidders or target companies) were involved in only one of the top 20 announced European deals, and French investors were more active in acquiring outside Europe. The United States remains the leading investor in France, with US investments representing 18 per cent of the foreign investments completed in France.4

i Cross-border inbound deals

Material inbound M&A transactions included, inter alia, the €3.25 billion acquisition of Antelliq by Merck & Co Inc, a US pharmaceutical company; the €2.59 billion acquisition by General Electric Company of Alstom’s stakes in three energy joint ventures created with General Electric in 2015; and the €2.25 billion acquisition of Linxens Group by Tsinghua Unigroup.

ii Cross-border outbound deals

Notable outbound M&A transactions included, inter alia, the €12.4 billion acquisition of XL Group Ltd, a US insurance company, by AXA SA;5 the €5.41 billion acquisition of a 50.01 per cent stake in Gatwick Airport Limited by French Vinci Airports SAS; and the €3.7 billion acquisition of Ablynx, a company conducting pharmaceutical, medical and biotech activities, by the French listed company Sanofi SA.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Less activity in 2018, many opportunities in 2019

As mentioned in Section I, M&A activity declined in 2018 compared to 2016 and 2017. However, the first months of 2019 give signs of hope, as the deals announced so far this year have already reached an aggregate value of €9.9 billion, compared to the €8.6 billion reached for the first quarter of 2018.

The contemplated sales of significant stakes owned by the state in la Française des Jeux, Aéroport de Paris and Engie could generate high-value transactions and boost the M&A market in the second half of 2019. Private equity firms are also planning exits from high-valued portfolio companies.

ii Development of private equity activity

In 2018, the private equity trend was still moving upwards both in terms of value and deal count. Buyout and exit deals reached an aggregate value of €23.6 billion, which is close to pre-crisis levels, 39 per cent of which is being driven by domestic private equity firms.

3 Financial data extracted from Mergermarket, ‘Trend Report Q1–Q4 2018 (France)’
iii  Most active sectors in 2018

In 2018, telecoms, media and technology (TMT), consumer, industrial, chemical and business services were the most targeted sectors.

The TMT sector broke all European records, reaching €169.1 billion in 2018 up from €61.5 billion in 2017. The sale by Altice of the fibre-to-home services provided by SFR to Allianz, AXA and OMERS for €1.8 billion was a notable transaction.

The consumer sector was the second-most active sector in 2018 with the acquisition of Neovia Group by Archer Daniels Midland Company for €1.54 billion being a key transaction.

The industrial and chemical sector was the third-most active sector in 2018.

iv  Tender offers in 2018

In 2018,† tender offers declined considerably, both in terms of the number of bids (22 in 2018 compared with 27 in 2017) and the aggregate value of the target companies (€12.5 billion in 2018, which is eight times less than the value seen in 2017, when the equivalent figure was €106.2 billion).

All the offers made in 2018 were friendly, with half being initiated by the companies themselves (as part of share buyback programmes) or by their long-standing shareholders. The takeover bid made by Allianz SE for Euler Hermes was one of the most important public M&A deals of 2018, with a target company valuation of around €5.2 billion, together with the bid made by Total SA for Direct Energie for €2.6 billion.

VI  FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

i  Overview of financing sources

After a remarkable year in 2017, 2018 was characterised by a slowdown in M&A transactions due notably to the return of market volatility. As a result, a decrease in activity was observed in all financing segments.

2018 marked a turning point for the corporate eurobond market as it was the first time the amounts raised have decreased since 2011. By mid-December 2018, €270 billion had been raised compared to €300 billion in 2017. This decrease can be partly explained by an announcement by the European Central Bank (ECB) in June 2018 that it was ending its quantitative easing policy (which occurred at the end of December 2018). Since March 2015, the ECB had acquired nearly €2,600 billion worth of assets on the markets, including nearly €180 billion corporate bonds. However, French non-financial companies issued nearly €65 billion worth of bonds in the course of 2018, which represented 16 per cent more than 2017. On the other hand, convertible bonds issues fell by nearly 40 per cent, representing a total amount of €2.4 billion in 2018 compared to €4 billion in 2017.

Additionally, with nearly €90 billion borrowed by way of loans by companies between January and November 2018, the syndicated loan market recorded a year roughly in line with 2017 (€95 billion). However, one of the traditional drivers, namely acquisition finance, only had a limited impact on these results. Indeed, despite a few significant transactions, M&A accounted for only around 20 per cent of the total amounts of loans raised in 2018.

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† Financial data extracted from the Observatoire des offres publiques 2019 report.
Recent legal reforms

Amendments to the 2016 reform of the contract law

On 1 October 2018, the law modifying and clarifying the 2016 reform of the contract law came into force. Such reform has a direct impact on all contracts, including finance documentation. This law is attempting to strike a balance between developing familiar features of French law (for instance, the obligation to inform the other party of any information of decisive importance for its consent, and the requirement that contracts be negotiated, formed and performed in good faith) while adding certainty for creditors (for instance, the legal provision on hardship introduced by the 2016 reform – Article 1195 of the French Civil Code – is now expressly excluded when it comes to transactions on securities or finance documents further to Article L211-40-1 of the French Monetary and Financial Code). Such law has also reconfirmed that parties are allowed to assign under French law through two distinct procedures, either through receivables arising out of a loan contract or the benefit of the entire contract as a whole.

Further inroads into the banking monopoly regime

The publication of Decrees No. 2018-1004 and No. 1008 of 19 November 2018 is further evidence that the banking monopoly rules are ever-shrinking in relation to investment funds, as a number of funds could purchase a participation in non-revolving loans but were precluded from being initial lenders for the same loans. While Ordinance No. 2017-1432 of 4 October 2017 had defined a new regime for certain specialised financing vehicles (which were then allowed to lend within the framework of the European long-term investment funds Regulation, or alternatively within the restrictions imposed on the securitisation vehicles), the new Decrees have redefined the direct lending capabilities of such specialised finance vehicles and securitisation vehicles by reference to the rules applicable to specialised professional funds, which represent a relative alleviation of the applicable conditions.

Modernisation of the law on security interests

The 2018 edition of this publication mentioned that the security agent role had been modernised through Ordinance No. 2017-748 dated 4 May 2017, which came into force on 1 October 2017. Such reform allowed security agents to be the direct holder (rather than the initial lender) of both security interests and personal guarantees granted by the security grantor. Foreign institutions have welcomed this reform, which was designed by reference to the common law of trusts for security agent roles in common law countries. However, it appears that as a matter of practice, French banks have generally chosen to stick, by and large and somewhat surprisingly, to the previous regime whenever possible.

The PACTE law contains a number of proposals with a view to reforming the law pertaining to security interests and allows the government to legislate by way of ordinances to that effect.

The law suggests establishing a general right of assignment of receivables as security. This security interest currently exists in France only to the benefit of banking institutions, which are the only possible assignees of receivables in the context of certain forms of security by way of assignment (Cession Dailly). The creation of this new security interest would have the effect of aligning French law with the laws of other countries such as England, where this security already exists as security assignments. The PACTE law also aims at modifying the rules relating to guarantees and third-party security. It also suggests introducing more
flexibility regarding the rules on security trusts in the Civil Code. Finally, the PACTE law aims at a better articulation between the securities law and insolvency proceedings, and for this purpose authorises the government to simplify, clarify and modernise the rules relating to security interests and secured creditors in the context of insolvency proceedings.

iii Recent legal reforms

Looking forward, it is already clear that France will witness a number of important changes over the next few months. In particular, the impact of Brexit (the modality of which is not yet settled at the time of writing), the rapid emergence of green lending (either as regards green projects or merely with loans whose margin will be affected by the environmental performance of the borrower) will ensure that the French financings sector will remain very dynamic for the foreseeable future.

VII EMPLOYMENT LAW

On 22 September 2017, the government enacted several ordinances that were ratified by Parliament on 29 March 2018: the Macron labour law reform has brought significant changes to French labour law with a view to simplifying the existing rules and regulations under the French labour code and granting more flexibility for employers in respect of employee management, thus attempting to make France more attractive to foreign investors. The Macron labour law reform includes provisions that may have an effect on M&A transactions: the main ones are as outlined below.

The Macron labour law reform has created a unique representative body in lieu of the existing staff delegates, works councils and health and safety committees: social and economic committees (SECs). An SEC will have to be implemented in companies with 11 or more employees by 31 December 2019 at the latest. SECs will replace the works councils as from such date, and will exercise similar functions to those of the works councils. As is the case for works councils, relevant compulsory consultations with SECs must be carried out within certain time limits (see Section VII.iv).

Introduction of greater flexibility around employment restructuring

Rules governing collective redundancies for economic reasons

Under French law, to implement collective redundancies for economic reasons employers must provide valid economic grounds justifying the redundancies. Since the Macron labour law reform, these grounds must now be assessed at the level of the French territory only (i.e., at the level of the French employer company only, or at the level of the French company and any other entities of the group located in France if those entities belong to the same business sector as the French company). Before the Macron labour law reform, such grounds were assessed at the level of the group as a whole in France and abroad.

These amendments further progressed the simplification of the redundancy rules that had been initiated under Law No. 2016-1088, which entered into force on 8 August 2016 (El Khomri law). The El Khomri law introduced two main changes to the redundancy rules: the

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codification of two grounds of dismissal previously only recognised by case law (restructuring aimed at safeguarding a company’s competitiveness and the closure of a company); and the addition of economic indicators defining the concept of economic difficulties.

Since the El Khomri law was enacted, economic difficulties are now mainly appreciated on the basis of a significant decrease in the number of orders from or the turnover of a company, appreciated by reference to a number of quarters and the number of employees within a company (e.g., in companies with less than 11 employees, a decrease of the turnover during one quarter is considered as a sufficient ground for an economic redundancy). These indicators do not constitute an exhaustive list, and any other element justifying the existence of economic difficulties can be used to justify economic difficulties. Therefore, despite these modifications, French case law will continue to be of key relevance when establishing whether a company is facing economic difficulties.

The Macron labour law reform has also provided security and visibility with regard to potential disputes arising following a dismissal by introducing a judge-binding scale of damages – the Macron scale – granted for unfair dismissals (employees with less than one year of seniority within a company can be awarded up to one month’s salary, while employees with 30 years’ seniority and above can be awarded up to 20 months’ salary). However, since its enactment, the Macron scale has met with resistance from the labour courts, as some judges consider that the capping of damages would interfere with the right to adequate compensation granted by the Termination of Employment Convention (No. 158) of the International Labour Organization and the European Social Charter. A future ruling of the French Supreme Court on this issue is therefore awaited.

Collective mutual termination procedure

To facilitate job reorganisations and head count adjustments other than for economic reasons, the 2017 Macron labour law reform introduced an ad hoc voluntary termination procedure called the collective mutual termination procedure. Recent case law has specified that this procedure could also apply to headcount adjustments based on economic grounds.9 Under the collective mutual termination procedure, employees apply for a voluntary departure plan that must be validated by the French Labour Administration. Companies will not have to demonstrate economic difficulties before implementing such an agreement. Under the supervision of the Labour Administration, a voluntary departure plan must contain specific provisions, and in particular on the maximum number of job terminations contemplated and the modalities of information for SECs (no consultation with an SEC is required). The collective mutual termination procedure does not prevent an employer from hiring new employees either for a new position or a position occupied by an employee who agreed to the mutual termination of his or her employment contract.

Employees’ right to make an offer to buy shares or assets in small and medium-sized companies

Pursuant to the Hamon law of 2014, as modified by the Macron law of 2015, companies with fewer than 50 employees, or companies with between 50 and 250 employees that fall into the category of small and medium-sized companies (i.e., companies with a turnover below €50 million or a balance sheet total below €43 million), must inform their employees of any

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9 Administrative Court of Cergy-Pontoise, 16 October 2018, No. 1807099
proposal to sell 50 per cent or more of the shares of the company or the sale of the company’s business as a going concern with a view to allowing them to make an offer to purchase the shares or the business. The Hamon law does not grant any priority or pre-emption rights to employees; however, the procedure does impact the timetable for a proposed transaction, and can also have an impact on the confidentiality of the transaction.

Regarding companies with fewer than 50 employees, such employees must be informed of a proposed sale no later than two months prior to the signing of the transaction. In addition, the transaction cannot take place before the expiry of this two-month period unless all employees have informed the company that they do not wish to make an offer.

In companies with between 50 and 250 employees, the employees must be informed of a proposed sale at the latest when the works council or the SEC of the company is informed and consulted on the transaction in question. Unlike in the case of companies with fewer than 50 employees, the law does not set any specific deadline prior to which the transaction cannot take place (except that the works council or SEC consultation process will have to be completed before any binding documentation with respect to the transaction is signed, in compliance with generally applicable French employment law rules).

The law provides that employees are subject to an obligation of discretion with respect to the information that they receive by virtue of the new law. For the moment, it is not clear what information regarding a company and its activities must be given to its employees in connection with a specific procedure. According to a strict interpretation of the law, when a company informs its employees of their right to make an offer to buy the company or the business, it is not required to give information on any other potential bidders or any documents relating to the company or its strategy. However, should one or more employees ultimately decide to make an offer to buy the company or the business, the Hamon law (and its implementing Decree of 28 October 2014) is silent as to the level of information that the company must provide.

Failing to comply with the obligation to inform employees that they can make an offer to purchase the shares or assets of a company exposes a seller to a monetary fine that cannot exceed 2 per cent of the value of the underlying transaction.

Following an information procedure under the Hamon law, the contemplated sale must take place within two years of the date on which the employees are informed of the transaction; otherwise, the company must complete the information process again.

iii Reinforced role of the works council or the SEC of the target of a takeover bid

Pursuant to Law No. 2014-384, which entered into force on 29 March 2014 (Florange law), in a public company takeover context, the works council or SEC of a target company must be formally consulted and issue an opinion (either positive or negative) on the takeover bid (whether friendly or hostile).

The consultation of the target company’s works council or SEC must be completed (i.e., a positive or negative opinion must be issued) within one month of an offer being filed. If the works council or the SEC has not issued an opinion within this time frame, it will be...
deemed to have been consulted, except in certain exceptional circumstances where the works
council or the SEC can justify in court that it did not receive sufficient information about a
transaction.

In any case, the board of directors or the supervisory board of the target company
cannot make a decision with respect to a takeover bid (including whether to recommend the
bid) until the consultation process with the target company’s works council or SEC has been
completed. Note that in a situation in which the bidder has entered into a prior agreement
with the target (generally called a tender offer agreement) specifying the main terms and
conditions of the offer and providing for a break-up fee based on the recommendation of the
target’s board, it should be carefully assessed whether such agreement triggers the obligation
to consult the works council or SEC prior to its signature.

During the consultation process, the target company’s works council or SEC may ask
the offeror questions about its industrial and strategic plans for the company. It may also
choose to be assisted by a third-party expert (whose fees will be paid by the target company,
and who will issue a report that will assess the offeror’s industrial and strategic plans and their
impact on the target company and its employees). The third-party expert has three weeks
from the filing of the offer to issue its report.

iv Defined time limits for works councils or SECs to issue opinions in compulsory
consultation situations

A decree dated 27 December 2013 establishes the relevant time limit for works councils to
issue their opinion in the event that their consultation is compulsory. Unless an agreement
is reached between an employer and trade union representatives (or, failing that, the works
council) that provides for a specific time frame for their consultation, the members of a works
council must issue their opinion within the following time limits (the starting point being the
date on which a employer discloses the information):

a one month generally;
b two months if a works council is assisted by an expert;
c three months if one or more health and safety committees (CHSCT) are involved in a
project; and
d four months if a temporary coordination committee of a CHSCT is created.

If a works council has not issued an opinion within the relevant time limits, it will be deemed
to have been consulted and to have issued a negative opinion.

As indicated in Section VII.i, SECs will replace works councils on 31 December 2019
at the latest. The defined time limits within which SECs will have to render their opinion in
compulsory consultations (and that apply as from the setting up of an SEC) are as follows:
one month generally; two months if an SEC is assisted by an expert; and three months in
very specific situations where the consultation is carried out in a company that has one or
more local SECs involved in the consultation process being assisted by at least one expert.12

As is the case with works councils, these time limits apply in the absence of an agreement
entered into between an employer and the trade union representatives (or, failing that, the
SEC), providing for a specific time frame for the consultation of SECs.

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v  Obligations to look for a buyer in the event of the closure of a business division
Among its provisions, the Florange law has introduced an obligation for an owner seeking to close a business to attempt to find a buyer for the business. This obligation applies to an intention to close any business division with more than 1,000 employees when such closure would result in planned collective redundancies (i.e., more than 10 employees). This obligation provides for specific information obligations toward the works council and the employees of the target business, as well as an obligation on the company or the group to consider all offers to acquire the business and to justify any decision taken in respect of such offers to the works council.

vi  Obligations of employers to fight corruption and protect whistle-blowers
The Sapin II Law on transparency, the fight against corruption and the modernisation of the economy created two new obligations for employers aimed at fighting corruption and protecting whistle-blowers.

Since 1 January 2018, employers with more than 50 employees must implement an internal process allowing employees to report, confidentially, any of the following that they have had knowledge of personally during their employment: any crime or criminal offence, a serious and obvious violation of an international treaty ratified or approved by France, or a threat or serious damage caused to the general interest.

Employers with more than 500 employees must also implement a code of conduct that must give a definition as well as examples of what could constitute an act of corruption, and also include disciplinary sanctions to be taken in cases of its violation; a process allowing employees to report, confidentially, any violations of the company’s code of conduct; and a training programme for executives and staff most exposed to the potential risks of corruption.

Any employee who submits in good faith a report of a violation will be considered as a whistle-blower and will benefit from a specific protective status against dismissal. Reports of violations must also be followed by an internal investigation that must verify the truthfulness of the report. Therefore, when implementing such processes, employers must ensure their compliance with the French labour regulations, in particular with regard to the protection of employees’ rights to privacy as well as with regard to mandatory information and the consultation of employee representatives, particularly when implementing monitoring devices.

vii  Risk of requalification of equity instruments granted to managers (management packages) as remuneration subject to social security charges
The Paris Court of Appeal ruled in July 2017 that gains realised by managers upon the sale of equity instruments (warrants in the case at hand) in the context of an leveraged buyout exit, when such instruments were granted to managers (because of their status) and kept by the latter to the extent that they remained within a company, should be considered as a salary for social contributions purposes (i.e., the gain would be subject to social contributions at a rate of around 40 to 50 per cent on an employer’s part, and around 20 to 30 per cent on an employee’s part).13

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13 Paris Court of Appeal, 6 July 2017, No. 14/02741.
Indeed, it was held that the conditions under which such warrants were granted (to employees only) and may be kept (for as long as the beneficiaries remain within a company) establish a strong link with the employment agreement or corporate office (e.g., directorship) of the relevant beneficiary.

The case was referred to the French Supreme Court, which confirmed the analysis of the Paris Court of Appeal insofar as it approved that its finding that such gains should be considered as salary as long as they were granted to managers because of their status of employee or corporate officer of the company. However, contradicting the Paris Court of Appeal, it considered that the basis for calculating the related social security contributions was the acquisition gain and not the capital gain on disposal. In turn, the Supreme Court remanded the case back to the Paris Court of Appeal, but made up of a different panel of judges. Should the decision be confirmed, it cannot be ruled out that this principle would apply to any kind of equity instrument awarded in the same circumstances as the ones at stake. The final outcome of this litigation will need to be monitored closely, considering its potential significant impact on the cost of management packages.

viii The PACTE law

Published on 23 May 2019, the PACTE law provides for a large set of rules intended to increase employees’ involvement in company decisions and achievements, notably by promoting employee share ownership, enhancing employee representation on boards of directors and supervisory boards and promoting employee profit-sharing and saving plans.

Promotion of employee share ownership

The conditions for the allocation of free shares have been simplified and broadened. In particular, the French Commercial Code limits the total number of free shares that could be granted by a company to its employees and managers to a maximum corresponding to 10 per cent of the share capital. Article 163 of the PACTE law provides that, for the purposes of this limit, free shares that have not been definitively allocated at the end of the vesting period, or those that are no longer subject to the retention obligation, are no longer taken into account (Article L 225-197-1 of the Commercial Code, amended). In addition, Articles 162 et seq. of the PACTE law support the development of employee share ownership by allowing, under certain conditions, the allocation of shares to employees in simplified joint-stock companies and by allowing employers to contribute unilaterally to employee share ownership funds.

Enhancement of employee representation on boards of directors and supervisory boards

The law provides for an increased number of employees on boards of directors and supervisory boards. More specifically, the boards of directors and supervisory boards of companies with more than 1,000 employees in France (including subsidiaries) or 5,000 employees in France and abroad (including subsidiaries) must include at least two employees when the number of non-employee board members exceeds eight (instead of 12) and at least one employee when the number of non-employee members is less than or equal to eight (instead of 12). In parallel, the scope of the exemption from the obligation to appoint employees within boards of directors and supervisory boards has reduced. In particular, public holding companies with less than 50 employees, which had so far been exempted from this obligation if one of their subsidiaries had appointed employees as board members, no longer are.
Promotion of employee profit-sharing and saving plans

Companies with fewer than 50 employees are exempted from the 20 per cent employer flat contribution on amounts paid for mandatory profit-sharing and voluntary profit-sharing, as well as on payments into an employee savings plan. Companies with 50 or more employees and less than 250 employees are also exempted from this contribution, but only on the amounts paid as voluntary profit-sharing. Such measures originated from parliamentary discussions about the PACTE law but were enacted in Law No. 2018-1203 of 22 December 2018 on the financing of social security for 2019.

VIII TAX LAW

i New mechanism to limit the deduction of interest expenses

The French finance law for 2019 carries out an overall reform of the deduction of interest expenses for companies subject to corporate income tax (CIT). The reform implements a general limitation on interest deduction to comply with the EU 2016 Anti-Tax Avoidance Directive (ATAD 1), under which Member States are required as a minimum standard to determine a threshold for deductibility of interest by reference to taxable earnings before interest, tax, depreciation and amortisation (EBITDA). These new rules are applicable for fiscal years opening as from 1 January 2019.

Article 34 of the French finance law for 2019 repeals the 25 per cent general reduction pursuant to the rabot mechanism as well as the Amendement Carrez limitation (an anti-abuse rule targeting acquisitions without substance), modifies the current thin capitalisation rules and incorporates them into the new limitation by lowering the applicable thresholds in the case of thin capitalisation (see below). However, the excessive interest rate rule for interest payments to related parties, the Amendement Charasse (an anti-abuse rule targeting acquisitions of shares of tax consolidated entities) and the French anti-hybrid provision still apply under the new rules.

The net borrowing costs within the scope of the new limitation are broadly defined as the excess of deductible financial expenses (after application of the above-mentioned excessive interest rate and anti-hybrid rules) over taxable financial income and other equivalent income received by a company. As under the rabot rule, financial income and expenses correspond to interest on all forms of debt, which can be sums left at the disposal of, or made available to or by, related or unrelated parties.

The new mechanism limits for non-thinly capitalised companies the deductibility of interest if and to the extent that the net borrowing costs of the concerned taxpayer exceed the higher of 30 per cent of its EBITDA and €3 million. A safe harbour rule applies for companies that belong to a consolidated group for financial accounting purposes: taxpayers are allowed to deduct an additional 75 per cent of the amount of net borrowing costs not allowed for deduction under the general limitation described above, provided that the ratio between their

16 Directive 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.
17 Article 39-1-3 of the FTC.
18 Article 223 B, paragraph 6 of the FTC.
19 Article 212-I-b of the FTC.
equity and their total assets is equal to or greater than the same ratio determined at the level of the consolidated group for financial account purposes to which they belong. As a tolerance measure also set out in ATAD 1, this condition is deemed to be met if the taxpayer’s ratio is lower than the group’s as a whole by a maximum of two percentage points.

The interest deduction threshold is reduced for thinly capitalised companies. The finance law provides for a new and wider definition of a thin capitalisation situation. While until now a situation of thin capitalisation was characterised when three different ratios were cumulatively exceeded (debt-to-equity ratio, adjusted earnings ratio and interest income ratio), a thin capitalisation situation is now only based on the excess of a single debt-to-equity ratio. Under the new deduction limit applicable in the case of thin capitalisation, the fraction of interest expenses related to indebtedness towards unrelated parties and indebtedness towards related parties up to one-and-a-half times the company’s net equity is deductible within the limits of the regular threshold (i.e., the higher of €3 million and 30 per cent of the company's EBITDA but reduced pro rata to the proportion of the corresponding debt over the total indebtedness of the taxpayer). The remaining portion of the net interest (i.e., related to indebtedness towards related parties exceeding one-and-a-half times the company’s net equity) is deductible within the limits of the reduced threshold, which is the higher of €1 million and 10 per cent of the company’s EBITDA (again reduced pro rata to the proportion of the corresponding debt over the total indebtedness of the taxpayer). A specific safe harbour provision allows a thinly capitalised company not to be subject to these reduced thresholds if the debt-to-equity ratio of such company is not higher, by more than two percentage points, than the debt-to-equity ratio of the consolidated group to which it belongs for financial account purposes.

The reform also provides for interest expenses and unused interest capacity carry forwards.

For taxpayers that are members of a French tax consolidated group, the rules apply at the level of the French tax consolidated group result. The applicable rules are broadly similar to those applicable to companies that are not members of a consolidated tax group. However, for thin capitalisation purposes, the above rules do not apply to interest paid between members of the same French tax consolidated group.

ii Modification of the tax consolidated group regime

The finance law for 2019 amends the French tax consolidated group regime, mostly to align this regime with EU principles.

Certain changes apply to the tax treatment of dividend payments. The 99 per cent exemption applicable under the French participation exemption regime between companies that are members of a French tax consolidated group (and also to dividends paid by eligible EU and EEA subsidiaries to members of a French tax consolidated group) is extended to dividends paid by eligible EU and EEA subsidiaries to a French company that is not a member of a tax consolidated group in cases where the French shareholder and the eligible EU or EEA subsidiary would have fulfilled the requirements to be members of a French tax consolidated group had the foreign subsidiary been located in France. Dividends paid between members of a French tax consolidated group that do not benefit from the parent–subsidiary regime are now exempted at the tax consolidated group level up to 99 per cent of their amount (they were totally exempt prior to the reform). In the same manner as for the dividends eligible for the parent–subsidiary exemption, this exemption is also extended to dividends paid by eligible EU and EEA subsidiaries to a French company that is not a
member of a tax consolidated group in cases where the French shareholder and the eligible EU or EEA subsidiary would have fulfilled the requirements to be members of a French tax consolidated group had the foreign subsidiary been located in France.

The reform also repeals the neutralisation at the French tax consolidated group level of the taxable portion of capital gains on share transfers eligible to the participation exemption regime, and debt waivers and subsidies granted between members of a French tax consolidated group. The taxable portion of capital gains on share transfers initially planned to be reduced to 5 per cent was eventually maintained at 12 per cent.

The finance law for 2019 legalises the ability to perform sales and provide services within the same French tax consolidated group for a price lower than the fair market value but at least equal to the cost price.

Finally, several mechanisms have been introduced to prevent the termination of existing French tax consolidated groups as a result of the Brexit by:

a postponing the closing of the fiscal year for the ineligibility of a French tax consolidated group or a group member triggered by the Brexit; and

b allowing without termination of the French tax consolidated group the substitution of a non-resident parent company by a foreign company directly or indirectly held by it, which fulfils the requirements to become a non-resident parent company.

Furthermore, the election by the parent company from one type of tax consolidation to another type (e.g., from a horizontal tax consolidated group to a vertical tax consolidated group) and the merger of the parent entity of a French tax consolidated group into another company of the same group no longer trigger the termination of the group, provided that certain conditions are met.

These new rules are applicable for fiscal years opened as from 1 January 2019 except for provisions concerning the termination of French tax consolidated groups that apply for fiscal years closed as from 31 December 2018.

### Calculation of the holding period of shares received by the contributor in a partial asset contribution

The finance law for 2019 provides for a new, favourable method for calculating the holding period for shares received by a transferring company in exchange for a contribution assimilated to a complete branch of activity (certain share-for-share transactions) and benefiting from the favourable rollover regime for French CIT purposes. A contributor is now deemed to have held new shares received as a result of a contribution as from the original acquisition date of the contributed shares by the contributor (i.e., the holding period is rolled over on the new shares received as a result of the contribution).

This is a welcomed change as until now, Article 210, B, 2 of the French Tax Code (FTC) only provided that capital gains relating to shares received in exchange for a contribution were calculated by reference to the value of shares in the transferring company accounts, but no legal disposition of the FTC indicated that the holding period of the shares received by the contributor was also rolled over. This point had become crucial given that the finance law for 2018 had repealed the former requirement to hold shares received in exchange for a contribution for three years in order to benefit from the favourable CIT regime, and the French participation exemption regime for capital gains is conditioned to a two-year holding period of the eligible shareholdings.

This change applies for fiscal years closed as from 31 December 2018.
iv Introduction of a general anti-abuse rule for CIT purposes

A new anti-abuse rule for CIT purposes is applicable for fiscal years beginning on or after 1 January 2019. The new Article 205 A of the FTC implements into French law the general anti-abuse disposition of ATAD 1.

The wording of this new anti-abuse clause replicates the wording of the general anti-abuse clause of Article 6 of ATAD 1. Consequently, an arrangement or a series of arrangements that, having been put into place for the main purpose, or as one of the main purposes, of obtaining a tax advantage, defeats the object or purpose of the applicable tax law, are not genuine, and thus will not be taken into account for tax purposes.

Contrary to the general abuse of law regime provided by Article L.64 of the French Book of Tax Procedures, there are no automatic penalties attached to the anti-abuse clause of Article 205 A of the FTC.

The new clause is not intended to replace other current anti-abuse mechanisms but will exist in addition to them.

IX COMPETITION LAW

The French Competition Authority has had responsibility for merger control since 2009, and has increasingly adopted a more efficient approach to the application of its rules. In 2018, 235 concentrations were reviewed and cleared by the Authority, five of which were cleared conditionally (that is, with remedies or injunctions).

It is also important to note that for the first time, the Minister of Economy made use of his power to evoke a case. Subsequent to an in-depth examination, the Competition Authority had cleared Cofigeo’s acquisition of securities and assets of the ready meal branch of Agripole20 subject to the divestment of both a production site and a brand. Without such injunctions, not only would Cofigeo become the undisputed leader in most of the relevant markets, but it would also own all the best-known brands in the sector. The remedies, therefore, aimed at preventing the price increase regarding essential goods.

The Minister of Economy made use of his power to evoke a case no later than on the day the Competition Authority’s decision was issued. This power enables the Minister of Economy to decide on a concern operation on the basis of public interests (other than the protection of competition), such as industrial developments or the stability of employment. The Minister highlighted that the target company was facing severe financial difficulties and that Cofigeo was an important job provider in a difficult employment area. The transfer of assets ordered by the Competition Authority would have exposed Cofiego and its employees to insolvency.

As a resultant, the Competition Authority’s decision will not be implemented and shall be replaced by that of the Minister of Economy.

i Application of the merger control guidelines of 10 July 2013

On 10 July 2013, new guidelines on merger control were adopted by the Competition Authority, revising the previous guidelines of December 2009 and taking into account the Authority’s experience since.

The guidelines on merger control set out measures aimed at facilitating the pre-notification process, specifying the criteria for the simplified notification procedure,

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20 Case No. 18-DCC-95.
the conceptual framework of the analysis of relevant markets and the role of this analysis, and proposing standard models for transfers of assets and trustee mandates. The guidelines also place greater emphasis on economic and econometric analysis, especially quantitative tests, when the data and methodology used are reliable and verifiable. In particular, the new guidelines introduce a reference to the upward pricing pressure, illustrative price rise and gross upward pricing pressure index (GUPPI) tests, used to measure the impact of a merger on prices without having to define the relevant market.

The GUPPI test was last used by the Competition Authority in its decision of 27 July 2016 authorising the acquisition of the Darty company by the Fnac group. In this decision, the Authority, for the first time in France and Europe, considered the market for the retail distribution of certain domestic electronic products to include both online and in-store sales. The Authority then based its analysis of the horizontal effects on the GUPPI test to conclude that a post-merger price increase by the new entity was likely. The Authority also noted that the transaction would lead to a risk of stores not being incentivised to propose price discounts or punctual promotions that would likely enhance local competition. To meet the identified concerns, the Fnac group has committed to divest six stores to one or more retailers of electronic products. Consequently, the Authority cleared the acquisition, considering that this divestiture will guarantee sufficient competition in the market of retail distribution of electronic products in Paris and its suburbs.

It should be noted that the French Competition Authority is currently reflecting upon a revision of its merger control guidelines. Such revision aims at incorporating recent case law developments regarding decision-making practices into the existing soft law rules governing the analysis of merger operations. Following the consultation of interested third parties, the Competition Authority has announced the adoption of new guidelines during the course of 2019.

ii Substantial penalties for gun-jumping

When French thresholds are met, a pre-merger filing is mandatory. This applies to all concentrations, including foreign-to-foreign transactions, even in the absence of an overlap between parties’ activities.

Individuals and companies acquiring control of all or part of an undertaking are responsible for notifying. In the case of a merger, this obligation is incumbent upon the merging entities. In the case of a joint venture, parent companies must file a joint notification.

Sanctions for not filing or for closing before clearance are as follows:

- corporate entities: up to 5 per cent of the turnover in France during the previous financial year (plus, where applicable, that of the acquired part generated in France); and
- individuals: up to €1.5 million.

An example of a sanction for the first type of gun-jumping (i.e., for failing to notify) can be found in case No. 13-D-22. On 26 December 2013, the Competition Authority imposed a fine of €4 million on Castel Frères, a company active in the wine sector, for failing to notify its acquisition of six companies before closing the transaction on 6 May 2011. It was only in...
September 2011, in the context of the examination of another acquisition, that this merger was reported to the Authority by a third party. On appeal, the fine was reduced to €3 million on the grounds that the transaction was notified shortly after the Authority’s request and that Castel Frères did not intend to bypass the competition rules.\(^{23}\)

Regarding the second type of sanction for premature implementation, the Competition Authority imposed a fine for a breach of the standstill obligation for the first time in 2016. In 2014, Altice, active in the French telecom market through its subsidiary Numericable, notified the planned acquisition of SFR and OTL, which was authorised by the Authority in October 2014. In April 2015, the Authority conducted a dawn raid on the premises of Numericable, SFR and OTL, and found evidence that Altice was involved in SFR’s business and strategy prior to clearance, notably in approving the participation of SFR in a public tender, assisting SFR in renegotiating a network sharing agreement with Bouygues Telecom, determining the prices of SFR internet retail offers and coordinating with SFR in the context of OTL’s acquisition. As a result, on 8 November 2016, the Competition Authority imposed a fine of €80 million on Altice Group for implementing two transactions prior to obtaining merger control clearance.\(^{24}\) This is one of the highest fines worldwide ever enforced for such a practice.

Finally, parties may be required, subject to a periodic penalty for non-compliance, either to file a concentration or to demerge. Transactions that have been completed without clearance are illegal and not enforceable. There are no criminal sanctions for not filing.

### Diversification of remedies that can be imposed by the Competition Authority

Regarding commitments and injunctions, in its new merger control guidelines the Competition Authority provides several examples of its decision-making practice, which is characterised by a preference for structural remedies (e.g., divestment of minority shareholdings). However, in the case of complex transactions, the Authority pragmatically accepts behavioural remedies, of which it provides several examples. Merger review over the past few years tends to confirm such trend. For instance, in 2016, in five cases out of six, the Authority conditioned its approval only on behavioural remedies. However, 2018 was a more balanced year, as in half of its cases, the Authority cleared transactions subject to structural remedies,\(^{25}\) and conditioned its approval only on behavioural remedies for the other half.

Recently, the French Competition Authority accepted fix-it-first commitments so as to remedy the anticompetitive effects of the acquisition of Alsa by Dr Oetker (Ancel).\(^{27}\) Within the market for fabrication and marketing of dessert mixes to supermarkets and hypermarkets, the Competition Authority identified the risk of a price increase following the completion of the transaction as well as a lack of credible alternative suppliers. The Competition Authority addressed in advance the aforementioned competition concerns and granted Dr Oetker

\(^{23}\) Judgment of the Supreme Administrative Court dated 15 April 2016, appeal No. 375658.

\(^{24}\) Situation of the Altice group with regard to Section II of Article L 430-8, decision dated 8 November 2016, case No. 16-D-24.

\(^{25}\) Acquisition of Zormat, Les Chênes and Puech Eco by Carrefour Supermarchés France, decision dated 27 April 2018, case No. 18-DCC-65; acquisition of Jardiland by InVivo Retail, decision dated 24 August 21018, case No. 18-DCC-148.

\(^{26}\) Acquisition of SDRO and Robert II by Groupe Bernard Hayot, decision dated 23 August 2018, case No. 18-DCC-142; creation of a full-function joint-venture between Global Blue and Planet Payment, decision dated 28 December 2018, case No. 18-DCC-235.

\(^{27}\) Case 19-DCC-15.
approval to enter a trademark licensing agreement for Ancel mixes for a duration of five years, renewable once. Thereafter, the licence would be conceded to Sainte Lucie, which is active in a distinct market, namely the market for fabrication and marketing of baking aids to supermarkets and hypermarkets. Sainte Lucie’s consistent growth in the past few years served to assure the Competition Authority of a credible alternative in the relevant market.

It is important to note that the Competition Authority carefully monitors the implementation of remedies, and may withdraw an authorisation in cases of non-compliance. In such a case, the parties will then have to either restore the situation to what it was before the transaction (i.e., unwind the operation) or re-notify the transaction to the Competition Authority within a month. Compliance with commitments by companies is central to the process of French merger control. The power of the Authority to withdraw merger approvals was validated in 2012 by a decision of the French Constitutional Court in the context of the appeal by Canal Plus and Vivendi against an order to re-notify the purchase of its former rival TPS. The Authority withdrew its approval on the ground that Canal Plus Group did not fulfil several commitments that were attached to the authorisation decision.

If such non-compliance with remedies is confirmed, the Competition Authority is also able to impose financial penalties on the notifying parties of up to 5 per cent of their net turnover achieved in France. In this regard, in 2018, the Competition Authority fined the Fnac and Darty Group €20 million for non-compliance with commitments made when Darty was taken over by Fnac.

**iv Contemplated changes in the French merger control regime**

The Competition Authority launched an initiative on 20 October 2017 to modernise and simplify the merger law. The topics proposed for consideration included, among others, the simplification of merger procedures (especially the current simplified procedure) and the introduction of limited *ex post* control by the Competition Authority or the reintroduction of a market share threshold.

On 25 April 2019, a decree was issued regarding the simplification of merger procedures: namely, the notification procedure has been streamlined. Parties are only required to submit one copy of the notification notice instead of four material copies. Additionally, the threshold from which a market is considered to be affected for the analysis of vertical effects was raised from 25 to 30 per cent. The decree also simplifies the summary tables of the financial data of the companies concerned.

The French Competition Authority’s reflection on limited *ex post* control is ongoing. To date, the Authority contemplates an *ex post* control system for concentrations that do not fall within the Commission’s jurisdiction but that present substantial competition concerns in France. The Authority is considering a time limit of between six months and two years at the end of which an *ex post* intervention would no longer be possible; and a cumulative worldwide total turnover excluding VAT of those companies exceeding a certain threshold (for example, the current threshold €150 million).

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28 Case No. 2012-280 further to a request for a preliminary ruling on a question of constitutionality.
29 Case No. 18-D-16.
France

X OUTLOOK

On 19 March 2019, the European Union adopted Regulation 2019/452, which establishes a framework for the screening of foreign direct investment into the Union. This new Regulation, which will apply as from 11 October 2020, aims to encourage cooperation and information-sharing between Member States and the European Commission where a foreign direct investment in one Member State is likely to affect the security or public order of other Member States.

It does not establish any centralised screening mechanism at an EU level under which an EU body would make the final decision on foreign investments. However, this new Regulation confirms the power granted to each Member State to implement a foreign investment control regime that may notably consider the effect of a contemplated investment on critical infrastructure (e.g., defence, electoral or financial infrastructure), on critical technologies or on the freedom of the press and media plurality.

More significantly, the new Regulation sets forth a cooperation mechanism in relation to foreign direct investments undergoing screening. Each Member State shall inform the European Commission and the other Member States as soon as possible when foreign investments are subject to a control procedure on its territory. The other Member States may then send comments to the Member State in which an investment is contemplated if they consider that such foreign investment is likely to affect its security or public order or if they have information relevant to such investment. At the request of a Member State or on its own initiative, the Commission may issue an opinion, and must issue such opinion when at least one-third of Member States consider that a foreign investment is likely to affect their security or public order. The Commission and Member States shall issue their comments and opinions within a reasonable period of time, and no later than 35 calendar days following receipt of the notification made by the Member State in which the investment is planned. The Member State conducting the screening of the related foreign investment shall give due consideration to the comments of the other Member States and to the Commission’s opinion.

Even though the Members States will retain the ultimate decision-making power in this respect, this new EU Regulation can be expected to add a layer of complexity to the review process and potentially impact approval timelines in the future.
Chapter 19

GERMANY

Heinrich Knepper¹

I OVERVIEW OF M&A ACTIVITY

2018 was, seen globally, a very good year for the M&A market, with aggregate volumes of M&A deals reaching an estimated US$3.5 trillion, an increase in comparison to 2007 of almost 12 per cent. According to Merger Market, 2018 was thus the third-biggest year in terms of volumes and the second-highest in average deal sizes. Global buyout activity reached US$557 billion, the highest total in a decade and 3.7 per cent more than 2017 (US$537 billion). M&A deals driven by private equity or financial investors or sponsors who exited their investment reached the second-highest number of deals on record, registering 2,450 exit transactions compared to a peak of 2,592 in 2017.

The value of European M&A also reached a post-crisis high (US$989.2 billion) in 2018, which was also the highest share of global M&A (28 per cent) by value since 2014. However, it was a year of two halves: the first six months were very strong followed by an increasingly difficult environment, which caused the market to stall notably in the second six months.

Although Europe experienced 11 megadeals (greater than US$10 billion) in 2018, four more than throughout 2017, all of them had been announced by May. Firms have been forced to reconsider high-profile investments through a combination of rising protectionism, government intervention and continued uncertainty. Just 10 deals in excess of US$5 billion were recorded in H2. These included Hitachi’s US$9.4 billion acquisition of ABB’s power grids business and the US$7.1 billion Calsonic Kansei/Magneti Marelli deal. Concerned by the activity slowdown in H2, dealmakers are anxious about whether 2019 will see a return of the buoyant levels of recent years.

Brexit was a major factor. The protracted uncertainty about the UK’s future relationship with the rest of the EU caused a market slowdown in M&A activity. This was acutely felt in the final quarter of the year as Theresa May faced battles on all sides of Parliament once her deal with the EU had been agreed.

The German M&A market (looking at transactions involving at least one significant German participant as buyer, seller or target) stalled or slightly dropped. Still, the German M&A market in 2018 ranked second in Europe after the UK. The clearly dominant transactions, both in Q1 and Q2, were the reorganisation of the German energy market caused by the acquisition of Innogy SE by EON, which accounted for more than one-third of the total 2018 deal value, and Vodafone’s takeover of Liberty Global’s assets in Germany and

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CEE. After a very strong beginning, increasing uncertainty led to a decline in market activity in Germany in the second half of the year, with deal values of US$15 billion and 8.5 billion, respectively, in Q3 and Q4.

Nevertheless, a number of high-profile M&A deals were seen in the past year. The single most notable M&A transaction with German involvement was the acquisition by E.ON SE of Innogy SE with a deal volume of approximately €38 billion, combined with a swap of assets between E.ON and the previous majority owner of Innogy, RWE. Further top ten German deals included:

a the acquisition by Vodafone plc of the German and Central European cable business of UnityMedia (including UnityMedia Hungary, Romania, Germany and the Czech Republic) from Liberty, for a total purchase price of €18.4 billion; the acquisition by SAP SE of Qualtrics, LLC from its previous (private equity) owners;
b the acquisition by Gebrüder Knauf Verwaltungsgesellschaft KG of USG Corporation for a purchase price of €5.3 billion;
c the sale by Macquarie of its participation in Techem GmbH, one of the German market leaders in usage tracking devices for households (in particular heating meters) for €4.6 billion;
d the acquisition by Procter & Gamble of the consumer health business from Merck KGaA (with a purchase price of €3.4 billion);
e the acquisition by Temasek Holdings BTE of a minority stake in Bayer AG (purchase price: €3 billion);
f the sale by Kühne Holding AG of its majority stake in VTG to Morgan Stanley Infrastructure Inc (€2.3 billion); and
g the acquisition by EQT Partners AB of Suse Linux GmbH from Microfocus International plc.

Given the sheer size of the single largest German M&A transaction (which was at the same time the third-largest M&A transaction worldwide), that is, the acquisition by E.ON of Innogy, the energy, mining and utilities sector was the most targeted sector by value. This takeover, creating one of the biggest energy utilities with a strong focus on renewable energies, demonstrated the global shift towards cleaner and more efficient energy business. The deal will see E.ON focus on driving sales by growing its supply and networks coverage, while RWE will consolidate its power generation assets and build its renewable capacity.

The total number of initial public offerings (IPOs) in Germany in 2018 in the prime standard segment of the German stock exchanges doubled in comparison to 2017 to a total of 16, thereby reaching their highest number since the outbreak of the financial crisis in 2007. The volume of IPOs increased as well, tripling to almost €12 billion (in 2017: approximately €3 billion). The main drivers for this positive development were the IPOs of Siemens Healthineers, Knorr-Bremse and DWS that, with a total aggregate IPO volume of €9.5 billion, accounted for more than 80 per cent of the total volume. Siemens Healthineers, with an IPO volume of €4.5 billion, achieved the single biggest IPO in Europe.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The main source of regulation for public takeovers in Germany is the Takeover Act, as amended in 2006 to implement the EU Takeover Directive, as well as the German Stock Corporation Act, which provides the general framework of the corporate legislation pertaining to German
Germany

stock corporations. In addition, provisions of the German Securities Trading Act, including provisions on the disclosure of holdings of listed securities and certain other instruments, are relevant in connection with any public takeover relating to German target companies (or, in some respects, companies with securities that are listed at a German stock exchange).

Further provisions relevant for the implementation of a public takeover and potential further steps after the completion of a takeover are set out in the German Act on Corporate Transformation, the Stock Exchange Act, the Offering Prospectus Act and the Commercial Code.

The Takeover Act creates a comprehensive legal framework that enables public takeovers to be conducted fairly and transparently. The Takeover Act is also designed to protect the financial interests of minority shareholders and employees of target companies. It contains, inter alia, provisions dealing with takeover bids and mandatory bids, including provisions on pricing and procedure, and requirements in relation to the contents of offer documents.

The Takeover Act also provides a specific squeeze-out procedure following a successful takeover bid (in addition to the general squeeze-out provisions under the Stock Corporation Act and the squeeze-out provisions under the Act on Corporate Transformations) and a right of sell out for minority shareholders following a successful takeover bid.

Pursuant to the Takeover Act, the Federal Ministry of Finance has adopted a number of regulations, one of which contains important provisions governing the contents of an offer document, the consideration payable in a takeover bid and exemptions from the obligation to make a compulsory offer.

In implementing the EU Takeover Directive, Germany has taken a minimalist approach, changing the existing German Takeover Act only to the extent necessary. In particular, Germany has opted out of the strict provisions of the Takeover Directive on frustrating actions that would have made such actions in hostile takeover scenarios generally subject to shareholder approval. Germany has also opted out of the breakthrough rule under the Takeover Directive that would have resulted in setting aside certain transfer restrictions and voting agreements during a takeover bid. The German non-frustration rules allow a target to take any action, including a frustrating action, with the consent of its supervisory board. However, it is generally acknowledged that in giving its consent, the supervisory board is bound to authorise a frustrating action in a takeover situation only if the benefit for the company of implementing the action clearly outweighs the interests of the shareholders.

Although the stricter prohibitions of defensive measures and the breakthrough rules under the Takeover Directive could be opted in by German publicly listed companies, this possibility has not been used by any of the larger German corporates.

The Stock Corporation Act contains provisions relevant for all German stock corporations (both public and private), including:

*a* provisions relevant to public and private takeovers of stock corporations;

*b* provisions relating to the implementation of permissible defences that can be employed against hostile public takeovers;

*c* provisions on the squeeze-out of minority shareholders by a majority shareholder (both in the case of publicly listed and private stock corporations) by a shareholder who has achieved 95 per cent or more of the shares of the corporation.

The Securities Trading Act contains provisions relating to reporting requirements for significant shareholdings and reporting obligations for listed companies regarding major new business developments; these reporting requirements for major shareholdings have
been significantly extended since 2011 to include reporting obligations for holders of other instruments linked to shares. On the other hand, the areas of insider dealing and market manipulation, which were addressed previously in the Securities Trading Act as well, are now regulated on a European level on the basis of the Market Abuse Regulation (MAR); see Section III.i.

The Act on Corporate Transformations contains the mechanics for a process of statutory mergers between two German companies, which can be an alternative to a takeover offer. It also contains the most important provisions regarding corporate restructurings that could be relevant in the post-closing phase both for public and private acquisitions, including, since 2011, provisions allowing the majority shareholder of a stock corporation (which itself has to be a stock corporation holding at least 90 per cent of the registered share capital of the target company) to squeeze out the remaining minority of up to 10 per cent by implementing a merger between the target and the shareholder (for the shareholder as surviving corporation).

The Stock Exchange Act and the Offering Prospectus Act set out the rules dealing with prospectus requirements applicable when issuing new shares as consideration for a takeover offer.

The Commercial Code provides for extensive disclosure obligations for publicly listed companies in respect of:

- the structure of their share capital;
- the statutory provisions and provisions under a company’s articles on the nomination and dismissal of members of the supervisory and management boards; and
- certain categories of agreements or matters that may frustrate a takeover offer, including agreements among shareholders on the exercise of voting rights and the transfer of shares (to the extent that these agreements are known to the management board), and material agreements of a company providing for a change of control clause.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i EU Market Abuse Regulation

A notable change to the capital markets laws that has had a significant effect on M&A transactions on a number of levels is related to the immediate applicability in all EU Member States of the Market Abuse Regulation (MAR), effective as of 3 July 2016. The provisions of the MAR have replaced a number of capital markets regulations of individual Member States and, in many cases, significantly increase and strengthen compliance obligations. In particular, any issuers with securities that are traded, at the initiative of the issuer, in the regulated unofficial markets, will in the future be subject to obligations to disclose inside information ad hoc, to maintain insider lists and to comply with regulations on directors’ dealings. In addition, rules restricting insider dealings and market manipulations will be significantly more strict, and potential sanctions in the case of infringements will be strengthened and more severe.

Two years after the coming into effect of the MAR, the assessment of its impact has yielded mixed results, and the Regulation itself as well as its application by the German...
regulator have also drawn significant criticism. According to a recent survey, the MAR has in fact not yet led to greater legal certainty, but has instead decreased clarity in areas such as \textit{ad hoc} disclosure duties. At the same time, while the bureaucratic hurdles faced by issuers have grown, investor protection has not improved.

The complicated \textit{ad hoc} rules not only cause uncertainty among companies in the mid to long-term, but could also develop into a considerable disadvantage for Germany as a jurisdiction in which to undertake M&A transactions.

If companies postpone \textit{ad hoc} disclosure early on as a precautionary measure, then they must simultaneously ensure that insiders no longer trade in the relevant securities. At an early stage, however, not all members of the management and supervisory boards are routinely informed. In practice, postponement can usually only be maintained for a short time.

In a fiercely competitive M&A environment, the rules result in a clear disadvantage for listed companies. Privately held companies or companies from non-EU jurisdictions with more business-friendly rules, on the other hand, can exploit advantages in an M&A situation.

\textbf{ii German Investment Code}

In 2013, the German legislator enacted the German Investment Code (GIC), which implemented the Alternative Investment Fund Managers Directive (AIFMD). The GIC applies, inter alia, to managers of alternative investment funds (AIFs) (including private equity funds) and aims to reduce the risks posed by AIF managers (AIFMs) to the financial system by introducing various mandatory disclosure, corporate governance, liquidity management and other requirements. In accordance with the AIFMD, the GIC contains certain \textit{de minimis} provisions under which AIFMs managing AIFs below certain thresholds are exempted from full application of the GIC and are subject only to a registration rather than a licensing requirement.

Certain elements of the GIC are of relevance to private equity investors. In particular, the GIC contains a requirement for AIFMs to hold a minimum amount of capital (Section 25). For an internally managed AIF (i.e., when the management functions are performed by the governing body or any other internal manager of the fund), the minimum level is €300,000; however, for an AIFM that is an external manager to an AIF (or AIFs), it is €125,000. In addition, if the value of the portfolios under management exceeds €250 million, the AIFM must provide its own funds equal to 0.02 per cent of the amount in excess of €250 million. This additional capital requirement is capped at €10 million. The GIC also imposes wide-ranging disclosure obligations on AIFMs. For example, managers are required to make regular disclosures to investors, including an annual report and numerous additional disclosures, such as details of investment strategy, liquidity and risks, and the use of leverage. In addition to these disclosures to investors, managers are required to disclose to the relevant authorities details of major shareholdings in non-listed (as well as listed) companies, if these holdings exceed or fall below thresholds of 10, 20, 30, 50 and 75 per cent (Section 289). These disclosure obligations are particularly onerous for private equity investors.

\footnote{Source: survey conducted by Hengeler Mueller Partnerschaft von Rechtsanwälten mbB and Deutsches Aktieninstitut, an association that represents the interests of publicly traded companies, banks, stock exchanges and investors.}

The GIC also provides for a restriction on asset stripping where a private equity fund subject to regulation under the GIC has acquired control over an unlisted company or over an issuer. In particular, independent from the specific legal form of a target, any amounts available for distribution must always be determined on the basis of the annual accounts of the immediately preceding fiscal year. In the case of targets in the form of a limited liability company (the most frequent corporate form in Germany), it remains unclear (and it has so far not been decided by any court) if these restrictions impose restrictions on capital or dividend distributions in addition to the statutory restrictions under the Limited Liability Company Act, in particular the capital maintenance rules. Furthermore, the GIC restricts the repurchase of own shares by a target acquired by a fund regulated pursuant to the GIC.

iii Foreign Trade and Payments Ordinance

The Foreign Trade and Payments Ordinance governs foreign direct investment (FDI) control in Germany. Generally, acquisitions of 25 per cent or more of the voting rights of a German company by non-European Economic Area investors are subject to foreign investment control by the Federal Ministry for Economic Affairs and Energy. Under new legislation introduced in December 2018, this threshold has been lowered to include minority acquisitions of at least 10 per cent if the target company operates in the area of critical infrastructure and related technology or manufactures certain military-related products or technology. The government had already broadened the scope of FDI control in July 2017 when it introduced a filing obligation for investments in the area of critical infrastructure and doubled the applicable review period. Despite these amendments, certain cases raised national security concerns, but were outside the scope of German FDI control because the investor did not reach the 25 per cent threshold. One such notable case was an attempt by a Chinese investor to acquire a minority stake in German power transmission network operator 50Hertz. Against this background, lowering the jurisdictional threshold to 10 per cent was seen as the government’s reaction to a hike in foreign acquisitions in certain sensitive sectors in Germany.

In conjunction with tighter FDI controls around the world, cross-border transactions may require separate FDI reviews in more than one jurisdiction. Currently, it is too early to make an assessment of the practical impact of the increased supervision. It is generally noted, however, that this corresponds to a global tendency towards protectionism, aimed (not explicitly, but nevertheless clearly) against attempts of Chinese companies (in particular state-owned enterprises) to gain footholds in Western key industrial sectors.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Germany continues to be one of the most attractive target jurisdictions in Europe, with 478 inbound transactions in 2018 (France: 287, Italy: 264, Netherlands: 259). Only the UK attracted more inbound deals, with 672 transactions in 2018.6

Outbound activity of German buyers acquiring target companies or businesses outside Germany dropped once again by about 52 per cent from US$77 billion in 2017 to US$37 billion in 2018.7

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6 Source: Merger Market, Deals with any German involvement.
7 Source: Merger Market – German outbound deals.
V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Significant transactions
The single most significant German M&A transaction was the acquisition of Innogy, which occurred only a few years after the spin-off of the renewables energy business from RWE to Innogy, thus creating the by-far largest utility company in Germany and one of the biggest players in renewable energies Europe-wide. Other significant transactions also involved energy, and in particular the renewable energy sector. Most notably, Copenhagen Infrastructure Partners sold its equity and mezzanine loan stake in Veja Mate, a German offshore wind park. Due to considerable challenges to the German utility industry following the government’s decision to exit both coal energy generation and nuclear energy, it is to be expected that, as the sector of renewable energies grows and diversifies, significant M&A transactions will remain in the pipeline.

Another significant transaction was the acquisition by Vodafone of Unity Media in Germany and Central Europe. For Germany, this transaction marked another round of the consolidation of the German telecoms and media cable network. The increasing efforts of German industry players and the government to promote Industry 4.0 and the expected introduction in Germany of the 5G network, following the announced auction of the relevant licences, is expected to spur further M&A activity in the telecoms and media sector.

ii Key trends
The reinstatement of US sanctions against Iran garnered much attention in 2018. For M&A markets, as well as for the financing of acquisitions, it is in the divergence between US and EU sanction policies, best reflected in their approaches to Iran, where the EU continues to try to salvage the deal that led to the relaxation of sanctions while the US reimposes sanctions. Many companies wish to trade freely worldwide, but where this is impeded, they desire certainty as to where they can trade without sanctions being imposed.

With the US sanctions having the effect that most trade by European companies with Iran risks the imposition of sanctions, and the EU legislating to seek to prevent European business changing their behaviour to comply with US sanctions, businesses often face a difficult choice between (potentially) losing access to the US markets and building business with country targets of US sanctions. Any weakening of EU and US relations over the coming years may well be reflected in the sanctions sphere with further divergence in other sanction programmes, such as the sanctions against Russia.

The unresolved situation regarding Brexit continues to make itself felt also in the M&A market and the market for acquisition financings, with many participants fearing that a drift between UK and Europe, including a drift between the applicable laws, may impede the globalisation of the M&A market and acquisition financing market, and lead to a fragmentation and regionalisation of these markets.

It is generally expected that the general slowdown of economic activity in Germany and the eurozone in general may result in increased numbers of restructurings, distressed financings and distressed M&A transactions in the near future. In the years following the

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8 A national strategic initiative of the government that aims to drive digital manufacturing forward by increasing digitisation and the interconnection of products, value chains and business models. It also aims to support research, the networking of industry partners and standardisation: https://ec.europa.eu/growth/tools-databases/dem/monitor/sites/default/files/DTM_Industrie%204.0.pdf.
immediate aftermath of the financial crisis, total numbers of restructurings and distressed financing cases decreased, partly (as is believed) as a result of the high availability of (relatively cheap) financing. An increased volatility in financial markets, the potential uptake of inflation and, as a result, increased financing costs, are expected to increase the number of restructurings as well as insolvencies in particular in Germany.

iii Hot industries

The automotive industry, still the most important traditional industry in Germany, has remained in the focus also of M&A activities and is expected to generate significant additional M&A activity in the future. Worldwide, the automotive industry has increased investment in electro mobility and automated driving; very often, this investment takes the form of the acquisition of start-up companies. At the same time, due to the receding significance of traditional petrol and fuel motors, the automobile industry is in parts expected to significantly shrink and to divest. Finally, also due to the challenges faced by the automotive industry, combined with the slowdown in economic activity in the eurozone and Germany in particular, it is expected that the number of restructurings, and thus the potential for distressed M&A transactions, will increase specifically in the automotive and automotive supplier industry.

In addition, the energy sector is expected to remain one of the most active fields in the M&A sector, partly due to the switch in Germany from both coal and nuclear power stations to renewables.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

The availability of M&A-related financing generally continued to be strong in 2018, given the still very low interest environment and competition for banks from alternative lenders such as debt funds on leveraged buyouts.

However, after years of nearly uninterrupted strength, the credit markets have shown volatility and signs of weakness recently. As a result, many acquirers seeking to finance their M&A deals in the debt markets have faced challenges rarely seen in recent years.

Different financing sources may have markedly different views of the risk that any particular financing transaction presents, and as a result may offer significantly divergent terms. Even in normal times, financial institutions (and particularly different types of financial institutions: money-centre commercial banks, investment banks or alternative lenders) have different risk tolerances, but recent volatility and unpredictability in the financing markets have resulted in greater differentiation in the terms that individual financing sources are willing to offer potential borrowers.

The Euro Overnight Index Average (Eonia) and the Euro Interbank Offered Rate (Euribor) are about to be either replaced or transformed, because neither complies with the recently introduced EU Benchmarks Regulation (BMR).

Euribor and Eonia are critically important interest rate benchmarks for the eurozone. The race is on to reform Euribor so that it complies before the BMR authorisation deadline of 1 January 2020. No attempt will be made to reform Eonia, however, and transition to a new overnight reference rate will be required.
European authorities have established an industry working group tasked with recommending alternative euro risk-free rates and a plan for adopting them. The European Central Bank is simultaneously developing Euro Short-Term Rate (ESTER), a new euro unsecured overnight interest rate, a possible alternative to Eonia and, potentially, to Euribor.

While regulators are supportive of the Euribor reform process, its success is not guaranteed. There are scenarios where the volume of transactions in the market that Euribor is meant to reflect prove insufficient even for a hybrid methodology. This could leave industry needing to adopt (as yet, undefined) new reference rates for new business from as early as January 2020.

Capital markets, in particular the high yield bond market in Germany, has remained at a relatively low level. Only a few German-domiciled or headquartered issuers tried to tap the high yield bond market, and some of them turned directly to the more liquid US market.

As a result of the impending Brexit (and the uncertainties around the immediate and long-term consequences of Brexit), financing banks and other lenders have become increasingly aware of the potential risks involving the choice of English law for financing transactions. So far, the vast majority of syndicated financing in Europe is still expressed to be governed by English law. However, unless the EU and the United Kingdom agree otherwise, court decisions rendered in the United Kingdom will, once the United Kingdom has effectively left the EU, no longer enjoy the benefit of direct enforceability under the EU Regulation9 on jurisdiction and the recognition and enforcement of judgments in civil commercial matters (repast). Increasingly, financial players are therefore looking at potential alternatives to English law as the governing law for financial products. Increasingly, in particular in smaller or mid-size transactions with a limited number of syndicate members, German law and German court jurisdiction are chosen in financing contracts.

VII EMPLOYMENT LAW

The most notable developments in German employment law in 2018 that may be of relevance in an M&A context essentially concern temporary agency workers, business transfers and the minimum wage. Additionally, in May 2018, the EU General Data Protection Regulation entered into force, further tightening the rules on data processing and imposing additional information and documentation requirements on employers.

i Temporary agency workers

In the aftermath of the 2017 fundamental amendments to the German Act on Temporary Agency Work (2017 Act), 2018 was a year of consolidation, characterised by court decisions, mostly those of local and regional courts, aiming to clarify and sharpen the interpretation of the new law. A number of these issues are pending on appeal before the federal courts. Key questions at issue relate to the counting of agency workers regarding statutory law thresholds, equal pay and duties to offer actual employment to agency workers.

As per the 2017 Act, agency workers count towards the thresholds for co-determination and works constitution purposes, provided that their term of service in an establishment exceeds six months. It remains unclear whether length of service has to be determined individually for each agency worker, or whether the relevant factor is that a given job has

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been occupied by (one or several consecutive) agency workers for a time period exceeding six months. Recent lower and regional court decisions have taken different positions on the issue.

On a related issue, courts at both the local and regional levels have held that the cancellation of contracts for agency work does not count towards the number of terminations required to constitute an operational change within the meaning of Section 111 of the German Works Constitution Act. Their key argument is that agency workers do not form part of the workforce of the hirer for the purposes of such norm, since the termination of a contract between a hirer and an agency does not make the agency worker lose its employer. Whether this will be upheld by the Federal Labour Court remains to be seen. The Federal Labour Court, on the other hand, has requested a preliminary ruling by the European Court of Justice (ECJ) on whether agency workers count towards the thresholds relative to mass redundancy proceedings. A decision thereon will likely also impact the operational change issue.

Another key contested subject is equal pay: principally, this has to be provided to an agency worker from the outset of his or her engagement by a hirer. Collective bargaining agreements (CBAs) may provide for postponement for up to nine or, under limited circumstances, up to 15 months. Employers not bound by CBAs may adopt the rules of regional CBAs for their industry, for example by reference to employment agreements. A challenge to such exemption as being in violation of the EU Directive on Agency Work has recently been rejected by a regional labour court. However, until decided by the ECJ, this will remain a source of uncertainty. Another contested item in this context is what elements count towards equal pay. The Federal Social Court has ruled that only compensation payments in the strict sense count, whereas payments compensating for costs incurred by an agency worker in connection with his or her engagement (e.g., travel cost reimbursements) do not. Nevertheless, many aspects of what exactly constitutes equal pay remain unclear. Finally, in this context, it is worth noting that per precedent by the Federal Labour Court, the results of social security audits conducted at an employer may be amended to his or her detriment if a different assessment is subsequently mandated, for example in light of a new precedent. The decided case concerned an agency that had to pay substantially higher contributions after a CBA applied by it had been declared void in court.

Under the 2017 Act, a general 18-month limit on the use of individual temporary agency workers by a hirer applies. Longer maximum terms may be permitted by CBAs, or indirectly by shop agreements put in place on the basis of a CBA. A number of CBAs concluded in the meantime allow for longer terms, for example of 48 months. Employers not legally bound by CBAs may adopt the maximum length permitted under a regional CBA that applies to their industry. In this context, CBAs commonly provide for a duty of the hirer to offer employment to an agency worker after a defined term of engagement, and oftentimes further provide that such duty can be excluded by conclusion of shop agreements regarding the use of agency work. Per decisions of the regional labour courts, such shop agreements do not have to specifically deal with offers of employment; rather, agreements on any issues relative to the use of agency workers suffice. The issue has been appealed to the Federal Labour Court.
ii  Business transfers

In the field of business transfers within the meaning of Section 613a of the German Civil Code, 2018 was yet another year of stability. The Federal Labour Court has essentially confirmed its stand on previously treated items and sharpened other aspects.

In one ruling, the Federal Labour Court denied the existence of a business transfer due to the lack of control over the business by the presumed new employer. In the given case, the original employer transferred its production equipment to a sister company, which agreed to and subsequently did act as toll manufacturer and agent for and in the name of the original employer. The Court held that the sister company failed to have control as it did not manage the business in its own name or act as owner of the business in relation to third parties. This was not overweighed by the fact that the company did act in its own name in relation to public authorities and workers’ unions in the context of the employment relationships that had presumably transferred.

Further to that, several cases are currently pending before the Federal Labour Court regarding the liability of an acquirer for company pension rights in the event that a transferred business was acquired from a company subject to insolvency proceedings, and preliminary rulings thereon have been requested from the ECJ. Key questions raised are whether an acquirer will only be liable for future service-related obligations, or whether he or she may also be held liable for obligations relative to pre-transfer periods of service; and whether an acquirer may be held liable for obligations relative to past service in cases where an employee did not have a vested expectancy at the time when insolvency proceedings were commenced. So far, the German courts’ stance has essentially been that an acquirer is not liable for past service-related obligations. In principle, these will fall within the responsibility of the mandatory statutory pension insolvency insurance provided they were vested, did not exceed certain value thresholds and were not channelled through a pension fund; otherwise, they are principally forfeited. If the ECJ were to find that the acquirer was liable for past service-related obligations, this would make the acquisition of businesses from insolvency substantially less attractive in cases where company pension obligations exist.

iii  Minimum wage

The minimum gross wage of employees across all sectors in Germany, which was €8.84 per working hour in 2018, was increased to €9.19 as per 1 January 2019 by regulation of the federal government, and will further increase to €9.35 in 2020.

In notable decisions on the subject, the Federal Labour Court further clarified which kinds of payments count towards the minimum wage requirement. As per earlier precedent, payments by an employer only count if they are made in return for work performed and are unconditional and irrevocable. That is to say, generally, payments do not count if they are made as a reward for a purpose other than the actual performance of work or for which statutory law defines a specific purpose. In 2018, the Court declared that attendance bonuses in principle do count.

Further thereto, the Federal Labour Court has ruled that contractual exclusion clauses in employment agreements concluded after the Minimum Wage Law took effect on 1 January 2015 and that do not explicitly exclude claims to the minimum wage from their scope will be void. However, it remains unclear whether this also applies in the case of employment agreements concluded before such time. Regional labour courts principally upheld such clauses in 2018, declaring that they were merely void insofar as claims to the minimum wage were concerned. Nevertheless, until a decision by the Federal Labour Court...
on the issue, there still is a risk that such clauses could be found void in their entirety, thereby substantially increasing the time frame for bringing claims. On a related note, the Federal Labour Court decided in 2018 that, different from exclusion clauses in employment agreements, clauses in CBAs agreed after the Minimum Wage Law took effect that fail to exclude minimum wage claims from their scope will only be void in such respect, and otherwise remain applicable.

Last, but not least, in May 2019, the federal government resolved to launch a new law introducing minimum compensation requirements for apprentices. If the law is adopted as it currently stands, from 2020 apprentices have to be paid a minimum of €515 gross per month in their first year, with prescribed increases in the next two years of their apprenticeship. In 2021, the first-year minimum amount shall increase to €550, and in 2023 to €620. Exceptions shall be permissible, based on CBAs.

iv Data protection law
In May 2018, the EU General Data Protection Regulation entered into force, further tightening rules on data processing and imposing additional information and documentation requirements on employers. Generally, the law makes data processing by employers more tedious and gives employees tort damages claims in the case of a violation of the duties thereunder. Employers now, inter alia, have to take organisational measures to ensure that no data is processed, stored or transferred in violation of the law. Employees have to be actively informed about the legal basis, purpose and duration of any data processing relative to them, as well as about recipients of their data, persons responsible for their processing, the data protection officer of the company, rights to raise complaints as well as revocation rights for any data processing permission. Further, employees can request information about the length of time that their processed data will be held and content of their processed data. And employers have certain information duties in relation to data protection authorities and affected employees in the case of violations of the law. Essentially the same applies in all EU Member States.

VIII TAX LAW
The most notable developments in German tax law from the previous edition to date that are of relevance in an M&A context concern the repatriation of German-sourced profits and new legislative developments on the German controlled foreign corporations regime and German real estate transfer taxes. Both legislative projects are still ongoing albeit being discussed for a long period.

i Repatriation of German-sourced profits and the anti-treaty shopping rule
Dividend distributions carry, in principle, a 25 per cent German withholding tax burden (plus the still-existing solidarity surcharge of 5.5 per cent thereon). German domestic law offers a reduction down to 15 per cent if the recipient is a foreign corporation and the EU Parent–Subsidiary Directive or an applicable treaty might provide for a lower, or even a zero, rate.

This is all, however, subject to the rather harsh German anti-treaty and directive shopping regime (Section 50d Paragraph 3 of the German Income Tax Act). The respective withholding tax reduction will not be granted if, among other things, the ultimate parent would not qualify for the reduced rate and the interposed recipient of the dividend was either not established for sound economic reasons, or does not engage in general economic
activities with sufficient substance. If an investment is made (as usually through, for example, a Luxembourg or Dutch HoldCo) with low (but sufficient) substance, these rules are always a major issue. While tackling abusive structures is obviously legitimate, the German substance requirements go beyond that, and the ECJ has held in two recent and ground-breaking decisions (Deister/Juhler and GS) that the previous and existing German anti-treaty and directive shopping regimes were in violation of both the freedom of establishment (Article 49 Treaty on the Functioning of the European Union) and the Parent–Subsidiary Directive.

Does this also apply to third-country cases such as investments through, for example, a Swiss or US HoldCo, which only benefit from the free movement of capital? The answer should clearly be yes, as the German substance requirements apply irrespective of whether the investor has a controlling stake, so that freedom of establishment does not block free movement of capital according to the ECJ’s established formula. German tax authorities have, not surprisingly, so far taken a very narrow view on how Deister/Juhler should be applied in practice, and it remains to be seen how the tax authorities and the German legislator will react to GS.

As a result, there is still a great deal (probably even more) uncertainty when it comes to tax-planning considerations on the repatriation of German-source profits. Alternative routes, such as share buybacks and distributions out of a corporation’s contribution accounts (if available and accessible at all), must still be examined. Receiving dividend distributions through a German partnership might also be an option on the back of the promising jurisprudence of the Federal Fiscal Court.

Very recently, the ECJ issued a combined decision on four cases (N Luxembourg 1, et al.) that contains rather explicit guidelines on what the ECJ considers as abusive, which criteria should be applied when testing an abuse, and who has the burden of proof. The legislator has to take this into account for the future of the German anti-treaty and directive shopping regime, which is, for the time being, in violation of EU law, and hence inapplicable.

ii German controlled foreign companies rules to be revised

As part of Germany’s obligation to implement the rules of the EU Anti-tax Avoidance Directive into German law, the German rules on controlled foreign companies (CFCs) must be revised. It is expected that the German legislator will take this opportunity for a more substantial review of the German CFC rules, which are widely perceived as outdated, for example, when it comes to passive activity and the threshold for low taxation. However, the exact content and scope of these revisions is still unclear, as legislation has so far only been leaked in an unofficial draft version.

iii Amendment of the real estate transfer tax rules

German real estate transfer tax (RETT) becomes due not just upon the direct transfer of German real estate itself but also upon certain direct or indirect transfers of shares or partnership interests in real estate-owning companies or partnerships. In particular, RETT is levied:

(a) on the direct or indirect transfer of 95 per cent (or more) of the interests in the assets of a real estate owning partnership within a five-year period (Section 1, Paragraph 2a of the RETT Act, Partnership Rule);

(b) if 95 per cent (or more) of the shares or partnership interests in a real estate-owning company are directly or indirectly transferred to a single person (including related persons) (Section 1, Paragraph 3 of the RETT Act);
if a person (including related persons) holds, as a result of a transaction, directly or indirectly, 95 per cent (or more) of the shares or partnership interests in a real estate-owning company (Section 1, Paragraph 3 or the RETT Act); or

if a person holds, as a result of a transaction, a direct or indirect economic interest of 95 per cent (or more) in a real estate-owning company (Section 1, Paragraph 3a of the RETT Act).

The threshold of 95 per cent means that, in practice, share deals are often structured in a way that manages not to trigger RETT. However, there is now a broad political consensus across party lines to amend the RETT rules with the explicit intention of capturing a larger percentage of share deals. Hence, and as long-awaited, the German Federal Ministry of Finance unveiled recently a draft bill for a reform of the RETT Act. Under the draft bill, the scope of the German RETT provisions regarding the taxation of share deal transactions would be substantially broadened. The main changes are as follows:

- Generally, the relevant threshold of currently 95 per cent will be lowered to 90 per cent.
- The general watching period of currently five years will be extended to 10 years.
- There will be a new provision that is modelled after the Partnership Rule and extends its scope to corporations. As a consequence, in the future a direct or indirect transfer of at least 90 per cent of the shares in a real estate holding corporation within 10 years to (any number of) new shareholders will trigger RETT (New Corporation Rule).

The threshold of 90 per cent for indirect transfers is generally calculated by a simple multiplication of the share and interest percentage. However, there is one notable exception: if there is a direct change of at least 90 per cent of the shares in a corporation holding shares in the real estate holding corporation, then 100 per cent of the shares held by the shareholder corporation would be deemed as transferred.

It remains to be seen how these draft measures will progress through the legislative procedure. For the time being, however, the draft bill should form the basis of any tax planning considerations, and in light of the temporal scope it might be worthwhile accelerating envisaged transactions in order to still come under the current, more beneficial rules. For the New Corporation Rule, this would require not just the signing but also the closing of the transaction.

IX COMPETITION LAW

In 2018, the number of merger control notifications reviewed by the Federal Cartel Office (FCO) remained stable. As in 2017, the FCO reviewed about 1,300 merger control notifications, and cleared almost all notified transactions (more than 99 per cent) within the Phase I deadline of one month. Only 12 of the transactions that were filed during 2018 raised (or continue to raise) competitive concerns and were (or still are) being reviewed in more detail (Phase II proceedings), which is slightly more than last year (10 transactions).

To date, the newly introduced transaction value threshold, which entered into effect on 9 June 2017 as part of the Ninth Amendment of the Act against Restraints of Competition (ARC), has not led to a considerable increase in merger control notifications. Against the background of the Facebook/WhatsApp transaction, the Ninth Amendment provides for a new Section 35, Paragraph 1a of the ARC. Transactions whereby one party generates a turnover in excess of €25 million in Germany, but the turnover of any other party is below €5

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people in Germany, are now nevertheless subject to merger control if the transaction value exceeds €400 million and the target company has significant activities in Germany. Focusing on technology and innovation-driven markets, the new threshold aims at preventing possible market foreclosure and barriers to entry as well as protecting the potential for innovation.

The new threshold raises two key questions: how to calculate the consideration and how to determine the local German nexus. To provide further guidance, the FCO and the Austrian Federal Competition Authority has published joint guidance on the interpretation of the new threshold. For the determination of the German local nexus, different criteria apply to different sectors and activities. As a definitive list of criteria cannot be provided, a case-by-case assessment remains necessary. The common denominator is that domestic activities must have market orientation despite the (intermediary) absence of monetisation, for example because a service is remunerated by means other than monetary payment, a service is (temporarily) offered free of charge but can be expected to be monetised in the future, or the activity consists of research and development of (future) products and services. Based on the purpose of the provision, the transaction value threshold shall cover those cases where the target shows a high degree of economic and competitive potential. It shall not address transactions where the (albeit small) generated turnover adequately reflects the market position and competitive significance.

Of the 12 Phase II transactions, three were cleared unconditionally and one was prohibited. The FCO did not allow Miba AG (Austria) and Zollern GmbH & Co KG, Sigmaringen to launch a joint venture to pool their hydrodynamic plain-bearing production activities. With the merger, buyers in the respective industrial sectors in Germany and other European countries would have lost an important supply alternative. The two parties were the major competitors in an already highly concentrated market with high barriers to entry, as the latter would require extensive technology knowledge and high investments.

While two cases are still under investigation, the parties of six transactions withdrew their filings after the FCO expressed its competitive concerns: Bunkering Service Providers for inland waterway vessels Reinplus VanWoerden Bunker GmbH’s and Nord- und Westdeutsche Bunker GmbH’s supply areas overlapped, and the merger would have reduced the number of competitors from three to two. Furthermore, Reinplus was also vertically integrated in the upstream fuel trading markets. In its assessment of the merger of towbar suppliers Horizon Global Corporation (US) and Brink International BV (Netherlands), the FCO closely cooperated with the British Competition and Markets Authority. Both authorities exchanged information and analysis regarding the competition issues that each authority was investigating, including discussions of possible remedies. One key issue was the important technical edge the merged entity would have had compared to its smaller competitors. Thus, both authorities reached similar conclusions that made the parties decide to abandon the transaction. In an attempted acquisition of the licence for the German-language edition of National Geographic by Gruner + Jahr, the FCO looked at online, television and print competition for science magazines and concluded that, despite a decrease in magazine circulation, Gruner + Jahr’s dominant position in print publications was not sufficiently controlled by television or online programmes. The other cases, in which a notification was withdrawn, involved acquisitions of hospitals and petrol stations (i.e., narrow local markets).

In addition to these withdrawals, the FCO emphasised in its year-end press conference that companies often informally approach the FCO before filing, in particular in cases that may be critical. Some of the projects presented to the FCO on a confidential basis will then not even be notified. The FCO is open to confidential guidance proceedings, and increasingly
engages with parties to a transaction before submitting a formal filing. Depending on the confidentiality of a transaction, the FCO may even start sending out requests for information to competitors or customers prior to, or at least on the day of, the formal filing, increasing the chance of a Phase I clearance in cases that require at least some kind of market testing. In the Karstadt/Kaufhof acquisition, the long and thorough preparation of the actual merger control proceeding allowed the case to be cleared during the one-month Phase I proceeding. The FCO sent out questionnaires to around 100 retail companies and suppliers on the day of the filing.

The Karstadt/Kaufhof deal was the most important transaction in the retail sector. Despite the fact that the two companies were the only German department store operators, the FCO did not assess the department store market, but focused on 20 different product categories, such as suitcases and bags, underwear, sports and outdoor, and household textiles. The FCO assessed the case under several possible market definitions ranging from a bricks and mortar-only perspective to the inclusion of online retailers, which the FCO described as an important shopping alternative providing for increasing competitive pressure. Competition between online and offline distribution was also important in the Douglas/Parfümerie Akzente and DocMorris/apo-rot Versandhandel cases. Douglas, the biggest brick-and-mortar perfume retailer, purchased Akzente Parfümerie, a strong online sales outlet. In the DocMorris case, the FCO explicitly concluded that mail order pharmacies compete with stationary outlets, which is why the combination of two mail order providers did not negatively affect competition.

The retail sector also accounts for one of 2018’s most important judgments of the Federal Court of Justice in the competition field. After its takeover of the Plus stores in 2008, food retailer EDEKA had unilaterally demanded special conditions from its suppliers (also called ‘wedding rebates’). A combination of demands with retroactive effect, cherry picking of individual preferential conditions granted to either of the parties and a request for substantial bonuses violated the Law on Tapping (Sections 19 (1), (2); 20 (2) ARC), because it asked suppliers to grant benefits without any objective justification. The Federal Court of Justice particularly emphasised that EDEKA not only compared conditions applicable at the time of the transaction. It also considered conditions that had applied only temporarily before the merger was completed.

Generally, recent merger control and antitrust cases have confirmed the FCO’s focus on digital markets. Following a 2016 market power of platforms and networks paper, and a big data and competition working paper of October 2017, in 2018 the FCO published working papers on online advertising and on competition restraints in online sales after Coty and Asics. Access to data has become the key parameter in many industries, including the energy, banking and insurance sectors. The FCO also issued a decision against Facebook prohibiting the social network from combining user data from different sources. According to the FCO, Facebook abused its dominant position by violating German data protection provisions. The decision is not yet definitive.

**X OUTLOOK**

We expect a significant increase in M&A activity in Germany within the next 12 months. Increasing globalisation, digitalisation, Industry 4.0, unsolved succession issues in Mittelstand companies, low interest rates and enormous liquidity in the markets will continue to be important drivers for M&A. Most German corporates are enjoying strong current trading in 2018. Solid balance sheets, double digit profitability margins and strong order backlogs.
facilitate M&A transactions and drive valuations. High levels of dry powder, combined with low interest rates and a scarcity of solid assets, are likely to lead to a further increase of transaction multiples.

Nevertheless, political and economic risks for the global economy are obvious. These factors also may have a significant impact on M&A activities. Among these uncertainties are the unresolved questions around Brexit, increasing tensions between the United States and China, a drift in respect of foreign policies between countries of the Western Hemisphere and a potential slowdown, if not reversal, of the decades'-long trend towards globalisation. While all these factors may in the short term even spur M&A activity, their long-term impact is in our opinion impossible to predict.
Chapter 20

GREECE

Cleomenis G Yannikas, Vassilis S Constantinidis and John M Papadakis

I OVERVIEW OF M&A ACTIVITY

Following many years of deep recession and increased levels of unemployment, Greece is now trying to recover and restore stability in the Greek economy. Increased taxation and social security are not helpful, and enterprises are awaiting for stability and solutions to structural problems of the Greek economy, which will allow extrovert business, new investments and the creation of new jobs.

At the same time, the government has started to make some progress with the privatisation procedures already announced as part of the policy framework. After significant delays, the implementation of several projects in the area of privatisations, such as Ellinikon, the privatisation of Thessaloniki port and the privatisation of DESFA, has eventually gone through to a significant extent. In addition, the new hyper fund was created with the aim of promoting privatisations in a much wider spectrum compared with what was planned some years ago. However, it remains to be seen how the government will finally treat this politically sensitive situation.

In addition, Greece has been heavily involved in the refugee crisis, which has significantly affected an economy and society that was already under pressure, adding further problems to be managed by the government and Greek society, and creating an odd environment in the country.

The private sector, to the extent that it is not dependent on the state, has shown it is capable of surviving despite these difficulties. Under improved circumstances in the financial environment, it should be able to grow rapidly and recover relatively quickly.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Greek M&A legal framework is mainly composed of the following:

1. Law 4548/2018, on public limited companies;
2. Law 4601/2019 (corporate provisions for business transformations);
3. Law 4172/2013 (tax incentives for business transformations);
4. Law 2166/1993 (tax and other incentives for business transformations (e.g., merger, split, spin-off));
5. Law 1297/1972 (tax incentives for business transformations);

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1 Cleomenis G Yannikas and Vassilis S Constantinidis are senior partners and John M Papadakis is an associate at Dryllerakis and Associates.
2 Sociétés anonymes, not to be confused with listed companies.
Privatisation Fund;
g Law 3864/2010 on the Hellenic Financial Stability Fund;
h Law 3777/2009 on cross-border mergers of limited liability companies (implementation
of Directive 2005/56/EC);
i Law 3401/2005 on prospectuses in the case of public offers of securities; (implementation
of Directive 2003/71/EC), which was amended by Law 4374/2016 (adopting EU
Directives 2013/50 and 2014/51);
j Law 3461/2006 on public takeovers (implementation of Directive 2004/25/EC);
k the Athens Stock Exchange Regulation; and
l Law 3959/2011 on Greek merger control provisions.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND
THEIR IMPACT

An important legislative initiative took place in 2018, aiming to modernise the provisions
governing the société anonyme and create a more attractive framework. In this respect, the
old L2190/20 has now been abolished and replaced by new L4548/2018. Within the same
modernisation framework, a new L4601/2019 has been further introduced, covering all
types of potential corporate transformations (including conversions, mergers, spin-offs),
regardless of corporate form. Some further initiatives are currently in progress regarding the
Commercial Registry and the revision of the corporate governance rules.

Indeed, requests from the business community concern more important measures that
need to be taken to increase the competitiveness of Greek enterprises in their daily operations,
such as fast-track permit procedures.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Notwithstanding the above efforts, the business environment in Greece remains to a large
extent characterised by bureaucracy, administrative procedures and actual disincentives for
foreign investors. One of the recent legislative initiatives refers to the reform of the framework
for strategic investments, the results of which remain to be seen in the near future.

Other than that, within the privatisation programme run by the Hellenic Republic
Asset Development Fund, the majority stake of Thessaloniki Port Authority was sold to a
German-led, French and Russian consortium. In addition, the tender process concerning
the sale of 66 per cent of the state-controlled Greek gas operator DESFA SA went through
successfully, with the Snam–Enagás–Fluxys consortium being awarded as the preferred bidder
of the process. On the other hand, the attempted sale of a 50.1 per cent stake in Hellenic
Petroleum ended in failure, as neither of the two consortiums that had originally expressed
an interest submitted a binding financial offer, while the ongoing process for the concession
of Egnatia Odos is significantly delayed.
V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

There have been a couple of M&A deals during the past 12 months. In the banking sector, probably the most interesting deal was the merger between Eurobank Ergasias and Grivalia Properties REIC. It was respectively announced that the merger creates the best-capitalised bank in Greece, and the deal was successfully completed in the second quarter of 2019. In the gambling sector, OPAP proceeded with the acquisition of 51 per cent of Stoiximan SA (Greek and Cyprus activities), one of the leading online betting companies in the region. Another interesting deal concerned the further investment by CVC Capital in the health sector by further acquiring Hygeia SA hospital after last year having acquired both the Metropolitan and IASO hospitals.

The real estate sector, after having suffered severely from the effects of the crisis, is already recovering, with a lot of ongoing investments especially in the tourism sector (e.g., Four Seasons Astir Palace Hotel Athens, Grand Hyatt Athens). It is worth mentioning that the recent trend in favour of short-term leases (e.g., through the Airbnb platform) have assisted in this development, but the commercial leasing of stores and offices has also started improving.

It is also finally worth noting the trend of several Greek companies to seek an alternative to bank financing through the issuance of bond loans. This tendency has continued in the past year especially through bonds listed on the regulated market of the Athens Stock Exchange.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

As far as mergers are concerned, there is no practical need for financing since they are implemented through an exchange of shares. Acquisitions can either involve an exchange of shares (which was the case in several past deals, especially in the banking sector) or a cash consideration, in which case financing is required. Such financing normally takes the form of one of the two following alternatives:

a self-funding by the shareholders of the acquiring company: the procedures for an increase in share capital are rather formal, as per the EU directives, especially when made in cash. A main point of interest is the price offered for the new shares to be issued (which cannot be less than market value), because this is linked with the valuation of the company and determines the balance between shareholders; or

b bank financing, which can either be in the form of a classic bank loan or that of a bond loan (common or convertible) issued by the company: experience shows a tendency in favour of bond loans due to their favourable tax and other treatment, as well as due to the easy transfer of bond titles, if needed. It cannot be ignored that, contrary to the recent past, the severe financial situation has heavily affected and practically eliminated bank financing for M&A.

In a case of intra-group financing, attention should be paid to the applicable provisions of Law 4548/2018 regarding related party agreements. In any case, one must also be cautious about the arm's-length principle, in accordance with transfer pricing rules.
VII EMPLOYMENT LAW

Employment legislation was not further developed during 2018 or to date in 2019 as far as M&A activity is (directly) concerned, except for a couple of provisions pertaining to the protection of employees’ rights in the case of ship transfers (as part of the business to be transferred).

On the one hand, there is a plethora of special provisions of law regarding, inter alia, mergers and restructurings of state-owned enterprises (SOEs) and within the banking sector. Numerous provisions have been further instituted on an *ad hoc* basis to regulate the employment relations of specific state organisations (see, for instance, Article 3 of Law 4138/2013 regarding the merger of local development organisations). However, no generally applicable rule can be derived therefrom that would be of any interest for the private sector; past governments very often established special legislative texts for M&A of SOEs due to their politically sensitive nature.

On the other hand, as a general rule, in the case of a merger there is a full succession of the surviving (absorbing) entity regarding all the rights and obligations of the merged company. Accordingly, the latter becomes fully liable for any and all labour obligations of the former. In the case of acquisitions, there are protective provisions regarding transfers of businesses (implementation of European law) that provide that both the transferor and the transferee shall be jointly and severally liable in respect of labour obligations that existed at the date of transfer. It is worth mentioning that the means of transfer (i.e., if it takes place via a contract – even an invalid one – or by law, or even by a simple assignment of the operation of the business without transfer of tangible or intangible assets) is irrelevant, but the transfer and succession in the employer’s position is examined on a case-by-case basis.

Since 2010, it has been expected that the downturn in the Greek market and the crisis in the Greek economy would generally give rise to significant changes in employment law, which might not refer directly to M&A topics but which would nevertheless have an impact, since the labour perspective is generally a critical point of assessment in an M&A deal. As part of the agreement for the financial support of the country, Greece undertook to proceed quickly with radical changes in many sectors of the Greek economy and in the labour market. The main areas that have been affected from a labour law perspective are as follows:

- introducing restrictions in the system of collective labour agreements or negotiations, and a more flexible regime;
- abolishing the procedure of referring collective labour disputes to an organisation for mediation and arbitration;
- increasing the thresholds in the case of group dismissals and, eventually, abolishing the authorities’ prior approval;
- decreasing severance pay and allowing its repayment in instalments;
- introducing more flexible employment terms (*sub minima*) for workers under the age of 25;
- extending probationary periods, facilitating greater use of part-time work, moderating wages for overtime and introducing remuneration connected to the productivity of a business; and
- keeping salaries temporarily frozen (initially) for three years after the conclusion of the previously mentioned memorandum.

There have been quite a few examples of the implementation of the above-mentioned guidelines during the past seven years. For instance, the Ministers’ Council issued Act No.
6/2012, which instituted an obligatory decrease of 22 per cent in minimum wages under the national collective labour agreement, and abolished the possibility of unilaterally resorting to arbitration in cases where collective bargaining fails. Law 4093/2012 further reduced the termination severance (mainly by preventing the accrual of seniority rights after November 2012), facilitated the split of annual leave, decreased the requirements for the operation of temporary work agencies and instituted a number of additional favourable provisions for the labour market. Most importantly, however, Law 4093/2012 abolished the system of determining the minimum wage through collective bargaining procedures by introducing the minimum wage itself. Finally, it vests the government with the power of adjusting the minimum wage.

In general, the purpose of the above amendments was to reduce the cost of labour and make the Greek employment market more competitive. On the other hand, various provisions have been instituted to protect vulnerable groups, such as older employees. Thus, it is obvious that, due to the financial support of EU Member States and the International Monetary Fund, Greece has been obliged to proceed more quickly to implement those measures to ensure the ‘flexicurity’ of the employment market.

However, based on the experience of recent years, the measures implemented so far have not efficiently served these purposes. The above situation, apart from rendering any reforms ineffective, has made it unclear whether each provision of this multitude of recent laws affecting the employment terms in the public and private sectors would survive if contested before the Greek courts. There had been various judgments of first instance courts (within the framework of injunction measures) that considered certain provisions concerning public sector employees as being contrary to the provisions of the Greek Constitution and European law. In addition, such legislative initiatives of the government had raised multiple concerns for the Committee on Freedom of Association of the International Labour Organisation’s governing body, especially as to what regards the weakening and eventual abolishment of collective bargaining rights and the overall scope of collective bargaining laws. It must be noted, however, that said changes and restrictions on collective bargaining agreements seem to be reduced after the expiration of the middle-term bailout programme, and the competent authorities will start interpreting the respective terms in a way that is more favourable to the unions’ side. For instance, a collective bargaining agreement at the level of a business could include provisions deviating from the agreement made for a specific market or profession and introduce provisions weakening workers’ rights and even reducing salaries, which is no longer the case as, since August 2018, said option is considered as no longer valid. Similarly, the government has reinstated the obligatory extension of collective bargaining agreements, which had been suspended until the end of the economic adjustment programme.

Moreover, the government has made use of the option to define the minimum wage, and by the end of 2018 had increased the minimum wage to €650 per month (the previous minimum wage was €586.80), and abolished the distinction between the minimum wage for young (up to 24 years old) workers and employees that gained a gross salary of €511.00. Said increase also impacted the social security contributions for both employers and employees, as well as of other professionals, as the new minimum wage is the basis for the calculation of the minimum social security contribution for professionals (e.g., lawyers, engineers). On the other hand, since 1 January 2019, a decrease in the social security contributions for this category of professionals has been introduced equal to one-third of the percentage calculated on the total income of the individual, but a suspended auxiliary social security contribution for these professionals started to be implemented as of 1 January 2019, although not any
more as a percentage on the individual’s income but just on the minimum wage amount (as determined with a calculation of years of service); therefore, the hit on the market seems to be less hard than was expected. In 2014, the Administrative Supreme Court found certain provisions of Ministers’ Council Act No. 6/2012, and in particular the ones requiring the consent of both parties (employer and trade union) for the initiation of an intermediation and arbitration process, to be non-compliant with the constitutional provisions, which led to the reinstatement of the previous regime of the unilateral application of the interested party (Law 4303/2014).

In 2016, the government launched a dialogue regarding the introduction of a new social security system, which was however rejected by, inter alia, the trade unions and professional associations. The draft bill comprised several structural changes in the area of social security, with the major ones being to have all social security funds and organisations merged into one; and the implementation, for all categories of employees, self-employed persons and other professionals, of a uniform treatment with regards to the calculation of their contributions based on their annual or monthly income falling within a range of 25 to 36 per cent. There were a variety of reactions about this restructuring of the social security concept (e.g., Greek lawyers abstained from their duties for almost six months), but the government managed to pass the legislation (Law 4387/2016). In terms of employment, a direct impact of the recent Social Security Act is employees being subject to more than one social insurance organisation (e.g., through being employees and self-employed at the same time), who are now required to pay more (approximately double) social security contributions without being entitled to additional pension amounts.

In 2017, Law 4472/2017 introduced a radical change pertaining to the collective dismissals legal framework by abolishing the ministerial veto that used to apply under the previous legal regime, which provided for an information and consultation procedure between the parties involved as well as the prior approval of the competent authorities in cases where the parties failed to reach an agreement. New Law 4472/2017 set out a different procedure on collective layoffs, including the extension of the consultation process of up to 30 days and the supervision of the procedure by a new supervising body, the Supreme Labour Council. Pursuant to these new statutory provisions, the Supreme Labour Council is now in charge of the collective layoffs process, and is also responsible for checking whether employers have abided by the consultation and information requirements set out in law. If the Supreme Labour Council finds that these requirements have been met, an employer is free to proceed with the intended group dismissal. On the other hand, non-compliance with these requirements would be the only reason for the government to discontinue a collective redundancy process, in the sense that the government’s role is now limited to the inspection of the existence of these typical consultation requirements.

Until very recently, Presidential Decree 178/2002 on the protection of employees’ rights in the event of a transfer of business (which harmonised EU Directive 2001/23) was not applicable in the case of ship transfers. Through Law 4532/2018, said protection is now extended to transfers of ships under the Greek flag, but only when they are part of the business to be transferred and on the conditions set forth in Law 4532/2018.

Finally, the government recently adopted the wording of the Revised European Social Charter as to what regards the termination of an employment agreement, and introduced into Greek employment law the compulsory ‘causal’ redundancy. Until the introduction of Law 4611/2019 (Article 48), Greek law provided that the termination of an employment agreement should not be grounded on a specific cause if it was made in writing and the
employee was receiving legal severance. Today, the right of an employer to terminate must be grounded on a specific cause as per Article 24 of the Revised European Social Charter (ratified by L4359/2016), and the employer must prove that these conditions have been met in cases where the validity of the termination is challenged. This new condition will probably affect and reduce the right of termination of employers, especially in cases of no apparent reason a termination.

VIII CIVIL PROCEDURE CODE

One of the first measures adopted by the parliament directly after the conclusion of the July 2015 agreement with the EU institutions was the adoption of a new Civil Procedure Code. Law No. 4335/2015 has introduced amendments in most areas of civil disputes aimed at expediting the process up to the hearing of cases (which, prior to this change, could take more than three to four years). The new Code provides that the whole process starts with the filing of a claim, without setting a more specific date for its hearing, which will take place within a maximum of 160 days from its submission. The process is concluded without a real hearing, and based only on documents and affidavits of the parties, while the presence of barristers is no longer necessary and grounds for the deferral of a hearing are practically abolished. Furthermore, the new Code has adopted a much quicker process for the enforcement of judicial decisions and a swift procedure for the collection of debts. The new Code came into force on 1 January 2016.

The first couple of years of implementation showed a slight improvement in the courts’ addressing of civil cases and delivering judgments more speedily. However, it seems that the main purpose and aim of the new Code will not be satisfied entirely, as the courts are showing that they cannot deal with the number of the cases addressed to them: hearing dates are now set in most cases eight to 12 months or more from the final submission of the pleadings of the litigants, and the publishing of judgments has started to show significant delays.

A new tool for dispute resolution was introduced in the past 12 months with the aim of helping the government in its effort to relieve the courts of the volume of cases and claims pending. Law 4512/2018 provides for a compulsory mediation before the start of any judicial proceedings in certain areas of day-to-day business activity (e.g., disputes over trademarks, patents and IP rights in general may not be submitted for resolution to the competent court before the claimant can prove that mediation has been attempted but failed). Other kinds of disputes that have to be addressed through mediation before any submission of claims to the competent courts are, inter alia:

a. claims based on medical malpractice;
b. compensation and claims from car accidents;
c. the collection of professional fees; and
d. claims based on stock exchange contracts.

Mediators should be accredited by the Central Mediation Committee, and are full-time professionals with special training in mediation techniques. The Law provides that the maximum length of the mediation process is 24 hours in total (which may be extended by the parties), and for a short period for the conclusion of the process within 15 to 30 days from the appointment of the mediator. This process initially was planned to be implemented on October 2018 after the accreditation of the new mediators, but it has been suspended for another year following several reactions of the local bars.
Greece

IX  TAX LAW

Following the complete replacement of the Code of Income Taxation (CIT) and the introduction of a new Code of Fiscal Procedure, both of which came into force on 1 January 2014, as of 1 January 2015 the Greek Accounting Standards\(^3\) abolished the Code of Transactions Tax Reporting and the Greek accounting legislation, thereby becoming more compliant with the International Accounting Framework.

During 2018, changes in the tax legislation continued, mostly aiming at implementing reforms agreed by the government within negotiations for financial support and enhancing the collection of public revenues, but also adopting EU rules and complying with commitments under international treaties.

The most important tax issues are as follows.

i  **Transfers of shares**

From 1 January 2014, any capital gain that derives from a transfer of shares of non-listed companies is subject to a 15 per cent tax if the transferor is an individual (Articles 42 and 43 CIT). In the case of legal entities, the capital gain shall be added to the gross income and, should there be a profit from the business activity, it shall be subject to the tax rates that apply to income from business activities (i.e., 28 per cent for fiscal year 2019). For the calculation of the capital gain, the acquisition cost is deducted from the price.

The aforementioned tax is also imposed on the transfer of shares of listed companies provided that the following conditions are cumulatively met: the transferor participates in the share capital of the company with a stake of at least 0.5 per cent, and the shares to be transferred have been purchased after 1 January 2009. In any case, a tax on stock market transactions is also imposed.

ii  **Corporate income tax rate**

The corporate income tax rate for public limited companies, limited liability companies, private capital companies, Greek branches of foreign corporations and, in general, any company that maintains double-entry accounting books, which was raised from 26 to 29 per cent for fiscal years 2015 onwards, shall be gradually reduced to 28 per cent (for fiscal year 2019), 27 per cent (for fiscal year 2020), 26 per cent (for fiscal year 2021) and 25 per cent (for fiscal years 2022 onwards) (Article 58, Paragraph 1 CIT).

iii  **Taxation on dividends**

For profits distributed from 1 January 2019 onwards, a withholding tax of 10 per cent is applicable on dividends. From 1 January 2017 until 31 December 2018, the rate of said tax was 15 per cent.

Withholding of the aforementioned tax exhausts the tax liability, provided that the taxpayer is an individual (Article 36 Paragraph 2 CIT) or a legal entity that is not a Greek resident and does not have a permanent establishment in Greece (Article 64 Paragraph 3 CIT). Under specific conditions, which are set out by Article 63 CIT (adopting Directive 2011/96/EC), intra-group dividends may be totally exempt from withholding taxation.

Dividends distributed to Greek legal entities or legal entities with a permanent establishment in Greece are also subject to withholding tax at a rate of 10 per cent, although

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\(^3\) Law 4308/2014.
an exemption under the conditions of Article 63 CIT may apply in the case of intra-group dividends. However, their income from dividends is added to their annual gross income and taxed as a profit at a rate of 29 per cent. In such a case, the tax withheld is credited against the tax payable.

Pursuant to Article 48 CIT, intra-group dividends received by a legal entity that is a tax resident of Greece are totally exempt from tax, provided that:

a the recipient holds a minimum participation of at least 10 per cent of the value or number of the share capital, core capital or voting rights of the legal entity that makes the distribution of profits;

b the aforementioned minimum participation is held for at least 24 months; and
c the legal entity that makes the distribution of profits:
   • has a legal status that is included in the list of EU Directive 2011/96/EC;
   • is a tax resident of an EU Member State, in accordance with the laws of that state, and may not be considered as a tax resident of a third country (non-EU Member State) by virtue of the double taxation treaty that has been signed with that third country; and
   • is subject to one of the taxes listed in EU Directive 2011/96/EC.

In such cases, dividends received by the legal entity must form a tax-free reserve until they are further distributed to the entity’s shareholders.

Pursuant to Directives 2014/86/EC and 2015/121/EC, intra-group dividends are exempt from taxation to the extent that the respective dividends have not been deducted by the subsidiary. Furthermore, the aforementioned exemptions (of Articles 48 and 63 CIT) shall be alleviated in cases where it is considered that a non-genuine arrangement exists (i.e., an arrangement that has not been put into place for valid commercial reasons reflecting the economic reality).

iv Transfer pricing

The new CIT and the Code of Fiscal Procedure include transfer pricing (TP) provisions that differ in some ways when compared to the previous legal framework, and that are applicable for fiscal years starting as of 1 January 2014. It should be noted that under the new legal framework, an advanced pricing agreement may be established with the Ministry of Finance.

Taxpayers having intra-group transactions exceeding the thresholds provided in the above legislation have two main obligations: preparation of a TP report for the documentation of intra-group transactions within the deadline for submission of the annual tax return (the report is submitted to the tax authorities upon request and within 30 days of the request), and the filing of a summary information table within the same deadline. TP legislation provides serious penalties for the violation of the arm’s-length principle and for the failure to comply with the above obligations. There are also new penalties provided for the inadequacy, inaccuracy or late submission of the summary information table and TP report. Finally, the new TP legislation specifically refers to the OECD Transfer Pricing Guidelines for the documentation of intra-group transactions. There are also various circulars of the Ministry of Finance issued to date that establish special rules for the documentation of intra-group transactions.
v  Losses
In accordance with the new CIT, losses incurred abroad cannot be used against profits of the same tax year or against future profits unless there is income that derives from other EU or EEA Member States and there is no provision in a double taxation treaty that provides a tax exemption for it. By virtue of a recent circular issued by the Ministry of Finance, losses incurred abroad shall be monitored per country and may be used against future profits incurred in the same country. Moreover, by virtue of a more recent circular, before the deduction of said losses in Greece, Greek entities shall need to prove before the fiscal authorities that they have made every effort to deduct losses abroad and have failed to do so.

In addition if, during a fiscal year, direct or indirect ownership of the share capital or voting rights of a company is changed by more than 33 per cent of its value or number, the transfer of losses ceases to apply as regards losses incurred during that fiscal year and the previous five years, unless it is proven by the company that the change of ownership has been exclusively made for commercial or business purposes, and not for tax-avoidance or tax-evasion purposes.

vi  Deductibility of interest – thin capitalisation rules
According to the CIT, borrowing costs are not recognised as deductible business expenses to the extent that the surplus of the interest expenses against income from interest exceeds a rate of 30 per cent of taxable profits before interest, taxes, depreciation and amortisation (EBITDA). The term borrowing costs includes, apart from interest on loans, inter alia, other costs economically equivalent to interest and expenses incurred in connection with the raising of finance, as well as the finance cost element of finance lease payments and the capitalised interest included in the balance sheet value of a related asset. It should be noted that the aforementioned rate used to be higher during previous fiscal years, and was gradually reduced.

However, interest expenses shall be recognised as fully deductible business expenses up to an amount of €3 million net-registered interest expenses per year. Any interest expense that is not deductible pursuant to the aforementioned rules shall be carried forward with no time limit. This does not apply to credit institutions or to leasing and factoring companies.

vii  The new CIT definitions and provisions
The new CIT introduces certain new definitions and provisions, the most important being terms for legal entity and legal form, and the introduction of the true place of exercise of management criterion.

The Code of Fiscal Procedures introduces definitions of tax avoidance, whereas a general anti-abuse clause has been introduced pursuant to which:

> the tax administration shall ignore any arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or the purpose of the applicable tax law, are not genuine, having regard to all relevant facts and circumstances.
viii Statute of limitations

The statute of limitations period varies depending on the category of tax and the fiscal year.

The basic statute of limitations for fiscal years 2014 onwards is five years, which may be raised to 20 in cases of tax evasion, which covers a very broad number of cases. The 20-year statute of limitations also applies to fiscal years that had not been time-barred on 1 January 2014. However, by virtue of a more recent opinion given by the state’s Legal Council, the 20-year statute of limitations shall not be applicable for fiscal years up to and including 2011.

For a very long time, the expiry of the statute of limitations has been continuously extended by special laws. According to a recent decision of the Supreme Administrative Court in Plenary Session, in brief, such extensions of the statute of limitations have been judged to violate the Constitution.

Another aspect of the statute of limitations concerns fiscal years 2011 to 2013, during which the tax audit for sociétés anonymes was required to be carried out by a Greek certified auditor issuing a tax certificate under the then-applicable Law 2238/1994. According to certain jurisprudence, the tax authorities do not have the right to conduct an audit on sociétés anonymes with no comments in the tax certificate after the lapse of 18 months from the end of each relevant year unless exceptional circumstances exist. For periods starting from 1 January 2014 onwards, acquisition of an annual tax audit certificate does not affect the statute of limitations.

X COMPETITION LAW

Merger control provisions are included in Law 3959/2011 regarding the protection of free competition (Articles 5 to 10) and are enforced by the Hellenic Competition Commission (HCC), an independent administrative authority.

The Greek merger control system provides for pre-notification to the HCC (30-day deadline) in cases of concentration where the following two thresholds are cumulatively met: all participating enterprises have an aggregate worldwide turnover exceeding €150 million, and at least two of them each has a national (Greek) turnover of at least €15 million. In such a case, the transaction cannot be completed without the clearance of the Competition Commission. The latter theoretically has the power to block a transaction (but has not blocked any application to date).

There is currently no post-notification obligation for minor mergers under Greek law.
Chapter 21

HONG KONG

Jason Webber

I OVERVIEW OF M&A ACTIVITY

M&A activity in Hong Kong remained high in 2018, with a total of 584 announced deals and a total disclosed value of US$167.93 billion in 2018, representing a decrease compared with 2017.

The Hong Kong securities markets showed a decrease in terms of market capitalisation but an upturn in terms of trading activity in 2018. A total of 218 companies were newly listed on the Stock Exchange of Hong Kong Limited (SEHK) in 2018, and the total amount of equity funds raised on the SEHK in 2018 was approximately HK$544.13 billion.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The law governing M&A comprises primary legislation, regulatory rules, the law of contract and case law.

The primary legislation that applies principally to Hong Kong-incorporated companies in general is the Companies Ordinance (CO) and includes provisions relating to financial assistance for the acquisition of a company's own shares, merger relief, transfers of shares and schemes of arrangement affecting mergers. The Securities and Futures Ordinance (SFO) is also relevant, covering the regulation of offers of securities, and the communication of invitations and inducements to engage in securities transactions.

For companies in certain industries, there is also specific legislation that may be relevant, for example:

a the Banking Ordinance for banking, restricted licence banking and deposit-taking companies;

b the SFO for securities, financial advisory and asset management companies;

c the Broadcasting Ordinance (BO) and the Telecommunications Ordinance (TO) for radio, television broadcasting and telecommunications companies; and

d the Insurance Companies Ordinance for insurance companies.

1 Jason Webber is a partner at Slaughter and May. The author would like to thank Nicola Lui and Dimitri Au-Yeung for their assistance in preparing this chapter.

2 Statistics on mergers and acquisitions involving Hong Kong companies differ significantly among various sources. This summary covers all M&A activity where Hong Kong was the target, seller or bidder region between 1 January 2018 and 31 December 2018.

3 Source: SEHK Fact Book 2018.
Prior approval of ownership changes from the relevant regulatory bodies may be required under the legislation listed above.

If an M&A transaction involves a company whose shares are listed on the SEHK, the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (Listing Rules) will also apply. In addition, the Securities and Futures Commission (SFC), in consultation with the Takeovers and Mergers Panel (Panel) – a committee formed by the SFC pursuant to the SFO – has issued the Code on Takeovers and Mergers and Share Buy-backs (Takeovers Code), which applies to takeovers, mergers and share buy-backs affecting public companies in Hong Kong and companies with a primary listing of their equity securities in Hong Kong. The Takeovers Code is not statutory and does not have the force of law, but the Listing Rules expressly require compliance with the Takeovers Code. As a non-governmental statutory body, the SFC regulates the securities and futures markets in Hong Kong and oversees the development of these markets. Its decisions apply to M&A of public companies.

Since Hong Kong is a common law jurisdiction, the law of contract (which is largely derived from English law) and case law also form an important part of the law governing M&A.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i The Takeovers Code

To ensure that the Takeovers Code takes account of market developments and developing international practice, it is regularly reviewed by the Executive of the SFC in consultation with the Panel. On 13 July 2018, the SFC introduced certain amendments to the Takeovers Code that came into effect immediately, including an upwards revision of the shareholder voting approval threshold for whitewash waivers from a simple majority of independent votes to 75 per cent of independent votes, with a separate simple majority independent shareholder approval requirement for the underlying transaction.

4 The Takeovers Code states that all circumstances are to be considered, and an economic or commercial test is to be applied (taking into account primarily the number of Hong Kong shareholders and the extent of share trading in Hong Kong), in deciding whether a company is a public company. For the purposes of the CO, a private company is a company incorporated in Hong Kong that, by its articles of association, restricts the right to transfer its shares; limits the number of its members to 50, not including persons who are in the employment of the company and persons who, having been formerly in the employment of the company, were, while in that employment, and have continued after the termination of that employment to be, members of the company; and prohibits any invitation to the public to subscribe for any shares or debentures of the company (Section 11 of the CO).

5 Under the ’one country, two systems’ approach, implemented after the transfer of sovereignty over Hong Kong to the People's Republic of China (China) on 1 July 1997, Hong Kong remains a common law jurisdiction.

6 English case law has persuasive authority only and is subject to interpretation by the Hong Kong courts.

7 Source: Consultation Conclusions on proposed amendments to the Codes on Takeovers and Mergers and Share Buybacks, SFC (https://www.sfc.hk/edistributionWeb/gateway/EN/consultation/conclusion?refNo=18CP1).
ii Listing Rules

The Listing Rules reflect currently acceptable standards in the marketplace and are designed to ensure that investors have, and can maintain, confidence in the market. To ensure that the Listing Rules take account of market developments and developing international practice, the SEHK regularly reviews the Listing Rules and may, subject to the approval of the SFC under Section 24 of the SFO, make amendments to the Listing Rules. Effective from 30 April 2018, three new chapters were added to the Listing Rules, together with consequential amendments, to:

a permit listings of biotech issuers that do not meet the normal financial eligibility tests under the Listing Rules;
b permit listings of companies with weighted voting rights structures; and
c establish a new concessionary secondary listing route for Greater China and international companies that wish to list on a secondary basis in Hong Kong.8

These changes aim to facilitate the listing of companies from emerging and innovative sectors on the SEHK. As stated above, there were a total of 218 newly listed companies on the SEHK in 2018, compared to 174 newly listed companies in 2017.

Separately, the SEHK is proposing to tighten the rules on backdoor listings and the continuing listing criteria to address concerns over the perceived negative impact of increased market activities related to shell companies. The SEHK issued a consultation paper on its proposed rule amendments in June 2018,9 and will publish its consultation conclusions in due course.

iii The CO

The CO came into effect on 3 March 2014. Various key concepts under the CO that are relevant in the context of M&A are as follows:

a the requirements for approving a scheme of arrangement differ depending on the type of scheme. For privatisation schemes and members’ schemes involving a takeover offer or a general offer, the disinterested shares test (which requires not more than 10 per cent of the total voting rights attached to all disinterested shares to be voted against a proposal) applies so as to align with the requirement under the Takeovers Code in the context of a takeover. The headcount test (which requires that a majority of the shareholders of the target company voting on a scheme of arrangement (either in person or by proxy) must vote in favour of it) applies to creditors’ schemes and members’ schemes not involving a takeover offer or a general offer, and in these situations, the court is given discretion to dispense with the test in appropriate circumstances;
b a company and its wholly owned subsidiaries may amalgamate and continue as one company without the sanction of the court provided that certain conditions are met. Such conditions include, for example, that each amalgamating company is a Hong

Kong-incorporated company limited by shares, that each amalgamating company is solvent and that no creditor of an amalgamating company will be prejudiced by the amalgamation;

c. general prohibition on private and public companies providing financial assistance for an acquisition of shares in itself, and streamlined whitewash procedures are extended to listed companies. In addition, it is expressly provided that a company is not prohibited from giving financial assistance for the purpose of an acquisition of shares in its holding company if the holding company is incorporated outside Hong Kong; and

d. increased flexibility for companies to structure and organise their share capital in light of updated concepts relating to share capital (par value (or nominal value), share premium and the requirement for authorised capital have been abolished). Despite the absence of share premium, merger relief continues to be available. The amount required to be recorded as share capital in respect of the consideration shares issued by an acquiring company is the subscribed capital attributable to the acquired shares.

Significant controllers register

To enhance the transparency of company ownership and control, from 1 March 2018, all Hong Kong-incorporated companies (except those listed in Hong Kong) are required to create and maintain a register of significant controllers pursuant to Part 12 of the CO. A company's significant controllers are, in broad terms, natural persons and corporate entities immediately above the company in the ownership chain with significant control over the company.

Companies (Amendment) (No. 2) Ordinance

On 1 February 2019, the Companies (Amendment) (No. 2) Ordinance 2018 came into effect. This Ordinance amends certain provisions of the CO to improve its clarity and facilitate business in Hong Kong, one notable amendment being a clarification that subsidiaries of a non-Hong Kong holding company may take advantage of the court-free procedure for horizontal amalgamation under the CO provided the merging companies are Hong Kong companies.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Given Hong Kong's position as a hub for investment into China, its status as a major regional financial centre, and the widespread use of offshore companies for investment into and out of China, a substantial number of transactions have foreign involvement, including in the form of acquisitions by offshore companies. An analysis by reference to foreign involvement in transactions is therefore not particularly meaningful.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

A key trend observed in 2017 was the increased use of consortium structures involving both private equity and strategic investors to undertake acquisitions as a means of sharing risk and creating value through synergies. This trend continued in 2018, with examples such as CK Group’s proposed consortium bid for Australia’s APA Group Limited, which is described in more detail below, and the US$200 million investment by a group of investors led by
Sequoia China in Klook Travel Technology Limited, a Hong Kong-based travel activities and services booking platform. Another trend observed in 2018 was the increased interest in deals with a technology focus. Examples include Alibaba Group’s acquisition of China-based online food delivery platform Ele.me and the Tencent-led investment in UBTECH Robotics, a China-based intelligent humanoid robots manufacturer.

The most active sectors for M&A activity in Hong Kong in 2018 included technology and fintech, energy and infrastructure, logistics, real estate, financial services and consumer. It is expected that interest in these sectors will continue in 2019.

There were numerous high-profile M&A transactions in 2018. The largest proposed outbound deal was the bid by a consortium led by CK Asset Holdings Limited in June 2018 to acquire all outstanding shares in APA Group Limited for approximately A$12,979 million. APA Group Limited is listed on the Australian Securities Exchange and is a major natural gas pipeline operator in Australia. Although the proposed transaction was recommended by the board of directors of APA Group Limited and was approved by the Australian Competition and Consumer Commission, the Treasurer of the Australian government vetoed it in November 2018 on the basis that the proposed deal would be contrary to the national interest as it would result in a single foreign company group having sole ownership and control over Australia’s most significant gas transmission business.

A notable tech transaction was the Series C equity financing announced in June 2018 by Ant Small and Micro Financial Services Group Co, Ltd (Ant Financial), an affiliate of Alibaba Group Holding Ltd, which raised approximately US$14 billion. This fundraising included a US dollar tranche, which was backed by global institutional investors such as GIC Private Limited, and a renminbi tranche, which was primarily supported by existing Ant Financial shareholders. Ant Financial has confirmed that it would use the funds raised to accelerate globalisation plans for its Alipay payment platform, one of the largest online payment platforms within China, and to invest in developing financial technology.

As a significant number of companies whose shares are listed on the SEHK have controlling shareholders, there is not a large number of unsolicited M&A offers. Nonetheless, in 2018, there was a rare hostile takeover attempt by Re Strategic Investments Pte Ltd (Re Strategic), which operates under the control of PAG Real Estate, to acquire a controlling stake in Spring Estate Investment Trust (Spring REIT). Spring REIT is a real estate investment trust that primarily invests in real estate in China. Re Strategic was one of the substantial unitholders of Spring REIT, and PAG Real Estate is an Asian alternative investment fund. The offeror sought to acquire a controlling stake of Spring REIT in order to replace the manager. Although the initial offer price was subsequently revised, the acceptance condition was not met and the bid was ultimately unsuccessful.

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In addition, there were a number of high-profile proposed privatisations of Hong Kong-listed companies in 2018, including GuoLine Overseas Limited’s failed proposed privatisation of Hong Kong-listed Guoco Group Limited and Swire Pacific Limited’s successful privatisation of Hong Kong Aircraft Engineering Company Limited.¹⁷

VI  FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

In common with many jurisdictions, Hong Kong’s Takeovers Code requires an offeror to have certainty of funds to make an offer for a public company. Under the Takeovers Code, an announcement of a firm intention to make an offer should include a confirmation by a financial adviser (or another appropriate third party) that resources are available to the offeror sufficient to satisfy full acceptance of the offer (a sufficiency statement). Such confirmation is not only required when the consideration is cash, or includes an element of cash, but also when the consideration consists of, or includes, any other assets except new securities to be issued by the offeror. The executive may also require evidence to support the sufficiency statement, and evidence that the offeror has sufficient resources to complete the purchase of shares that gives rise to the offer obligation.

Depending on how an acquisition is structured, M&A transactions in Hong Kong are usually financed by:

a  internal resources;
b  shareholders’ loans;
c  equity issues;
d  debt issues;
e  loan facilities from banks and financial institutions; or
f  a combination of two or more of the above.

VII  PENSIONS AND EMPLOYMENT LAW

Under Hong Kong law, there is no specific regulation that provides for the transfer of employment contracts when there is a change of ownership of a business, as opposed to an employing company. Employment contracts would therefore be terminated in the case of an acquisition of a business, and the new employer would have the freedom to decide whether to enter into new employment contracts with existing employees. However, generally speaking, where termination of an employment contract takes place due to a transfer of business, this would constitute redundancy, and employees previously employed may be entitled to severance payments and long-service awards, for which the old employer would be liable. However, under Sections 31J and 31C of the Employment Ordinance (EO), severance payments and long-service awards are not payable in the case of a business transfer if, not less than seven days before the end date of an employee’s previous contract, the new employer has offered to renew the employee’s contract, or to re-engage him or her under a new contract, on no less favourable terms and conditions, and the employee has unreasonably refused that offer. If an offer of renewal or re-engagement is accepted by the employee, the new contract has effect as if the renewal or re-engagement had been a renewal or re-engagement by the old employer.

without any substitution of the new employer; therefore, the employment relationship will be regarded as being continuous for the purposes of the EO. Any redundancy issues that may arise in future disposals of the business would be passed to the new employer after the renewal or re-engagement.

Generally speaking, under the Mandatory Provident Funds Schemes Ordinance (MPFO), an employer must enrol its employees as members of one of the registered MPF schemes (as defined in the MPFO) available in the market in Hong Kong. An employer may enrol different employees in different registered schemes. During the contribution period (as defined in the MPFO), the employer must contribute to the registered scheme from its own funds an amount determined in accordance with the MPFO, and deduct from employees’ relevant income for that period as a contribution by the employees to the scheme a further amount determined in accordance with the MPFO. An employee and an employer may make additional voluntary contributions to the employee’s scheme.

Where there is a proposed disposal of a business, the existing employer and the proposed new employer should consider the implications of the MPFO and arrangements to deal with the accrued benefits of employees under the applicable MPF scheme. If a merger or acquisition is to be effected by way of a share sale, it is not likely that there will be MPF implications (unless the target company is spun out from a group of companies that operates a group-based scheme), as the merger or acquisition will not involve a change of employer. The surviving party or acquirer would nevertheless be well advised to carry out due diligence to ensure that all target employees are employed by the target company on terms that comply with the MPFO.

However, if a merger or acquisition is to be effected by way of a business transfer involving a change of employer, the employee must, in accordance with Section 14 of the MPFO, elect to transfer the accrued benefits to a contribution account under the new employer’s MPF scheme, retain the accrued benefits in the previous MPF scheme under a preserved account or transfer the accrued benefits to a preserved account of another MPF scheme.

Both the seller and the buyer must observe and comply with the requirements of the MPFO with respect to the transfer of the accrued benefits of employees.

On 1 May 2011, the Minimum Wage Ordinance came into effect in Hong Kong and introduced a statutory minimum wage. The statutory minimum wage was raised by 8.7 per cent from the previous rate with effect from 1 May 2019.

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18 Section 31J of the EO.
19 Subsection 3 of Section 31J of the EO and Paragraph 5 of Schedule 1 of the EO.
20 Under the MPFO, an employer means any person who has entered into a contract of employment to employ another person as his or her employee.
21 A contribution account is an account mainly used to accumulate MPF contributions in respect of current employment and investment returns.
22 A preserved account is an account in which accrued MPF benefits in respect of former employment are held.

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VIII TAX LAW

Hong Kong’s competitive economy is reflected in the transparency, predictability and simplicity of its low-rate tax system. These attractive qualities mean that, unlike many other jurisdictions, Hong Kong tax is generally not the determining factor in the way in which a transaction is structured in Hong Kong. There is no capital gains tax on the disposal of assets, including the disposal of shares and property. In addition, dividends are not classified as taxable income, and there is no withholding tax on dividends.

Stamp duty on the transfer of Hong Kong shares is currently 0.2 per cent of the consideration paid (or market value), and is generally payable in equal shares of 0.1 per cent by both the seller and the buyer. Transactions that are structured as schemes of arrangement do not attract stamp duty. Stamp duty on the transfer of immovable non-residential property in Hong Kong ranges from 1.5 per cent (for transactions up to HK$2 million) to 8.5 per cent of the amount or value of the consideration (for transactions over HK$21,739,130) and is usually paid by the purchaser.23 The Stamp Duty Ordinance is the principal source of legislation governing this area.

The Inland Revenue Ordinance sets out three separate taxes on income: profits tax, salaries tax and property tax. Liability to tax under these three heads, as a general rule, is limited to persons or entities carrying on a trade, profession or business in Hong Kong, and to income that arises in or is derived from Hong Kong. To this extent, the residence status of persons and companies is irrelevant to income tax assessment. For the year of assessment from 2018 to 2019 onwards, a two-tiered profits tax rate applies. Corporations are taxed at 8.25 per cent on assessable profits up to HK$2 million and 16.5 per cent on any part of assessable profits over HK$2 million, whereas unincorporated businesses are taxed at 7.5 per cent on assessable profits up to HK$2 million and 15 per cent on any part of assessable profits over HK$2 million.

In respect of loan repayments, as a general rule a borrower’s interest expenses will be deductible where the lender is subject to Hong Kong profits tax on its receipt of the interest. In addition, where a financial institution (whether onshore or offshore) makes a genuine loan, interest expenses will generally be deductible.

IX COMPETITION LAW

The Competition Ordinance, Hong Kong’s first cross-sector competition law, came into full effect on 14 December 2015. Previously, only the broadcasting and telecommunications industries were subject to competition law, as provided for in specific provisions of the BO and the TO (now largely repealed). The former TO provided a regulatory framework for the Communications Authority to consent to certain M&A involving carrier licensees in the telecommunications industry.

The Competition Ordinance retains a merger control regime in Hong Kong for the telecommunications industry known as the Merger Rule. Like the regime under the TO, the Merger Rule applies only to mergers involving carrier licensees, and the Communications

23 The same range of stamp duty is applicable to the transfer of immovable residential property executed on or after 23 February 2013 but before 5 November 2016. The stamp duty applicable to the transfer of immovable residential property executed on or after 5 November 2016 is a flat rate of 15 per cent of the consideration or value of the property (whichever is the higher).
Authority has concurrent jurisdiction with the Competition Commission in relation to the Merger Rule. However, unlike the merger regime under the TO, the Competition Ordinance does not specify thresholds upon which regulatory consent is triggered. Instead, the Merger Rule refers to the acquisition of control, which could apply even if the acquisition involves a minority interest not exceeding 30 per cent. A merger could be prohibited if it has or is likely to have the effect of substantially lessening competition in Hong Kong. It is worth noting that notification of mergers is voluntary rather than mandatory, but in practice the Communications Authority is consulted in most (if not all) cases, even when no competition concerns are expected.

Since the entry into force of the Competition Ordinance, the Communications Authority has reviewed four transactions under the Merger Rule to date. In each of these cases, the Communications Authority decided not to commence an investigation either on the basis that each transaction was unlikely to have the effect of substantially lessening competition in Hong Kong or, in respect of the most recent case, on the basis that the commitments offered by the parties addressed effectively the competition issues identified. The first such decision under the Competition Ordinance, announced by the Communications Authority on 31 March 2016, was in respect of the indirect acquisition of New World Telecommunications Limited, a carrier licensee under the TO, by HKBN Ltd, the holding company of Hong Kong Broadband Network Limited, another carrier licensee under the TO. The second decision, announced on 10 November 2016, was in respect of the HK$9.5 billion acquisition of the entire equity interests of Wharf T&T Limited, a carrier licensee under the TO. More recently, on 3 October 2017, the Communications Authority announced it had decided not to commence an investigation under the Competition Ordinance in respect of the acquisition by Asia Cube Global Communications Limited of the entire equity interests of Hutchison Global Communications Investment Holding Limited, which wholly owns Hutchison Global Communications Limited, a carrier licensee under the TO. The latest case concerned the proposed acquisition by HKBN Ltd of WTT Holding Corp, both of which hold carrier licences under the TO. On 17 April 2019, the Communications Authority accepted commitments from the merging parties to address competition issues that it had identified as being likely to arise relating to building access and wholesale service provision. The Communications Authority decided to accept the commitments and not to commence an investigation into the proposed transaction.

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24 New World Telecommunications Limited is indirectly owned by Concord Ideas Ltd.
27 Green Energy Cayman Corp is indirectly owned by MBK Partners and TPG Capital.
29 Asia Cube Global Communications Limited is wholly owned by a fund managed by I Squared Capital, a private investment firm.
In the run-up to the drafting and passing of the Competition Ordinance, which, on the whole, was supported by the public, there was some debate about whether there is a need for merger control in Hong Kong to govern general M&A activity (outside the telecommunications sector). The Public Consultation Paper on Detailed Proposals for Competition Law in 2008 showed a softening of the government’s stance on this issue, from ‘we do not need a merger control regime’ to inviting views on three possible options regarding such a regime. The recommendation of the Commerce and Economic Development Bureau of Hong Kong (CED Bureau) was that merger activities are not to be regulated except in the telecommunications sector, which is already subject to such regulation under the former TO. The CED Bureau stated that this proposal would give the Competition Commission more time to focus on its initial work of implementing the proposed Competition Ordinance, and would allow for a more effective assessment of whether merger control provisions would be desirable in other (or all) sectors in the future once the Competition Commission has accumulated some experience in the operation of the competition regime. This was the position ultimately adopted in the Competition Ordinance. It has been suggested that the Competition Commission would seek to introduce a fully fledged merger control regime within two to three years of the Competition Ordinance taking full effect. The Competition Ordinance is currently undergoing a review, which will include an assessment of whether a cross-sector merger control regime should now be introduced.

X OUTLOOK

The government has forecast that Hong Kong’s GDP is likely to grow by 2 to 3 per cent in 2019.33 Hong Kong’s economic performance in 2019 will be influenced by, among other things, developments in external demand, the performance of the global economy and geopolitical developments in major advanced economies, for example the trade dispute between the US and China and Brexit.

The increasing trend of protectionist policies by international governments is likely to continue to be a challenge for cross-border transactions involving sensitive industries and strategic assets. Regulatory compliance will be another key challenge. In Hong Kong, the HKSE has stated its intent to address perceived abuses related to reverse takeovers by tightening relevant regulations. Of a wider application is the European Union’s General Data Protection Regulation (GDPR), which came into force on 25 May 2018. The GDPR has extraterritorial reach, applying to all firms with establishments in Europe or that provide goods and services to individuals in Europe. It is, therefore, expected that there will be an increased emphasis in M&A transactions on data protection compliance under the GDPR, from due diligence of target companies to post-transaction integration.

Nonetheless, the M&A market in Hong Kong has remained busy, with 129 M&A deals completed in Q1 2019, with a total disclosed value of US$32.06 billion.34 Despite global challenges, M&A activity in Hong Kong is expected to remain steady in 2019. It

33 Source: 2018 Economic Background and 2019 Prospects, Financial Secretary’s Office, government of the Hong Kong Special Administrative Region (HKSAR) (https://www.statistics.gov.hk/pub/B6XX00042019AN19E0100.pdf). The HKSAR government has stated that its GDP growth forecast is predicated on the assumption that the US–China trade tensions would not escalate from the tariff measures announced as at the time of the publication of its report (in February 2019) or might even ease somewhat.

34 Source: Mergermarket.
is expected that private equity-led transactions will continue to feature strongly, especially in the active tech and fintech sectors. The flow of Chinese outbound investment will likely be maintained in respect of targets that are regarded as prudent and strategic investments in support of the One Belt, One Road initiative, further supported by favourable Chinese policy developments such as the series of measures announced by the People’s Bank of China in May 2018 to further enhance cross-border funds flow management. Therefore, while there are several material variables that could impact on deal appetite in Hong Kong in 2019, the overall outlook of the M&A market in Hong Kong for 2019 remains optimistic.
Chapter 22

HUNGARY

József Bulcsú Fenyvesi and Mihály Barcza

I OVERVIEW OF M&A ACTIVITY

One hundred and seven deals were publicly disclosed in Hungary in 2018, reflecting a decreasing M&A market when compared with 133 published deals in 2017. The estimated size of the M&A market also decreased by 17 per cent in terms of value versus 2017. As in previous years, real estate was the most active industry in Hungary ahead of technology and consumer products. Share of inbound transactions increased from 28 per cent in 2017 to 40 per cent in 2018.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The main source of legislation governing M&A activity and corporate governance in Hungary is Act V of 2013 on the Civil Code (Civil Code), and specifically Book Three, which contains the general rules applicable to all forms of legal persons, including high-level rules on the transformation, merger and demerger of legal persons, and sets forth definitions of the types of legal transformations allowed by Hungarian law.

The provisions constituting the legal framework for transactions in Hungary implemented by way of transformations, mergers or demergers may be found in Act No. CLXXVI of 2013 on the Transformation, Merger and Demerger of Certain Legal Persons (Transformation Act). This contains the prerequisites and procedures to be followed in the case of a company transformation, and the documentation, transparency and financial requirements of mergers, demergers and spin-offs, prescribing specific rules for companies limited by shares, especially in the field of audit and management reports.

In the event that a company involved in a merger is not domiciled in Hungary but in another country of the European Union, in addition to the provisions of the Civil Code and the Transformation Act, the rules laid down in Act CXL of 2007 on Cross-Border Mergers of Limited Liability Companies (Cross-Border Mergers Act) shall also be observed. The Cross-Border Mergers Act serves the implementation of Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005.

The procedural aspects of registering M&A in Hungary are set forth in Act V of 2006 on Public Company Information, Company Registration and Voluntary Liquidation

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(Company Procedures Act). The Company Procedures Act lists the specific documents to be prepared and submitted to court to register a merger or acquisition, and sets out the applicable procedural requirements.

Part Three of Book Three of the Civil Code provides for the regulation of business associations, regulating in Chapter No. XV the aspects of the acquisition of majority interests (i.e., the direct or indirect purchase of 75 per cent of the voting rights) in limited liability companies and private companies limited by shares. These rules set forth a special statutory tag-along right obliging a shareholder who acquires a majority interest to purchase the shareholdings of the other shareholders at least at equity value if such other minority shareholders wish to sell their stake after the acquisition.

Act CXX of 2001 on the Capital Market (Capital Market Act) contains essential rules on issuing and offering securities. Such rules must be observed if any of the target companies concerned with an M&A transaction is a company limited by shares. In respect of publicly traded companies, the Capital Market Act sets forth the specific provisions for the acquisition of majority interests in public companies limited by shares, such as reporting obligations, initial public offerings and minimum offer prices. Tender offers and M&A activity in the financial sector are controlled and approved by the Hungarian National Bank, which became the general supervising authority of financial institutions and markets in 2013. Act CXXXIX of 2013 sets out the scope of activity and the procedural rules applied by the Hungarian National Bank.

In the field of M&A legislation, special rules apply to companies engaged in the energy, media and financial sectors. The acquisition and transformation of such companies may also require the prior approval of the competent regulatory bodies, setting further preconditions and documentation requirements for carrying out a successful merger. The competent authorities for these sectors include the Hungarian Energy and Public Utility Regulatory Authority, the National Media and Infocommunications Authority and the Hungarian National Bank, respectively.

Irrespective of the industry or sector concerned, M&A reaching a certain market threshold shall be reported to, or approved by, the Hungarian Competition Authority (GVH). The reporting obligations and the rules for approval are set forth in Act LVII of 1996 on the Prohibition of Unfair Trading Practices and Unfair Competition.

Besides the above acts and laws, significant parts of foreign investments in Hungary are also protected by way of bilateral investment treaties (BITs). BITs grant basic rights to foreign investors in compliance with international standards, and enable them to seek remedies before international forums if their right to fair and equitable treatment should be violated.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Amendments to the Civil Code

Amendments were made to the Civil Code to clarify or eliminate ambiguities in the new act, as well as to achieve compliance of the act with other laws.

After an essential amendment to the Civil Code in 2016 eliminating concerns about the undesired personal liability of managing directors in relation to third parties, which made it clear that (except in the case of a managing director causing damage intentionally) instead of a managing director being directly and personally liable, a legal entity shall be liable in relation to third persons if its managing director caused damage to a third person when acting
in his or her capacity as managing director, and other notable modifications concerning rules of dividends and collateral, in 2017 further material amendments were brought about in relation to securities.

The regulation of securities was replaced with a new and simplified regime: on the one hand, legal rules outside the Civil Code will have to be observed in depth for detailed rules of securities; on the other, the new unified regulation for dematerialised and printed securities leaves room for legal interpretation as to whether certain rules pertain to dematerialised or printed securities only, or to both of them.

Although the Civil Code compiles the general rules of securities, and detailed rules are incorporated into other pieces of law, it is also worth mentioning that a new act regarding bills of exchange was introduced at the end of 2016, effective from 2017. Besides remaining compliant with the relevant convention regarding bills of exchange, such new legislation contains rules falling within the competence of the Member States, and includes modernised procedural rules applicable in lawsuits regarding bills of exchange.

### Financial and banking regulations

The most important drivers of recent changes in Hungarian financial regulations that can affect M&A transactions have been amendments of the law in relation to implementing EU rules and the introduction of national rules to supplement directly applicable EU regulations. With effect from January 2018, the Hungarian legislator transposed Directive 2015/2366/EU on payment services in the internal market and Directive 2014/65/EU on markets in financial instruments (MiFID II Directive), which led to the amendment of the Banking Act, the Investment Services Act and the Capital Markets Act, and to the adoption of a new Decree 35/2017 (XII.14) of the Hungarian National Bank on the provision of payment services.

Amendments to the Investment Services Act include the transposition of the MiFID II Directive.

The Hungarian National Bank adopted amendments to its recommendations in connection with risk assessment of encumbered assets and the restructuring of jointly financed corporate debtors. Although these recommendations are not legally binding, they have soft law effect in the Hungarian financial sector due to the fact that the Hungarian National Bank is the supervising authority of the financial market.

Pursuant to these recommendations, the Hungarian National Bank set out a guideline to credit institutions regarding which assets are qualified as encumbered assets. Generally, any asset is deemed as encumbered if the asset is pledged or is subject to any dealing as a security or for improving an institution’s credit rating, and cannot be freely withdrawn from such dealings. As a non-exhaustive list, the encumbrance may arise from, inter alia, secured payment guarantees, securities granted for dealings on derivatives, security agreements, secured financing agreements and secured bond issuing. Based on the recommendations, the Hungarian National Bank requires that a risk assessment of encumbered assets includes an evaluation of risks arising from changes in the value of the encumbered assets, and the

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3 Act CCXXXVII of 2013.
5 Recommendations 6/2017 (V.30) and 14/2018 (III.6) of the Hungarian National Bank.
risks and characteristics of local markets. Furthermore, credit institutions are required to monitor the level of encumbrance over the encumbered assets, the reason for encumbrance, the amount of assets free of encumbrance and any changes thereof.

Upon the restructuring of jointly financed debts, the Hungarian National Bank requires constructive, good-faith negotiations between creditors and a debtor. It is recommended that the creditors involve independent advisers to reach a mutual agreement in the restructuring phase, and credit institutions should develop internal policies about the restructuring of debts, which policies are in line with their general strategy in connection with non-performing corporate loans. The Hungarian National Bank recommends that credit institutions not only calculate the direct operation costs of the debtors when granting a bridge loan: they shall also evaluate whether the payment of any taxes and publicly due burdens may be included in the scope of the bridge loan to avoid any enforcement of such obligations, which could endanger the restructuring procedure. Creditors shall require that the debtor put forward a plan to maintain continuous operation and to give regular updates of its financial status. Creditors shall also check and ensure that the bridge loan does not breach any obligations of the debtor towards any creditors that are not participating in the restructuring procedure. In the event that such breach is threatening, the consent of that creditor to the bridge loan shall be required. The Hungarian National Bank considers a restructuring effective if the continuation of the debtor's operation is restored and the debtor remains able to discharge its obligations following the restructuring.

### Administration and proceedings

Pursuant to changes introduced in 2016, administrative aspects of transactions have become simpler and more client-friendly. Under an amendment to the Company Procedures Act, changes in company data (including the deletion of a company from the company registry) are now reported to all the competent authorities by the Hungarian court of registry, instead of the company (or its legal successor) having to notify all the relevant authorities separately. Furthermore, certain changes in company data may now be reported to the court of registry free of any procedural fees. In 2017, the registration of certain corporate changes became quicker for companies limited by shares, and a specific procedure was regulated for private companies limited by shares for going public.

As a consequence of a new codex on Hungarian civil proceedings, adopted in 2016 and coming into force as of 1 January 2018, further changes have arisen regarding certain aspects of company proceedings, and remarkable changes have been introduced regarding litigation that also affect potential litigation related to companies or transactions. Increased attention will have to be paid to such new rules to successfully proceed and litigate under the new civil proceedings regime.

Although it is not a new piece of legislation, a trend significantly affecting companies in 2018 was the increasing requirement of compliance with the General Data Protection Regulation. Such compliance is now thoroughly observed in the course of M&A transactions, and a number of investors and purchasers have required targets and sellers to ensure compliance to the best of their abilities.

In 2018, the Parliament adopted the Security Review Act. Under the Act, transactions requiring ministerial approval (i.e., they may not be implemented before such approval is granted) are:

a. those to be carried out by a foreign investor (an investor resident or registered in a country outside of the EU, the EEA or Switzerland);

b. those relating to certain specific strategic activities (activities concerning national security such as defence, dual-use products, cryptography and wire-tapping products, government IT services as well as key services in the financial, energy and telecoms sectors); and

c. those whose implementation is considered a triggering event (e.g., acquisition of at least a 25 per cent (10 per cent in the case of a publicly listed company) ownership ratio – direct or indirect – in an existing or newly founded Hungarian company); those registering a Hungarian branch office for the purpose of carrying out strategic activities; or those extending the scope of their activities of a Hungarian company to strategic activities.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Although the deals with the highest transaction value in 2018 involved foreign parties, as in previous years, the Hungarian market was dominated by domestic transactions (where both the target and the buyer were Hungarian), representing 48 per cent of all disclosed transactions in 2018 over foreign transactions.

Regarding transactions related to foreign targets or buyers, inbound transactions were also dominant (40 per cent of the disclosed transactions). Inbound foreign investments came from the UK, France, Switzerland and the Czech Republic.

Outbound transactions remained at a rather low level (12 per cent of all disclosed deals).

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

Considering publicly disclosed transactions, the absolute leading sector in terms of the number of deals in 2018 was real estate, with 27 deals, which is the same number that was seen in the previous year.

The second sector behind real estate was technology, where there were 15 transactions published in 2018, an increase from the 11 during the same period in 2017.

Further active sectors in 2018 were consumer products and retail, healthcare and banking and capital markets.

In line with the previous year, strategic investors were in a majority in Hungary in 2018. Approximately 74 per cent (79 deals) of the deals were executed by strategic investors.

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6 Act LVII of 2018.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

In the past couple of years, financial institutions have cleared significant parts of their non-performing loan (NPL) portfolios from their balance sheets either by selling them to third-party bidders, or by restructuring them into subsidiaries to operate and manage the NPL portfolios separated from the parent financial institution. Consequently, in recent years, many transactions have focused on the restructuring of currently existing debts and portfolios. In 2017, corporate lending increased by 10.4 per cent.7 Within such dynamic increase, the credit amount granted to small and medium-sized enterprises (SMEs) increased by 12 per cent. The increase in the market was also influenced by sizeable single transactions. The largest expansion was seen in the energy sector, with a 38 per cent increase since 2016,8 which included the acquisition of the Mátrai Power Plant by Opus Global Nyrt.9

Because of the divestment of NPL portfolios and the financial crisis, several Hungarian financial institutions have adopted a more specialised focus and policy in relation to the projects and investments they are willing to finance. Knowing these policies and the drivers of credit institutions can be a key factor when selecting a financier. Therefore, choosing experienced advisers on the borrower side who can also support investors in selecting the right financier for their project has become even more important. Nevertheless, in general, banks are competing for good projects and investors after years of deleveraging in the Hungarian economy. Based on a report of the Hungarian National Bank, in the last quarter of 2017 financiers loosened their strict criteria on corporate lending. Banks are calculating further growth in the outstanding credit amount (substantially as long-term credits). Subsidised loans and financing are also available to certain investments and projects (e.g., renewables). However, access to these is rather limited.

Interest rates for credits denominated in Hungarian forints or in a foreign currency decreased in 2017. Credits are generally granted in Hungarian forints or in euros. However, changes in the currency exchange rate still pose a risk. Since the beginning of April 2018, the forint/euro exchange rate has deteriorated by 3.5 per cent, and at the time of writing, it currently stands, with minor fluctuations, at 319 forints to one euro.10

Equity funds are also active in Hungary. Such funds are mainly either financed by the state, state-owned institutions and entities, or by the European Union. Although private equity funds are present in Hungary, their activity level and net investments are still low in the whole CEE region. The share of private equity funds from the overall volume of transactions has not significantly developed in recent years.

To facilitate the lending activities of private equity, the Hungarian National Bank and the state-owned Exim Bank have launched several equity funds, including hedge funds. These funds have clear investment policies to support and promote projects and transactions that are beneficial for Hungary’s public affairs. Additionally, in 2017 multiple private equity funds were created to finance acquisitions of specific strategic companies (e.g., the acquisition of MKB Bank Zrt by Metis Private Equity Fund). Although these private equity funds took part in large transactions, the aggregate volume of funds held in such companies is still relatively low compared to other regions.

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8 M&A Barométer Magyarország 2017, published by Ernst &Young Tanácsadó Kft.
9 https://index.hu/gazdasag/2017/12/14/meszaros_cseh_ceggel_osszeallva_viheti_a_matrai_eromuvet/.

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Furthermore the government, co-financed by the European Union, is making new funds available to the investment market. Such new investment funds will support mainly SMEs and research and development projects.

VII EMPLOYMENT LAW

There have been no major legislative changes in the employment rules in connection with corporate transformations in Hungary in the past couple of years. However, we are experiencing a slight change of focus when it comes to mergers or acquisitions of businesses also involving a transfer of personnel. The Hungarian labour market has always been sensitive to such changes. Corporate changes and reorganisations have often been associated with mass layoffs, and recently, in several instances, the closure of plants and business units as well. In general, trust in employers is usually lower than it is in Western Europe. Consequently, this may cause loss of talent or key personnel even before the conclusion of a transaction. Therefore, in the course of a transaction, communication is of paramount importance, and it is similarly vital to maintain good relationships with employee representatives, and to pay attention, to retain key personnel to safeguard operations and preserve the business potential of a target.

It is usual to decide early in the planning phase of a transaction whether the employees of the target will be retained by the purchaser. Rules pertaining to mass layoffs and transfers of undertakings, including the protection of employees’ rights, are harmonised with the respective EU directives and remained unchanged in 2018. However, beyond the general rules on the protection of employees, and consultation and announcing obligations, individual communication with employees is just as important both in the case of a mass layoff and in an M&A transaction in which the employees of the transferred business unit are intended to be retained.

Considering that shortages can be experienced on the Hungarian market for several key workforce positions, retention of key staff can sometimes be more challenging than layoffs. In several cases, interim loyalty or other types of incentive schemes may be of great help for a purchaser in retaining experienced and valuable staff. Sometimes, putting restrictive covenants in place specifically for the purposes of a transaction may also work well.

VIII TAX LAW

Under Hungarian law, specific rules regarding M&A, spin-offs and divisions of companies are regulated by Act LXXXI of 1996 on Corporate Tax and Dividend Tax, which has to be interpreted together with the general rules of the Hungarian civil law on business associations.

i Corporate tax

The biggest recent change in the legislation relevant to M&A and companies in Hungary is the change in the corporate income tax rate.11 Until the end of 2016, the corporate income tax rate was 10 per cent of the positive tax base (accounting profits adjusted with certain items)
up to 500 million forints, and 19 per cent above 500 million forints. From the beginning of 2017, the corporate income tax rate is 9 per cent of the positive tax base, regardless of any threshold.

As of 2018, large companies in the central region of Hungary are entitled to a tax credit under certain circumstances, including for investment projects resulting in product diversification or new procedural innovation; and for investment projects with a value of at least 6 billion forints, and of at least 3 billion forints in the case of investment projects serving to create jobs.

Again as of 2018, favourable corporate tax rules for notified shares may be applied also for shareholdings under 10 per cent.

ii  Revaluation of assets and tax base adjustments
In the case of a transformation of a company structure, fixed assets (+/-), liabilities (+/-), receivables (-) and provisions (+/-) can be revaluated.

The corporate tax base normally has to be adjusted by the revaluation difference mentioned above at the predecessor, and by the difference between the accounting net book value and fiscal net book value of tangible and intangible assets at the predecessor and in the case of a spin-off at the successor (in the tax year of the transformation).

However, in the case of preferential company transformations it is possible to avoid corporate tax adjustments. The conditions for the preferential company transformation status are that both the predecessors and successors must be companies, none of the shareholders of the predecessors acquire more than 10 per cent cash over the acquisition of shares of the successor and there is no change in the proportion of the shareholders in the case of a spin-off (a merger into the only shareholder of a one-person company is also considered to be a preferential transformation).

In the case of a preferential company transformation, corporate tax adjustments may be avoided if the following conditions are met: the successor keeps a record of all assets and liabilities taken over from the predecessor as if no reorganisation had taken place (it has to continue the records with the same purchase value, and accounting and fiscal net value); the deed of foundation of the successor refers to this liability; and the preferential company transformation status is referred to in the corporate tax return of the predecessor.

iii  Asset deals
A sale of assets of a company is usually subject to corporate tax. The taxable profit is the difference between the selling price and the fiscal net book value of the assets. However, it is possible to avoid corporate tax impacts in the case of a preferential asset deal where an independent division of the company (with its own structure, assets and ability to operate) is sold to a buyer in exchange for the acquisition of shares.

Similar to a preferential company transformation, the special rules can be applied if:

- a) the asset transfer agreement lists all assets, liabilities and accruals (including purchase values, net accounting and fiscal book values), and has a declaration to apply special accounting rules;
- b) the buyer keeps all assets taken over in its books as if no asset deal had taken place (e.g., it continues the records with the same purchase value, accounting and fiscal net value as taken from the seller); and
- c) the seller reports the preferential asset deal status in its corporate tax return.
iv Real estate companies
A transfer of real estate may be subject to property transfer duty not only in the case of an asset deal but also a share deal, if a company is considered to be a real estate company having at least 75 per cent real property within its total assets (not including cash, receivables and accruals). The general transfer duty rate payable by the buyer is 4 per cent up to 1 billion forints and 2 per cent over such amount. This regulation is applicable to indirect owners as well, but there are exemptions for related companies having a registered principle business activity of real property selling, leasing or management.

v Transfer pricing
As of 2018, a new transfer pricing regulation came into force. The aim of the new regulation is to introduce changes to comply with the requirements set forth by the EU Joint Transfer Pricing Forum.

IX COMPETITION LAW
i New turnover thresholds
As of 15 January 2017, new turnover thresholds were introduced into the Hungarian merger control law. According to these, a concentration shall be notified to the GVH if the aggregate net turnover in and from Hungary of all undertakings concerned exceeded 15 billion forints in the last audited financial year, and the net turnover in and from Hungary of each of at least two of the undertakings concerned exceeded 1 billion forints in the last audited financial year (this latter threshold was raised from 500 million forints).

Even if the above thresholds are not met, the GVH may investigate a transaction within six months after its implementation if it is not obvious that the merger would not have a significant impediment on effective competition, in particular by creating or strengthening a dominant position; and the aggregate net turnover in and from Hungary of all undertakings concerned exceeded 5 billion forints in the last audited financial year. In such cases, however, no suspension obligation applies.

According to a GVH notice, a concentration shall be regarded as obviously not significantly impeding effective competition if the parties' combined market share does not reach 20 per cent on any overlapping (horizontal) markets or 30 per cent on vertically related markets (or, where such market shares are reached, the market share increment stemming from the concentration is below 5 per cent).

ii Calculation of turnover
The recent amendments have introduced a change in the calculation of turnover of Hungary-based companies. Prior to the amendments, in the case of entities incorporated in Hungary, all of their net turnover, whether from sales within or outside of Hungary, had to be taken into account. As of 15 January 2017, again in the case of Hungary-based entities, it is only the net turnover from sales into Hungary that shall be taken into account for the purposes of the turnover calculation (i.e., export sales shall be deducted).

12 http://abt.hu/hu/adozasi-hirek/.
iii Procedure and filing fee

Transactions that obviously do not significantly impede effective competition will be cleared within eight calendar days (fast-track procedure). A formal merger control procedure will only be initiated in cases where, on the basis of a notification, such impediment on effective competition cannot be obviously excluded, where the notification is regarded as incomplete by the GVH or where the special approval of the Media Council is required.

In the case of fast-track procedures, the filing fee is reduced to 1 million forints. The filing fee for regular Phase I and Phase II proceedings has remained unchanged (altogether, 4 million forints for Phase I procedures and 16 million forints for Phase II procedures).

iv Recent developments in case law

Since 2016, the GVH has begun imposing significant procedural fines in merger control proceedings for incomplete or incorrect data supply. In cases Vj-33/2016 and Vj-1/2017, following the issuance of a clearance decision, the GVH discovered that the notifying parties had provided incorrect information regarding the group structure or the relevant markets. These clearance decisions were therefore revoked, and substantial procedural fines (7 million forints to 75 million forints) were imposed. The GVH has also been recently more vigilant in cases concerning a breach of the suspension obligation: for example, it imposed such fines in early 2018 in case Vj-44/2017.

X OUTLOOK

As a consequence of a new codex on Hungarian civil proceedings adopted in 2016, which came into force as of 1 January 2018, further changes have arisen regarding certain aspects of company proceedings, and remarkable changes have been introduced regarding litigation that also affect potential litigation related to companies or transactions. Such new rules will have to be paid increased attention to successfully proceed and to litigate under the new civil proceedings regime. The coming months or years will be a notable period for the interpretation and practice of the new procedural rules to crystallise.

Legislation has been adopted to simplify registrations and make official proceedings simpler and quicker, which may have a positive impact on registration proceedings related to M&A transactions. Among other things, to simplify the registration of company data, commercial courts will be notified by certain other authorities to register changes to certain data of persons registered in a company's registry automatically or \textit{ex officio}, sparing the registration of such changes by the company in separate proceedings.

Compliance with the General Data Protection Regulation is still a continuing trend, and some aspects are expected to be crystallised in practice.
Chapter 23

ICELAND

Hans Henning Hoff1

I  OVERVIEW OF M&A ACTIVITY

In 2019, the Icelandic economy is facing its first downturn after the very strong phase seen since the start of the country’s economic recovery from the crisis that started in 2008. This downturn is to some extent due to the bankruptcy of WOW air in late March 2019, which resulted in a severe decrease in the number of tourists travelling to Iceland. However, while the tourism sector had greatly helped the Icelandic economy and stabilised the Icelandic krona, a slowdown of the tourism boom had been expected for some years.

There was a considerable number of M&A during the past year spanning the whole range of industries existing in Iceland. In the tourism sector, the Icelandair hotel chain, which was put up for sale last year, appears to have been acquired by the Malaysian Berjaya Corporation. While a Marriott hotel is currently being built next to Harpa, Reykjavik’s iconic concert and convention centre at the Reykjavik harbour, for about US$175 million, the share of the developer Carpenter & Company in the project has decreased, and a number of Icelandic investors have stepped in, increasing their share to 66 per cent. Another transaction in the energy sector was the US$373 million spent by an investment vehicle held by 14 Icelandic pension funds together with Ancala Partners on a 66.6 per cent share in HS Orka. HS Orka produces geothermal energy in south west Iceland, and also owns a 30 per cent stake in the Blue Lagoon, which is one of the top destinations for tourists in Iceland.

There was even some public M&A activity. An investment company named AU 3 ehf. made a takeover bid for a 27 per cent stake in Heimavelli, a listed real estate company, but had to withdraw its bid after the stock exchange operator declined the request of 81 per cent of the shareholders to delist the company.

There were also some notable deals in the seafood sector. Iceland Seafood International acquired the Icelandic seafood company Solo Seafood for US$65 million. Solo Seafood owns the distribution company Icelandic Iberica, which is mostly active in Spain. Following the acquisition of HB Grandi by Brim last year, Brim sold its 33 per cent share in the seafood company VSV Iceland for US$75 million.

At the same time of the demise of WOW air, Icelandair, the former national carrier, strengthened its capital base, while US-based PAR Capital Management acquired a 12.4 per cent stake in the company investing US$44 million.

Prosthetic producer Össur withdrew from the stock market in Reykjavik, and it has been listed in Copenhagen alone since 2017. In addition, the country’s largest listed

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company, Marel, which produces fish and meat-processing machinery, has taken up a dual listing, with its stock now being traded on the Amsterdam stock market in addition to being listed in Iceland.

The restructuring and repayment of the national foreign debt is still occurring much faster than scheduled initially. The tourism sector has even out-rivalled the fishing sector, and the earnings of this power-intensive industry with its aluminium smelters and silicon metal plants. With this strong tax income, the state has further decreased its national debt and also refinanced the remaining debts with very favourable conditions. Due to the improved credit rating and the low interest on international markets in general, Iceland managed to issue a bond of over €500 million, which will run for five years and only bears 0.122 per cent interest per year. At the beginning of 2019, the national net debt was 593 billion kronur, which is 23 per cent of GDP. This is a huge step forwards compare to the end of 2013, when the national debt was 50 per cent of GDP.

As in previous years, the four publicly listed real estate companies Reginn, Reitir, Eik and Heimavellir have strengthened their property portfolios.

There is some ongoing debate regarding the renewal and improvement of the country’s infrastructure. For example, under review is how a train system could improve transport in Reykjavik and the area surrounding the city, and the extension or even relocation of existing airports is also being looked into. Because hydropower and geothermal energy make up the largest portion of the energy market, it has taken some time to set up Iceland’s first wind farms; however, the first larger projects have now been realised.

Such infrastructure investment could create opportunities for international and domestic investors alike. Several Icelandic pension funds have thus set up an infrastructure investment fund that aims at financing infrastructure projects in public–private partnerships.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Icelandic legal system is similar to the legal systems of other Nordic countries, and is particularly influenced by the legal systems of Denmark and Norway. However, it is also influenced more by case law than its neighbouring Nordic jurisdictions, and thus its legal system is closer to a common law system. Even though Iceland is currently not aiming for accession to the EU it has, together with Norway and Liechtenstein as the other European Free Trade Association (EFTA) states that are also part of the European Economic Area (EEA), adopted much of the EU legislation due to the EEA rules. However, the Third Energy Package has still not been adopted in Iceland. It is subject to very controversial debates.

Agreements regarding domestic deals up to a certain size are conducted mostly in Icelandic and are fairly short. Larger deals (e.g., with international parties or financing) are usually conducted in English, and the documents are more detailed. The expansion of Icelandic investors into Europe and other parts of the world pre-2008, and the financial crisis bringing foreign creditors into close contact with Iceland, have contributed to bringing domestic M&A documents close to international practice.

It is quite common for privately held companies to have a group of shareholders rather than being held entirely by one person. Therefore, negotiations usually include talks with several shareholders even though the more active shareholders lead the discussions, and speak also for those who have only invested in the company but are not involved in its management.

Main sources of corporate law are the Icelandic Limited Act and the Stock Corporation Act. Transferring shares in a company does not require notarisation. Shareholder lists that
have to be kept by boards do not have to be submitted to the Register of Enterprises, but the Act on Financial Statements requires that shareholders and their shareholdings at year-end are disclosed in companies’ financial statements, which have to be published.

Under both Acts, a squeeze-out of the minority shareholders can be requested if one shareholder holds more than 90 per cent of the capital and votes in a company. Likewise, a minority shareholder can demand redemption of its shares if a single shareholder holds more than 90 per cent of the capital and votes in a company. The articles of association may contain rules about the redemption of shares and the valuation method; only in a stock corporation must there be a statement about this question in the articles of association even if there is no deviation from statute law. The redemption price offered by the requesting party can be challenged by the other party, and if no agreement is reached, court-appointed experts shall determine the price.

The main rules for public takeovers are to be found in Chapter 10 of the Act on Securities Transactions. A mandatory offer to the other shareholders shall be made if a shareholder has acquired 30 per cent of the votes in a listed company, either by its own shareholding or by acting in concert with other shareholders. A mandatory offer shall also be made if a shareholder has gained the right to appoint the majority of the board members. A mandatory takeover bid must be made within four weeks after the shareholder knew or should have known that the relevant threshold had been crossed. The offer period ranges from four to 10 weeks. The decision to make a voluntary takeover offer must be announced without undue delay. If a target company faces financial problems, the Icelandic Financial Supervisory Authority can grant an exemption from the duty to make a mandatory offer to a party that wants to save the company from serious financial problems or that wants to take part in the financial restructuring of the company if its board agrees to this. The breakthrough rule has not been implemented in Iceland. While the Financial Supervisory Authority monitors compliance with these rules, the rules of the NASDAQ OMX Iceland stock market regulate the trading of securities in listed companies.

New foreign direct investments may now be again eligible to tax and other benefits pursuant to the Act on incentives for initial investments in Iceland.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Due to the fact that only a handful of companies remained listed on the Icelandic stock exchange during the turbulence following 2008 and the modest size of the market in general, it is unsurprising that there were few changes in the legislation on takeovers in Iceland after the modernised Act on Securities Transactions entered into force in November 2007. Since then, only minor amendments have been made.

The same applies to corporate law. While there were many changes and debates about changes in insolvency law and restructuring, and competition issues in general, there have been few changes to the corporate law during the past couple of years. However, changes due to the Shareholder Rights Directive and other changes in the legislative EU framework have been adopted.
IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

The Icelandic software company Origo has sold a 55 per cent stake in the software company Tempo, valuing the whole company at US$62.5 million. The purchaser is Los Angeles-based Diversis Capital, which specialises in software and technology companies. Software company Libra was sold to Dutch company Five Degree, again signalling how international the markets have become.

While the privatisation of Íslandsbanki and Landsbankinn has still not been fully accomplished, Arion banki now has more shareholders from the private sector. Two funds managed by Tacomic Capital Advisors purchased a 5 per cent share in Arion for UK£41.8 million. From the bankruptcy estate of Arion’s predecessor, Kaupthing, the fashion company Karen Millen is now for sale, and it is expected that the buyers will be international investors rather than investors from Iceland.

While Iceland has now got a quite active startup scene, quite a few Icelandic startups have managed to procure funds from foreign sources, the latest example being Kerecis with a US$16 million round in order to further enhance its products in the healthcare market.

A mid-cap deal was the divestment of Gear4 by Strax, which sold its subsidiary that produces accessories for mobile phones to ZAGG, which is based in Utah, US, for €35 million (plus a possible earn-out of €9 million).

A smaller outbound investment was the acquisition of the Scottish engineering company KSLD by the Icelandic engineering company Efla. This investment is the last of a series of acquisitions in other European countries such as Norway.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

With the tourism sector slowing down, the focus of investors is more on infrastructure projects, and the past year has shown in general how closely linked the Icelandic economy has become to both the economies of North America and Europe. Because economic activities were in full swing over the past couple of years, virtually all types of transactions – not only public and private deals, but also, for example, management buyouts – can be seen again. Almost all industries are involved. While the large banks are not yet still fully privatised, the concentration of the market continues. The former investment bank Kvika (the successor to Straumur Investment Bank) accomplished four takeovers during the past year. The acquisition of asset management company GAMMA for US$20 was the last in this series, at least for the time being.

With the initial public offering of Arion bank and new shareholders joining, the privatisation of the banking sector has started for the second time since 2003, and questions of Landsbankinn’s future ownership is still of high interest due to the bank’s eminent role in financing many of the larger companies in Iceland.

The concentration of the real estate market, with the large listed companies Reginn, Reitir, Eik and Heimavellir strengthening their property portfolios, continues. The Icelandic Competition Authority has approved Reginn’s acquisitions of two real estate companies named HTO and Fast-2.

As previously mentioned, investment focus has moved slightly away from the booming tourism sector to other parts of the economy and to infrastructure projects.

One of the most thriving sectors is still life sciences. In addition to the pharmaceutical company Alvogen, which is led by former Actavis CEO Robert Wessman, there is quite a number of smaller companies that are increasing their international reach and may, mid-term,
contribute a significant portion to Iceland’s earnings abroad. Often, such development is accompanied by M&A activities, and it is likely that large international players will also acquire some of the Icelandic startups in this field.

Geothermal energy production is currently a hot industry, and up to 7 billion kronur will be spent on research and demonstration projects in the European project Geothermica. In addition, Iceland is participating in the European Strategic Energy Technology Plan, which aims to improve low-carbon technologies. Iceland, with its wealth of renewable energies, is a preferred platform for such projects.

In terms of business success, Marel, the producer of fish and meat-processing technology, must be mentioned in this context. Not only has Marel’s annual turnover continued to grow; Marel has increased its market position in many of its key markets and continues its profitable operations.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

The new banks, Landsbankinn (successor to Landsbanki), Arion banki (successor to Kaupthing) and Íslandsbanki (successor to Glitnir), which took over domestic businesses during the banking crisis in 2008, still have very strong market positions and continue their profitable operations. The privatisation in the banking sector will most probably also impact the financing of deals.

Depending on the parties to an M&A deal, the financing varies. Pension funds and institutional investors often pay in cash. Companies either opt for traditional bank financing or also issue bonds. The bond market in Iceland has picked up again, and faster than the stock market, after the 2008 crisis. The financing of growth in the parts of the economy that have been expanding also depends on the type of investment. In the tourism sector, new hotel buildings have mostly been financed domestically, but the investments of foreign entities in energy-intensive industries seem to be financed from abroad to a considerable extent. Iceland is at a crossroads, with its decades-old tradition of linking almost all loan agreements to the consumer price index. However, this relatively new development that loans are without an indexation seems to get stronger every year.

VII EMPLOYMENT LAW

The Transfers of Undertakings Directive\(^2\) was transformed into Icelandic law in 2002. The Icelandic Act on the Legal Position of Employees in the case of a transfer of an undertaking is applicable if a business unit is transferred in such a way that it maintains it characteristics (i.e., the structure of assets that are used in an economic objective regardless of whether it is a main or ancillary part of the operations). If such a transfer occurs, the rights and obligations of the transferor transfer to the purchaser, and the purchaser shall observe the remuneration and work conditions according to the collective labour agreement until it expires under, or is terminated or superseded by, a new collective labour agreement. The same principle applies in the case of a transfer regarding a bankrupt entity, with the exception that rights because of non-performance by the assignor do not transfer in this case.

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\(^2\) Directive 2001/23/EC.
The transferor and the purchaser shall jointly inform the union workplace representatives (or the employees themselves if there are no representatives) about the date of the transfer, the reasons for the transfer, and the legal, economic and social consequences of the transfer for the employees, and whether any measures are planned regarding the employees. The aforementioned information shall be given well in advance, and if there are plans to take measures regarding the employees, the matter shall be discussed with their representatives (or otherwise directly with them) to reach an agreement. Both parties, transferor and transferee, are obligated under these provisions.

The Icelandic Act on Mass Redundancies is applicable if at least 10 employees are made redundant in a company of 21 to 99 employees, if at least 10 per cent of the employees are laid off in a company of 100 to 299 employees, or if at least 30 employees are made redundant in a company with 300 or more employees. With the objective of reaching an agreement, a decision regarding layoffs shall be announced immediately to union workplace representatives or to another representative elected by employees for that purpose. Regarding cooperation, an attempt shall at least be made to avoid mass redundancies, reduce the number of affected employees or mitigate the consequences for them with the assistance of social measures that have, inter alia, the objective of facilitating a transfer to a new job or occupational retraining.

VIII TAX LAW

A corporation is considered to be resident in Iceland if it is registered here, and if it has its real management here or if its home, according to the company’s articles, is in Iceland.

Because Iceland is not a Member State of the EU, EU Directive 2009/133/EC on mergers is not applicable in Iceland.

There is the possibility of a tax-exempt merger if the absorbed company is completely absorbed by the absorbing company with all assets and liabilities, and the only consideration is shares in the absorbing company excluding any cash component. Under very strict requirements, a tax-exempt cross-border merger is possible. The main criterion for this is that the acquiring company is resident in the EEA or EFTA regions or in the Faroe Islands.

Foreign individuals and legal entities have to pay a withholding tax on dividends received. The applicable rate is 20 per cent for legal entities and 22 per cent for individuals. If dividends are paid from an Icelandic corporation to a foreign limited liability company in the EU or EEA, the withholding tax can be partly or fully refunded after a tax assessment. If a tax treaty is applicable, the withholding tax rate may also be reduced. Interest payments by an Icelandic company to a non-resident are generally subject to withholding tax. The tax rate is 12 per cent. If the recipient is a legal entity, the tax might be reduced according to a tax treaty Iceland is party to. If the recipient is an individual, a small tax-exempt amount is applicable. In a Supreme Court judgment of 2012, it was ruled that interest paid on a loan taken in an acquisition company to finance the acquisition of shares in the target company and that was merged together with the acquisition company in the target company is not deductible.

Regarding thin capitalisation of companies, it should be noted that Iceland only has a general anti-avoidance provision that might be applicable. In addition, a regulation regarding transfer pricing was enacted on 1 January 2015. The regulation applies to businesses with more than 1 billion kronur in revenue or assets, and requires the documentation of transactions between related entities.

The tax base generally follows commercial accounts. The tax resident’s worldwide income is taxable, with the possibility of deducting expenses made to generate that income.
Tax grouping rules allow for a tax consolidation in Iceland, the main prerequisite being a minimum shareholding of 90 per cent in the other companies of the tax group, which must all be in Iceland. There is no difference in the taxation of distributed or retained earnings. The new Act on Stamp Duties, which entered into force on 1 January 2014, provides only for the levying of a stamp duty for the transfer of ownership in real estate and in ships.

IX  COMPETITION LAW

Merger control proceedings are governed by the Icelandic Competition Act, and a notification of a merger is required if the combined revenues of the merging companies reach 2 billion kronur and if at least two of the merging parties have a revenue in Iceland of at least 200 million kronur. For the determination of the revenue, parent companies and subsidiaries are also relevant if they are directly or indirectly controlled by the merging companies.

If a merger has occurred that does not meet the above requirements for triggering a notification duty, but the relevant combined revenue is 1 billion kronur and the Icelandic Competition Authority is of the opinion that the merger may still reduce effective competition, it may order the merging parties to submit a notification of the merger.

The notification of a merger shall be jointly filed by the merging parties after the conclusion of an agreement, the announcement of a public bid or the acquisition of a controlling interest in a company, and before completion of the respective merger. It must not take effect while the Competition Authority is still examining the case. However, upon application, an exemption to this rule may be granted.

Upon receipt of an application, the Competition Authority will notify the parties within 25 working days as to whether it will further look into the case. This notification is a prerequisite to interdict a merger. If a merger is to be interdicted, this must happen within 70 working days from the time of the Competition Authority's announcement that it intends to investigate the matter. If further information is required, the period may be extended by up to 20 working days.

X  OUTLOOK

The economic outlook for Iceland is still rather positive, in particular because the country has the possibility to react to the economic downturn in allowing the krona lower against the main currencies of the countries Iceland doing trade with. Unlike the strategy of the Icelandic National Bank before 2008, there is now a much stronger minimum reserve policy in place, which should result in greater stability for the financial sector and, following indirectly from that, for other businesses.

The general investment climate is still positive and the government, which has been in office since the parliament elections held in autumn 2017, is also pursing many long-term projects that should help to keep Iceland in upcoming years within that group of European countries that are well prepared for the future.

The strong economy, still relatively low unemployment rate and highly educated population, along with the country’s wealth of energy and natural resources, offer a stable environment for M&A activities in Iceland.
I OVERVIEW OF M&A ACTIVITY

India is the fastest growing major economy with a projected gross domestic product of 7.3 per cent in 2019 and 7.5 per cent in 2020. India's economy is expected to reach US$2.95 trillion by the close of 2019.

While aggregate M&A transaction volume decreased (1,640 transactions in 2018 as compared to 1,824 in 2017), the aggregate deal value in 2018 (US$129.4 billion) increased from 2017 (US$63.2 billion). The increase in value may be attributable to increased sales of stressed assets (pursuant to the corporate insolvency resolution process), consolidation across sectors and a surge in big-ticket transactions. India's continuous rise in the World Bank's Ease of Doing Business rankings is also a contributing factor.

E-commerce, fast moving consumer goods and agro-chemicals witnessed some major deals in M&A in 2018 (see Section V for details). The acquisition of 77 per cent of Flipkart (India's largest e-commerce website) by Walmart Inc for about US$16 billion is the largest-ever...
e-commerce acquisition in the world and the largest M&A transaction of 2018.\(^9\) In addition, real estate, energy and manufacturing, collectively, witnessed significant activity.\(^{10}\)

## II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The principal statutes governing M&A are the Indian Contract Act 1872 (Contract Act), the Companies Act 2013 (Companies Act), the Competition Act 2002 (Competition Act), the Foreign Exchange Management Act 1999 (FEMA), the Insolvency and Bankruptcy Code 2016 (Insolvency Code) and subsidiary legislation.

Listed entities must additionally comply with, inter alia, the Securities and Exchange Board of India (SEBI) (Substantial Acquisition of Shares and Takeovers) Regulations 2011 (Takeover Code), the SEBI (Prohibition of Insider Trading) Regulations 2015 (Insider Trading Regulations) and the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 (LODR Regulations).

### i The Contract Act

The Contract Act sets the paradigm for definitive agreements. Importantly, non-compete stipulations are relatively limited, and damages will not be awarded in excess of the loss suffered. Concomitantly, liquidated damages are, effectively, a cap on damages that may be awarded depending on the extent of loss proved. Punitive damages are not awarded.

### ii The Companies Act

The Companies Act addresses company law including mergers and restructuring, while the Insolvency Code applies to insolvency resolution and liquidation.

Public companies are subject to more onerous compliance requirements than private limited companies.

The Companies Act was amended in 2018 primarily with a view to creating greater transparency in corporate structures while also increasing the ease of doing business in India. The key amendments include the introduction of provisions to determine significant beneficial ownership and, therefore, significant influence or control over an Indian company; simplification and liberalisation of the private placement process; and easing of the restrictions on providing loans to group companies.

**Authority and capacity**

The board of an Indian company must approve any acquisition or divestment of shares. If the aggregate of the consideration (including for business or asset transfers) and the amount of guarantees or securities extended by the company (to a company other than any of its wholly owned subsidiaries), or proposed to be extended, exceeds the greater of 60 per cent

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of the acquirer company’s paid-up capital, free reserves and securities premium account, or 100 per cent of its free reserves and securities premium account, then at least 75 per cent of the shareholders must also approve.

**Pre-emptive rights, restrictions on transfers, puts and calls**

The Companies Act mandates free transferability of shares of a public company but recognises private arrangements between its shareholders as valid contracts. Implicitly, pre-emptive rights and restrictions on transfers are enforceable *inter se* shareholders.

**Types of companies**

Public, private, sole trader and small companies are permitted. The latter two are geared towards promoting domestic entrepreneurship.

**Schemes of merger and demerger**

The Companies Act permits schemes of compromise or arrangement between a company and all or a class of its creditors or members. Schemes can effect a restructuring, merger, demerger, hive-off or other reorganisation.

Every scheme must be approved by the board of each company concerned, at least 75 per cent of the shareholders of each company and at least 75 per cent of the creditors, and subsequently sanctioned by the relevant National Company Law Tribunal (NCLT).11

Schemes involving listed companies require SEBI and stock exchange prior approval at two stages: one month before the application to the NCLT for sanction and after NCLT sanction.

Schemes involving foreign companies require approval from the Reserve Bank of India (RBI) before filing with the NCLT. The transferee company must ensure that the valuation in respect of such schemes is conducted by recognised professional valuers in accordance with the internationally accepted principles on accounting and valuation.

**Resident directors and independent directors**

Under the Companies Act, every Indian company must have at least one director who was resident in India for at least 182 days during the financial year; this period is proportionately adjusted for newly incorporated companies at the end of the financial year of incorporation.

Every public company, whether listed or unlisted, must additionally have at least two independent directors if its paid-up capital exceeds 100 million rupees, its turnover exceeds 1 billion rupees or its debt exceeds 500 million rupees.

**Related-party transactions**

The Companies Act defines a related party as including holding, subsidiary and associate companies12 (including foreign companies) and entities in which directors are interested. All contracts with related parties that are not at arm’s length must be approved by the board in meeting and, where the consideration exceeds specified thresholds, by a shareholders’ resolution.

11 Approval of the NCLT is not required for a merger of two or more small companies and a merger of a holding company and its wholly owned subsidiary.

12 Investing entities will be considered associate companies.
iii  The Competition Act

*Regulation of combinations*

The Competition Act prohibits persons or enterprises from entering into a combination that has or is likely to have an appreciably adverse effect on competition within the relevant market in India.

Separately, the Competition Commission of India (Competition Commission) must approve a combination if the assets or turnover of the entities proposing to combine exceed prescribed thresholds. In the case of a business or asset transfer, an exemption from approval of the Competition Commission is available if the value of the relevant assets being transferred or the turnover attributable thereto is within the thresholds.

The Competition Commission publishes a summary of every notice of a combination received for stakeholders to review and submit their comments. It approves a combination based on, inter alia, the actual and potential levels of competition in the market, barriers to entry, market share, perceived benefits and the perceived adverse impact of the combination.

*Mergers or amalgamations*

The thresholds above which notice of a merger must be filed are as follows:

<table>
<thead>
<tr>
<th>Enterprises considered for valuation</th>
<th>Thresholds in India</th>
<th>Aggregate global threshold</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enterprise remaining after the merger or created as a result of the amalgamation</td>
<td>Asset value: more than 20 billion rupees</td>
<td>Asset value: more than US$1 billion, including at least 10 billion rupees in India</td>
</tr>
<tr>
<td></td>
<td>Turnover: more than 60 billion rupees</td>
<td>Turnover: more than US$3 billion, including at least 30 billion rupees in India</td>
</tr>
<tr>
<td>The group* to which the enterprise remaining after the merger or created as a result of the amalgamation will belong</td>
<td>Asset value: more than 80 billion rupees</td>
<td>Asset value: US$4 billion, including at least 10 billion rupees in India</td>
</tr>
<tr>
<td></td>
<td>Turnover: more than 240 billion rupees</td>
<td>Turnover: more than US$12 billion, including at least 30 billion rupees in India</td>
</tr>
</tbody>
</table>

* A group means two or more enterprises that are directly or indirectly in a position to exercise at least 50 per cent of the voting rights in another enterprise to appoint 50 per cent or more members on the board of directors, or control the management or affairs of the other enterprise

*Acquisitions*

The thresholds above which notice of an acquisition of shares or a business must be filed are as follows:

<table>
<thead>
<tr>
<th>Enterprises considered for valuation</th>
<th>Threshold in India</th>
<th>Aggregate global threshold</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target aggregated with acquirer</td>
<td>Asset value: more than 20 billion rupees</td>
<td>Asset value: more than US$1 billion, including at least 10 billion rupees in India</td>
</tr>
<tr>
<td></td>
<td>Turnover: more than 60 billion rupees</td>
<td>Turnover: more than US$3 billion, including at least 30 billion rupees in India</td>
</tr>
<tr>
<td>Target aggregated with the group to which it will belong</td>
<td>Asset value: more than 80 billion rupees</td>
<td>Asset value: US$4 billion, including at least 10 billion rupees in India</td>
</tr>
<tr>
<td></td>
<td>Turnover: more than 240 billion rupees</td>
<td>Turnover: more than US$12 billion, including at least 30 billion rupees in India</td>
</tr>
</tbody>
</table>
An acquirer that already, directly or indirectly, controls another enterprise engaged in a business similar or identical to the target must notify the Competition Commission if the following thresholds are exceeded:

<table>
<thead>
<tr>
<th>Enterprises considered for valuation</th>
<th>Threshold in India</th>
<th>Aggregate global threshold</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target aggregated with the enterprise controlled by the acquirer and engaged in a similar or identical business as the target</td>
<td>Asset value: more than 20 billion rupees</td>
<td>Asset value: more than US$1 billion, including at least 10 billion rupees in India</td>
</tr>
<tr>
<td></td>
<td>Turnover: more than 60 billion rupees</td>
<td>Turnover: more than US$3 billion, including at least 30 billion rupees in India</td>
</tr>
<tr>
<td>Target aggregated with the group to which it will belong</td>
<td>Asset value: more than 80 billion rupees</td>
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<tr>
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</tr>
</tbody>
</table>

**Combinations exempt from regulation**

The following combinations are, inter alia, exempt from the requirement of notifying the Competition Commission:

- **a** acquiring, solely as an investment or in the ordinary course of business, less than 25 per cent of shares or voting rights and not control. Acquiring less than 10 per cent of the total shares or voting rights of an enterprise will be solely an investment if the acquirer is not a member of the board, has no right to nominate any director on the board, has only such rights as are exercisable by an ordinary shareholder, and does not intend to participate in the affairs and management of the target;
- **b** acquiring additional shares or voting rights when the acquirer already holds between 25 and 50 per cent of the shares or voting rights;
- **c** any acquisition in which the acquirer already holds 50 per cent or more shares or voting rights;
- **d** acquisitions of assets by an acquirer’s business or acquired solely as an investment or in the ordinary course of business, except where the acquisition represents substantial business operations, or the acquisition leads to acquisition of control;
- **e** an acquisition pursuant to a bonus issue or capital restructuring or buyback of shares or subscription to rights issue not leading to acquisition of control;
- **f** merger or amalgamation of two enterprises where one has more than 50 per cent of the shares or voting rights of the other, where 50 per cent of the shares or voting rights in each enterprise is held by enterprises within the same group, or both;
- **g** until March 2022, an acquisition or amalgamation in which the value of the assets being acquired, taken control of, merged or amalgamated is less than 3.5 billion rupees or turnover attributable to the assets is less than 10 billion rupees;\(^\text{13}\)
- **h** until August 2022, any amalgamation of regional rural banks mandated by the central government;
- **i** until August 2027, any amalgamation, reconstitution or transfer of the whole or any part thereof of nationalised banks in accordance with special statutes in this regard; and

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\(^{13}\) This exemption was previously available only in the case of an acquisition, and the value of the assets and turnover of the enterprise as a whole were to be taken into account instead of the value of the assets and turnover being acquired.
j until November 2022, any combination involving central public sector enterprises operating in the oil and gas sectors under the Petroleum Act 1934 or under the Oilfields (Regulation and Development) Act 1948.

The exemptions in points b, c and f are not available if the transaction results in a change in control.

iv Exchange control regulations

The Indian rupee is not freely convertible, and the FEMA and its subsidiary rules and regulations restrict transactions between Indian residents and other persons.

Foreign direct investment (FDI), both primary subscription and secondary acquisition, is permitted in most sectors without prior approval and subject to compliance with conditions separate from licensing or domestic compliance of general application, including those relating to sectoral caps and pricing. All FDI must be reported through the government’s online FIRMS portal. Investment by a non-resident in less than 10 per cent of the capital of a listed entity will be considered foreign portfolio investment.

FDI is subject to pricing guidelines. These guidelines require the purchase price of shares to be at least the fair value (in the case of an Indian selling shares) or not more than the fair value (in the case of an Indian acquiring shares) determined by any internationally accepted pricing methodology. The valuation must be contemporaneous with the transaction.

Foreign investors may pay the entire consideration for an acquisition or subscription up front or defer, including through escrow, up to 25 per cent of the total consideration for up to 18 months. Similarly, indemnity obligations to a foreign investor of up to 25 per cent of the consideration are permissible without prior government approval.

v The Insolvency Code

The Insolvency Code contemplates a time-bound resolution of insolvency. The NCLT shall within 14 days of an application being submitted either admit or reject the application. The process under the Insolvency Code, once admitted, is required to be completed within 180 days of the date of admission. A further extension of 90 days may be granted by the NCLT if 66 per cent or more of the committee of creditors approves the extension. No further extension is permitted thereafter. If no resolution plan is approved at the expiry of the 180 or 270-day period, as applicable, the NCLT shall pass an order for liquidation.

Applications, once accepted, may be withdrawn if 90 per cent of the committee of creditors approve the withdrawal.

Currently, certain lacunae exist as, among other things, stakeholders have identified certain limitations under the Insolvency Code that hinder the effective resolution of insolvent companies.

14 A central public sector enterprise consists of companies in which the shareholding of the central government exceeds 51 per cent.
15 Illustratively, foreign direct investment in defence is permitted only up to 49 per cent without the prior approval of the government.
16 Aggregate foreign portfolio investment in a company is restricted to 49 per cent or less.
17 Illustratively, certain stakeholders are of the view that where a company undergoing insolvency has inadequate funds to remain afloat, the financial creditors of that company should bear the cost of the insolvency proceedings.
vi  The Takeover Code

The Takeover Code is a comprehensive code that applies to a change of control of listed companies (other than companies listed without making a public issue on the institutional trading platform)\(^\text{18}\) of a recognised stock exchange. Control includes the right to appoint a majority of the directors, or control the management or policy decisions of a company, and applies to the acquisition of shares or voting rights.

**Public offers**

*Mandatory offers and creeping acquisition*

The Takeover Code mandates a public offer on acquiring 25 per cent or more of the voting rights of a listed company and, if a shareholder already holds shares or voting rights to that extent, on acquiring more than 5 per cent of the voting rights of that company in any 12-month period ending on 31 March.

A public offer must be for at least 26 per cent of the total shares of the target company (excluding shares held by the acquirer), subject to maintaining the mandatory minimum public float of 25 per cent.

**Voluntary offers**

A shareholder with 25 per cent of the shares or voting rights of a listed company may make a voluntary public offer to acquire at least 10 per cent of the voting rights of that company, provided that the mandatory minimum public float of 25 per cent remains unaffected.

**Conditional offers**

A public offer may be conditional on a minimum level of acceptance and on regulatory approvals.

**Consideration and performance surety**

An acquirer may offer cash, shares of another listed company, listed debt securities, or any combination of these as consideration for the shares tendered in response to a public offer.

The formula to calculate the minimum offer price is geared to the historical performance of the shares of the listed company. However, if the negotiated acquisition price is higher than the historical trading price, the negotiated price must be the minimum price of the public offer.

Every person making a public offer must deposit monies in an escrow account as performance surety. Indian banks may provide guarantees as surety for non-residents if such guarantees are covered by counter guarantees of a bank of international repute.

**Disclosures of shareholding**

Every person acquiring 5 per cent or more of the shares or voting rights of a listed company must disclose aggregate shareholding and voting rights to the concerned stock exchange within two working days of the acquisition.

\(^{18}\) An institutional trading platform is a trading platform in a small or medium-sized enterprise (SME) exchange for listing and trading of securities of SMEs, including start-ups.
Every person holding 5 per cent or more of the shares or voting rights of a listed company must disclose every subsequent acquisition or divestment of 2 per cent or more of the total shareholding in a company even if such subsequent acquisition or divestment results in the shareholding falling below 5 per cent.

Separate annual disclosures must be made on 31 March each year.

**Delisting of target company**

A company may be delisted in compliance with the delisting regulations.

The promoters or an acquirer making an open offer under the Takeover Code may offer to purchase shares held by the public, and delisting may be permitted if, following the offer, the promoters hold 90 per cent of the company and at least 25 per cent of the public shareholders have participated in the offer. The acquirer or promoter may make a counter offer if the price determined is not acceptable provided that the counter offer is not less than the book value of the company.

**Schemes of amalgamation**

The open offer process is not triggered if the shares of a listed company are bought through an NCLT-approved scheme of amalgamation.

**Non-compete payments**

The Takeover Code provides for any non-compete fees paid to be included in the transaction value, while in a scheme of amalgamation, the same may be paid outside the deal value.

**vii Insider Trading Regulations**

The Insider Trading Regulations oblige shareholders, promoters, employees and directors of listed companies to disclose any transaction or series of transactions involving shares of a listed company having a trading value of 1 million rupees or more.

Insiders may also formulate irrevocable trading plans that are to be publicly disclosed and mandatorily implemented.

**viii LODR Regulations**

The LODR Regulations apply to listed entities that have listed specified securities on an Indian stock exchange, and mandate event-specific disclosure and separately, periodic disclosure of, inter alia, changes in shareholding, proposals to change capital structure, information that may have a bearing on the operation or performance of the company, M&A activity, as well as transactions with group companies.

The LODR Regulations prevent directors and key management personnel of a listed entity from entering into compensation or profit sharing agreements with shareholders or third parties in connection with shares of the listed entity without the prior approval of the board and the public shareholders. This proscription was specifically included to regulate arrangements between private equity investors and management of listed entities.

Certain mergers, demergers and schemes of arrangement involving a listed company require approval of the majority of the public shareholders of the listed company.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i The Companies Act
The provisions of the Companies Act relating to M&A have recently been notified, changing the M&A landscape significantly.

Merger into a foreign company
Previously, the Companies Act did not permit the merger of an Indian company with a foreign company, and only permitted the merger of a foreign company with an Indian company. However, the Companies Act now permits cross-border mergers with foreign companies in certain jurisdictions, subject to RBI approval.

The RBI has promulgated regulations for cross-border mergers that primarily combine compliances under various regulations and statutes (e.g., pricing guidelines and sectoral caps as discussed above).

Creditors’ objections
The Companies Act provides that a scheme of arrangement can be challenged only by shareholders holding at least 10 per cent of the shareholding by value or by creditors representing 5 per cent of the outstanding debt of the company. This should shorten timelines and preclude frivolous objections.

Ease of Doing Business Index
India’s ranking improved significantly, from 100 in 2017 to 77 in 2018.19 This improvement can be attributed to the government’s continued efforts in this regard, including the migration of several regulatory functions to e-portals, improving the country’s position in the enforcing contracts indicator, and the simplification of procedures for tax, labour and corporate regulatory compliance.

ii FDI policy and foreign investment
FDI of up to 100 per cent is allowed in single brand product retail trading under the automatic route for products branded during manufacturing with the same brand as is used globally. This initiative aims to attract a larger number of foreign investors engaged in production and marketing. However, given that local sourcing requirements remain for FDI over 100 per cent, it remains to be seen whether the liberalisation will lead to further FDI.

Further, foreign investment in a company engaged in the business of investing and registered with the RBI as a non-banking financial company (NBFC) would fall under the 100 per cent automatic route. However, foreign investment in core and other investment companies is permitted only under the government route.

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iii  Startup India

The Startup India initiative promotes entrepreneurship and innovation by helping start-ups secure funding. A start-up is a new entity that is headquartered in India, is less than 10 years old and has an annual turnover of less than 1 billion rupees. Because of the muted success of this initiative, the government made several changes, the most notable being tax benefits to start-ups, as discussed later in this chapter. Certain additional benefits have also been introduced, such as self-certification, funding corpus of 100 billion rupees and concessions on patent and trademark filings. The impact of these changes remains to be seen.

iv  Stressed assets

In the past, the RBI has prescribed various routes to be followed by financial institutions for restructuring debt of defaulting borrowers. In February 2018, the RBI notified a new framework mandating that insolvency proceedings be commenced against corporate borrowers where a debt resolution plan was not effected within 180 days. However, in April 2019, the Supreme Court struck down the RBI’s new framework as ultra vires. While the RBI is likely to notify new guidelines for debt restructuring, for the present, financial institutions have greater flexibility for the restructuring of debt and disposal of stressed assets, as the somewhat unreasonable 180-day time frame is no longer applicable.

IV  FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Foreign investors continue to be key players in Indian M&A with inbound investment increasing by 17 per cent.20

Below is a country-wide summary (top 10 only) of foreign involvement in Indian M&A (in terms of US$).21

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<thead>
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<tbody>
<tr>
<td>1</td>
<td>Mauritius</td>
<td>15,728</td>
<td>15,941</td>
<td>132,408</td>
<td>32</td>
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<tr>
<td>2</td>
<td>Singapore</td>
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<td>12,180</td>
<td>79,747</td>
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<td>3</td>
<td>Japan</td>
<td>4,709</td>
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<tr>
<td>4</td>
<td>United Kingdom</td>
<td>1,483</td>
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<tr>
<td>5</td>
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<td>6</td>
<td>United States</td>
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<tr>
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<tr>
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<td>United Arab Emirates</td>
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<td>6,054</td>
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Total FDI inflows from all countries: 43,478

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<td>6,054</td>
<td>1</td>
</tr>
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</table>

Total FDI inflows from all countries: 43,478


V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Significant transactions

Flipkart/Walmart
One of the biggest deals of 2018 was Walmart’s US$16 billion acquisition of 77 per cent of Indian e-commerce company, Flipkart, making it the largest acquisition in the Indian e-commerce sector to date.

HUL/GSK CH
Hindustan Unilever Limited, one of the largest fast moving consumer goods companies in the country, is set to merge with GlaxoSmithKline Consumer Healthcare Limited to further strengthen its position in the food business and branch into the health and wellness business. With a reported transaction value of US$4.5 billion, the merger is awaiting regulatory approvals.

Larsen & Toubro/Mindtree
Larsen & Toubro (L&T) is in the process of a hostile takeover of Mindtree, an IT consulting company. L&T triggered a mandatory open offer by agreeing to acquire shares from the promoter of Mindtree and placing an order to acquire shares from the secondary market. While the value of the deal was only 80 billion rupees, the transaction is significant as hostile takeovers are rare in the Indian context.

UPL/Arysta
The acquisition of Florida-based Arysta Life Science Inc, by Indian company UPL (formerly United Phosphorus Limited) for US$4.2 billion was the largest overseas deal in 2018. Currently at number nine, after the merger, UPL will be the world’s fifth-largest crop protection company.

ii Hot industries

The manufacturing sector was the focus of significant activity, with Tata Steel acquiring Bhushan Steel for US$5.5 billion under a corporate insolvency resolution process, Hindalco Industries acquiring Aleris Corporation for US$2.6 billion and Schneider Electric SA acquiring the electric and automation business of L&T for US$2.1 billion.

iii Key trends

Indian industry is experiencing a digital revolution with each sector capitalising on technology. The growth in the technology sector can be primarily attributed to increased internet penetration and government initiatives facilitating the same.

The real estate sector witnessed healthy activity; some notable deals include the acquisition of controlling interests in Essar Group’s Equinox Business Park by Brookfield Asset Management Inc for US$360 million and Indiabulls Properties and Indiabulls Real Estate Company by the Blackstone Group Lp for US$742 million.22

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VI  Financing of M&A: Main Sources and Developments

i  Indian banks

Indian banks are precluded from funding M&A other than providing guarantees as surety for offshore acquirers if such guarantees are covered by counter-guarantees of a bank of international repute.

ii  NBFCs

NBFCs provide acquisition finance but are subject to exposure norms that apply to business sectors, a single borrower and affiliated companies. Therefore, the available finance is limited and expensive.

While a foreign investor may encumber shares of the relevant Indian company to secure credit facilities raised outside India, prior RBI approval is required if the proceeds of the credit facilities are to be used for further acquisitions, and the required approval is not forthcoming.

iii  Leveraged buyouts

Leveraged buyouts (LBOs) are limited in Indian M&A as the Companies Act prohibits a public company from providing financial assistance to any person for the purposes of acquiring the shares of that public company. While this structure does not apply to private companies, LBOs are rare, although slowly gaining ground.

iv  Structured investments and structured payouts

Given the difficulties in raising finance from more traditional sources, structured equity and quasi-equity investments are the preferred routes to raise acquisition finance. Consideration may be paid over time on the basis of earn-outs or other specific deliverables being achieved, but as Indian law requires delivery of shares of a public company against payment, transactions must be carefully structured.

VII  Employment Law

Contracts of employment cannot be specifically enforced under Indian law. Therefore, if an employer company undergoes a change in control, there is a de facto requirement to obtain employee consent.

Employees’ consent must be handled sensitively, but as long as the terms and conditions of their employment are not adversely affected by a transaction, they are likely to give their consent. In larger industrial establishments, the prior consent of the relevant state government may be required, and this, too, is generally forthcoming.

As contracts of employment are not enforceable by specific performance under Indian law, key personnel may be offered a retention bonus or other incentive as appropriate.
VIII VIRTUAL CURRENCIES

The RBI prohibits all entities regulated by it (i.e., banks, NBFCs and payment system providers) from dealing with virtual currencies, or providing services to facilitate any person or entity dealing with virtual currencies. The RBI’s proscriptions are currently being challenged before the Supreme Court.

IX TAX LAW

M&A in India are subject to income tax, stamp duty and, in the case of asset sales (including certain business transfers), goods and services tax (GST). However, a business transfer structured as a transfer of an undertaking as a going concern with no specific consideration allotted to each transferred assets (a slump sale) is exempt from GST.

Indian law subjects any gains accruing on the transfer of a capital asset to tax. Capital gains arising from both share transfers (of unlisted shares) and asset transfers are taxed as long-term capital gains if the shares or assets are held for more than 24 months prior to completion of the transaction. In the case of a transfer of listed shares, short-term capital gains tax arises if the shares were held for less than 12 months; if held for more than 12 months, long-term capital gains tax arises. A transfer of listed shares on the market, whether long-term or short-term, is subject to securities transaction tax. From 1 April 2019, capital gains arising from a sale of listed equity shares, units of equity-oriented funds or units of business trusts will be subject to long-term capital gains tax if the shares have been held for more than 12 months and the gain exceeds 100,000 rupees.

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>Short-term capital gains</th>
<th>Long-term capital gains</th>
<th>Obligation to deduct tax at source</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Resident assessee (%)</td>
<td>Non-resident assessee (%)</td>
<td>Resident assessee (%)</td>
</tr>
<tr>
<td>Unlisted equity shares</td>
<td>Gain on transfer</td>
<td>30</td>
<td>40 or 30</td>
</tr>
<tr>
<td>Listed equity shares on market</td>
<td>Gain on transfer</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>Listed equity shares off market</td>
<td>Gain on transfer</td>
<td>30</td>
<td>40 or 30</td>
</tr>
<tr>
<td>Asset transfer</td>
<td>Gain (i.e., difference between sale consideration minus cost of acquisition or indexed cost of acquisition)</td>
<td>30</td>
<td>40 or 30</td>
</tr>
</tbody>
</table>

23 Including maintaining accounts, registering, trading, settling, clearing, giving loans against virtual tokens, accepting them as collateral, opening accounts of exchanges dealing with them and the transfer and receipt of money in accounts relating to purchase or sale of virtual currencies.
The rates in the above table may be subject to a surcharge at the following rates:

### Individuals

<table>
<thead>
<tr>
<th>Total income</th>
<th>Surcharge (%)</th>
<th>Health and education cess (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 to 10 million rupees</td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>Above 10 million rupees</td>
<td>15</td>
<td>4</td>
</tr>
</tbody>
</table>

### Companies

<table>
<thead>
<tr>
<th>Total income</th>
<th>Surcharge (%)</th>
<th>Health and education cess (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic company</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Zero to 10 million rupees</td>
<td>Nil</td>
<td>4</td>
</tr>
<tr>
<td>10 to 100 million rupees</td>
<td>7</td>
<td>4</td>
</tr>
<tr>
<td>Above 100 million rupees</td>
<td>12</td>
<td>4</td>
</tr>
<tr>
<td>Foreign company</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Zero to 10 million rupees</td>
<td>Nil</td>
<td>4 per cent</td>
</tr>
<tr>
<td>10 to 100 million rupees</td>
<td>2 per cent</td>
<td>4 per cent</td>
</tr>
<tr>
<td>Above 100 million rupees</td>
<td>5 per cent</td>
<td>4 per cent</td>
</tr>
</tbody>
</table>

### Tax efficiencies

For foreign investors, immediate tax efficiency is achieved if the applicable double taxation avoidance agreement permits a lower rate of taxation.

A slump sale is more tax efficient than an asset transfer simpliciter, as it allows for business losses to be carried forward and, as long as the undertaking has been held for more than three years prior to completion of the transaction, gains are subject to long-term capital gains tax notwithstanding that individual assets may have been more recently acquired. 'Slump exchange' structures are gaining popularity on account of their tax efficiency.

An NCLT-sanctioned scheme is also tax efficient if, inter alia, shareholders holding at least 75 per cent in value of the original entity become shareholders in the resulting entity.
The general anti-avoidance rules (GAAR) may also prove to be problematic. GAAR enables the tax authorities to declare an arrangement as an impermissible avoidance arrangement if they are of the view that the arrangement has been entered into with the primary intention of avoiding tax. The law provides that there is a presumption of an arrangement being an impermissible avoidance arrangement, and it is for the taxpayer to demonstrate that it has commercial substance.

ii Developments

After years of uncertainty, attempts are being made to make the tax regime in India more transparent and investor-friendly. While intention is articulated frequently, progress on the ground is, arguably, slow.

Reduced rate of corporate tax

From 1 April 2018, income tax rates of Indian companies having a total turnover or gross receipts of less than 2.5 billion rupees have been reduced from 30 to 25 per cent of the total income.

Tax benefits for start-ups

For start-ups incorporated between April 2016 and March 2021, a 100 per cent deduction of profits is proposed for three out of seven years. Further, start-ups and investors may seek exemption from tax payable out of income from other sources in respect of the issuance of shares at more than fair market value, subject to the fulfilment of the required thresholds.

IX OUTLOOK

India continues to rely on FDI as a significant driver of economic development, and the legislative support for easing business processes should facilitate further investments. Additionally, the resolution and acquisition of stressed assets under the Insolvency Code framework is likely to drive a substantial portion of Indian M&A in 2019 despite protracted timelines for the approval of resolution plans.

While India does seem to be on the cusp of an economic slowdown, the re-elected Modi government, which took office on 31 May 2019, has announced policy measures to stimulate economic growth and M&A activity in India.
Chapter 25

INDONESIA

Yozua Makes

I GENERAL OVERVIEW

Investors and the general business community have been keeping an eye on Indonesia’s political situation in 2019, and may wait to see the results of the political changes prior to making key business decisions, as the outcome of any legislative changes and the presidential election will have a big impact on the investment and business climate of Indonesia. 2018 saw a moderate economic slowdown, a trend that is likely to continue in 2019.

The Indonesian Investment Coordinating Board (BKPM) reported a total investment (including greenfield investments and acquisitions) of 721.3 trillion rupiahs in 2018, which is an increase of 4.1 per cent compared to 2017 but below the national investment target of 765 trillion rupiahs. The top five key target industries are:

1. electricity, gas and water supply;
2. transportation, warehousing and telecommunication;
3. mining;
4. food; and
5. housing, industrial estates and office buildings.

Indonesia is further solidifying its Asian roots: the FDI invested into Indonesia based on country of origin has all derived from Asian countries: Singapore, Japan, China, Hong Kong and Malaysia.

A report by the Indonesian Competition Supervisory Authority (KPPU) estimates that the amount arising from M&A deals in 2018 was about 150 trillion rupiahs. Some of those transactions were reported to KPPU, although a large number were not. KPPU accepted 74 reports in 2018, lower than the 90 that it accepted in 2017. Of the filings, 97 per cent concerned acquisition deals.

Since taking over the presidential office, President Joko Widodo has been initiating various regulatory reform measures packaged under a series of deregulation policies (or economic deregulation packages (EDPs)) aimed at tackling regulatory complexities and bureaucratic hurdles. The first EDP was launched in September 2015, and since then there have been revisions to support the objectives of EDP reforms.

More recently, the government enacted Regulation No. 24 of 2018 (GR 24/2018), which introduces the online single submission (OSS) system as the main reference for business licensing and the gateway for government services at various ministerial, agency and regional government levels. This was followed by a new Head of BKPM Regulation No.

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1 Yozua Makes is the managing partner at Makes & Partners Law Firm.
6 of 2018 on the Implementation of Capital Investment Licensing and Facilities. Similar to its predecessor of 2017, the Regulation recognises the possibility of simplified licensing for the services sector by allowing certain companies to apply directly for full licences, and by simplifying the process for merger approval from a two-stage to a one-stage process.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

In general terms, the statutory framework for the combination of businesses through a limited liability company is set out in Law No. 40 of 2007 on the Limited Liability Company the Company Law and various implementing regulations such as the Government Regulation No. 27 of 1998 on Mergers, Consolidation and Acquisition of Limited Liability Companies.

In addition to the aforementioned umbrella laws and regulations, the practice and procedure for implementing particular transactions must comply with other specific laws and regulations relating to the status or nature of the business of the target company, and is also regulated by specific bodies. For instance, banks, financial institutions and publicly listed companies are regulated by the Financial Service Authority (OJK). OJK is a body established by virtue of the Financial Authority Law merging the authority previously held by the Capital Market and Financial Institution Supervisory Board or Bapepam-LK (Bapepam) and the bank oversight authority of the central bank, Bank Indonesia to supervise all activities in the financial services industries under one agency, with the exception of payment services that are still under Bank Indonesia. Further, companies with foreign share ownership are regulated by the Capital Investment Coordinating Board (BKPM), and for tax purposes, all companies are subject to the relevant M&A regulations of the Directorate General of Tax and OJK, which also regulate share custodian services and securities broker-dealers. In addition, for M&A in the insurance sector, companies are required to comply with the Insurance Law and its implementing regulations; for M&A in the broadcasting sector, companies are required to comply with the Broadcasting Law and its implementing regulations; and for M&A in the telecommunication sector, companies are required to comply with the Telecommunication Law and its implementing regulations, and other sector-specific regulations to govern the respective M&A in such industry.

In general, the requirements pertaining to M&A in Indonesia are as follows:

a the announcement of an M&A proposal prepared by the acquirer and the target company or the merging companies, as the case may be, in newspapers;

b an extraordinary general meeting of shareholders of the target company or each of the merging companies (as the case may be) in which a quorum of at least 75 per cent of the total number of shares with voting rights are present (unless otherwise stipulated in a specific regulation), and in which approval is obtained from shareholders holding at least 75 per cent of the number of votes cast;

c the approval of creditors in respect of the proposed M&A transaction and a waiver of their rights for claims to be settled prior to the effectiveness of the merger or acquisition;

d a valuation of shares to determine the fair market value of the merger shares conversion formula;

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2 Law No. 40 of 2007 on the Limited Liability Company.
the approval of third parties, including but not limited to the approval of third parties required by prevailing law as well as pursuant to agreements entered into by the companies involved;

the approval of the relevant agencies having jurisdiction over the merging or acquired company or companies (e.g., OJK and the Minister of Law and Human Rights); and

the consent of any relevant industry regulator, depending on the nature of the target company’s business.

An M&A transaction involves different companies, which can potentially result in a conflict of interest among directors, commissioners, majority shareholders and affiliates. Thus, with regard to the acquisition of a public company, to provide legal certainty and protection to shareholders – particularly independent shareholders who have no conflicts of interest in particular transactions – OJK under Bapepam Rule No. IX.E.1 requires a publicly listed company conducting an M&A transaction to appoint an institution registered at OJK to appraise the transaction. In the event that OJK finds a conflict of interest, the transaction will require approval by the independent shareholders through a vote at a general meeting of shareholders. Another related regulation is Bapepam Rule No. IX.E.2, last revised on 28 November 2011. Rule IX.E.2 provides that the disclosure of material transactions with a value of between 20 and 50 per cent of a public company’s equity must be published within two business days of signing the transaction documents; if the value exceeds 50 per cent, the approval of the general meeting of shareholders is also necessary. The Rule also requires the results of material business transactions and changes in core business to be reported to Bapepam within two working days of completion.

In the banking sector, banks are subject to Government Regulation No. 28 of 1999 regarding Merger, Consolidation and Acquisition of Banks. Indonesia has acknowledged the single-ownership principle of the Indonesian banking industry known as the Single Presence Policy pursuant to OJK Regulation No. 39/POJK.03/2017 on Single Presence Policy. Pursuant to this policy, albeit only certain requirements and exceptions, a controlling shareholder of an Indonesian bank is allowed to be the controlling shareholder of only one bank. Another important regulation of bank ownership is OJK Regulation No. 56/POJK.03/2016 on Share Ownership of Commercial Bank. The rule sets out the maximum share ownership in Indonesian banks – around 20 to 40 per cent – differentiated based on the specific nature of the shareholders (whether a shareholder is also a bank, financial institution or an individual). The rule allows ownership that exceeds such limit, subject to OJK approval. Further, there is a specific requirement for prospective foreign investors to commit to the country’s economic growth, obtain the approval of the authority of the respective country of origin and be subject to certain ratings set out by Bank Indonesia.

Recently there have been regulatory discussions in OJK about issuing a new regulation on holding companies for financial conglomeration activities that requires companies operating across different financial sectors to form a holding company that is also subject to OJK supervision. Financial industry stakeholders are currently waiting for the introduction of this new regulation.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAWS AND THEIR IMPACT

In general, developments in corporate and takeover laws aim to make the process more transparent, taking into consideration concerns of different stakeholders such as creditors, employees, minority shareholders and consumers, and within the framework of environmental protection and fair competition.

The government is concerned about maintaining fair competition among business players in Indonesia. Consequently, regulations governing fair trade practices are frequently issued or amended. In connection therewith, KPPU recently issued implementing regulations to the Antimonopoly Law, namely KPPU Rule No. 10 of 2010, Rule No. 11 of 2010, and Rule No. 13 of 2010 and its amendments, which govern the consultation and post-notification requirements for mergers, consolidations and acquisitions, along with guidelines that, inter alia, provide for the scrutiny of contemplated M&A transactions. These rules were issued as the implementing regulations of Government Regulation No. 57 of 2010 on the Merger or Consolidation and Acquisition of Enterprise Share which may Result in Monopolistic Practices and Unfair Business Competition (GR 57/2010), which was recently issued by the government (see Section IX).

With respect to acquisitions of public companies (also known as takeovers), OJK has issued OJK Regulation No. 9/POJK.04/2018 regarding Takeover of a Public Company. This regulation introduces the concept of the mandatory tender offer (MTO), which is triggered by a takeover of a public company. The Rule requires a refloating obligation of 20 per cent of the shares obtained as a result of an MTO. However, OJK can grant an extension of the time period for a refloat of shares to the Stock Exchange in certain cases. Additionally, OJK also introduced OJK Regulation No. 54/POJK.04/2015 on Voluntary Tender Offer, which can be a tool for acquisitions for public companies with no controlling or simple-majority shareholders, amending the previous Bapepam Rule IX.F.1 of 2011.

In December 2016, OJK introduced a revision to the regulation concerning mergers and consolidations for public companies by virtue of OJK Regulation No. 74/OJK.04/2016. The regulation provides new paper requirements for OJK approval in the event of the merger or consolidation of public companies. The new requested documents include, among others, corporate shareholding and management documents, appraisal reports, business plans, notes on the new controller and management analysis reports. This regulation is aimed at further promoting investor protection and information disclosure.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Foreign direct investment in Indonesia is regulated by the Investment Law4 and its implementing regulations issued by BKPM. As the appointed regulator of direct capital investment in Indonesia, BKPM has mainly focused on the efforts of the government to attract foreign investors and build an international economic environment.

The most recent rules on foreign equity restrictions are stipulated in Presidential Regulation No. 44 of 2016, which determines what business sectors are open or closed for foreign investors, and if open, to what extent FDI is permitted (the Negative List). The Negative List is the first and most important regulation that any foreign investor

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4 Law No. 25 of 2007 on Capital Investment.
contemplating investment in Indonesia should consult. If the business of the companies in a contemplated M&A falls under the list of business fields that are closed to foreign investment as provided in the Negative List, then the foreign investor cannot invest in such business field in Indonesia. If the business falls under the list of business fields that are conditionally open for investment, however, then foreign investment in such business is permitted, but a contemplated M&A involving foreign investors will be limited regarding the level of foreign ownership of shares allowed in the Negative List. As a consequence of the involvement of foreign investors in an M&A transaction, the Indonesian company will be required to convert its status from a domestic company into a foreign investment company within the framework of the Investment Law.

The following are representative examples of the general application of current Negative List provisions regarding foreign investment, which are also subject to other specific regulations:

a. finance companies: the maximum foreign ownership is 85 per cent;
b. insurance: the maximum foreign ownership is 80 per cent; and
c. plantation: the maximum foreign ownership is 95 per cent.

Most private foreign direct capital investments in Indonesia are administered and supervised by BKPM. Consequently, most matters relevant to M&A transactions must be reported to and will require approval of the Chair of BKPM. BKPM Regulation 6/2018 sets out the procedures for obtaining BKPM approval for new investments, changes in shareholders, mergers or business expansions.

Public companies, on the other hand, are regulated by OJK. Unlike private companies, unless specifically provided under a separate regulation, publicly listed companies have no restriction on foreign ownership of shares if such investment involves foreign passive portfolio investors and not strategic or controlling foreign investors. Moreover, the provisions under the Negative List are not applicable to a public company whose shares are acquired by foreign investors in portfolio transactions made through the domestic capital market.

V SIGNIFICANT TRANSACTIONS AND HOT INDUSTRIES

For years, Indonesia has been substantially relying on the energy and mining sector, being a strong force in the oil and gas business and the world’s largest exporter of thermal coal. Ever since President Widodo took office, structure has become the top priority, as evidenced by the large number of deals focusing on electricity, gas and water supply, and telecommunication. Transportation and warehousing also made substantial contributions to both the economy and in terms of fixing Indonesia’s lagging logistical landscape. More recently, the rise of the middle class means rising consumer spending; therefore, consumer sectors such as retail, consumer technology, consumer goods, transportation (including aviation) and property (including housing, industrial estate, and office building) have become main targets.

2018 saw various major landmark deals in Indonesia, some driven by state-owned enterprise and some by the banking sector. State-owned cement producer PT Semen Indonesia Tbk (SMGR) completed a US$917 million acquisition of PT Holcim Indonesia Tbk (SMCB), a local business of LafargeHolcim. Semen Indonesia reportedly raised US$1.25 billion through a bridge loan to fund the purchase of an 80.6 per cent stake in Holcim Indonesia and another MTO for the remaining shares.
Again in 2018, PT Bank Tabungan Pensiunan Nasional Tbk (BTPN) merged with PT Bank Sumitomo Mitsui Indonesia (SMBCI), both subsidiaries of Sumitomo Mitsui Banking Corporation (SMBC). SMBC was a controlling shareholder in BTPN and SMBCI, holding 40 and 98.48 per cent, respectively. Another notable M&A deal in the banking sector took place in August 2018, when Bank of Tokyo Mitsubishi UFJ increased its investment in PT Bank Danamon Indonesia, Tbk to become a controlling shareholder with a 40 per cent interest by acquiring (directly or indirectly) an additional 20.1 per cent from Asia Financial (Indonesia) Pte Ltd (AFI) and other affiliated entities. The investment amount for the additional 20.1 per cent was reported to be valued at 17.187 trillion rupiahs.

Finally, in December 2018 two major M&A deals were closed, forging a path for Indonesia’s energy holding formation. After two years of negotiation, Indonesia’s state-owned mining holding company, PT Indonesia Asahan Aluminium (Inalum), finally raised its stake in PT Freeport Indonesia, the operator of the giant Grasberg mine in West Papua, to 51.23 per cent from its previous 9.36 per cent stake. Inalum spent US$3.85 billion purchasing the stakes. Meanwhile, Perusahaan Gas Negara Tbk (PGN) completed its US$1.35 billion acquisition of 51 per cent shares of PT Pertamina Gas (Pertagas) from PT Pertamina (Persero).

VI FINANCING OF M&A MAIN SOURCES AND DEVELOPMENTS

As in other jurisdictions, financing for M&A in Indonesia is generally derived from internal cash flows, bank loans (provided such financing is not intended for investment in speculations on shares), the issuance of new shares (share swaps) and the issuance of financial derivative instruments.

Various regulations are applicable depending on the nature of a financing scheme, including a reporting requirement to Bank Indonesia for foreign currency-denominated loans from offshore banks or entities; the submission of registration statements to OJK if a transaction involves conducting a rights issue; and approval of BKPM for an increase of equity to finance expansion (growth by acquisition instead of organic growth).

The prevailing regulations that affect the financing of M&A are as follows:

a Bank Indonesia Regulation No. 16/22/PBI/2014 regarding Reporting of Foreign Exchange Activity and Reporting of Application of Prudential Principles in relation to an Offshore Loan Management for Non-Bank Corporation, as amended by Bank Indonesia Regulation No. 21/2/PBI/2019;

b Bank Indonesia Regulation No. 18/18/PBI/2016 regarding the Purchase of Foreign Currency Against Rupiah through Banks; and

c Bank Indonesia Regulation No. 19/3/PBI/2017 regarding Short-Term Financing Facility for Commercial Banks which, inter alia, prescribes reporting and credit rating requirements in some cases.

Bank Indonesia also issued Bank Indonesia Regulation No. 7/1/PBI/2005 regarding Offshore Borrowing and Other Obligations of Banks in Foreign Currency, which was last amended by Regulation No. 21/1/PBI/1/2019, containing, among other things, obligation for banks to limit the daily balance of short-term offshore borrowing to a maximum of 30 per cent of capital.

Another key regulation on the matter is BI Regulation No. 16/21/PBI/2014 on Implementation of Prudential Principles for the Management of Foreign Loans of Non-Bank Corporations as amended by Bank Indonesia Regulation No. 18/4/PBI/2016. The Regulation
Indonesia

aims to prevent foreign loans and excessive foreign debt from hampering macroeconomic stability by providing guidelines for non-bank corporations to implement prudent principles in managing their loans with foreign parties. In managing foreign loans, companies must implement prudential principles by complying with the prescribed hedging and liquidity ratios and credit ratings. Hedging and liquidity ratios are based on foreign-currency assets (receivables) and liabilities (obligations) from forwards, swaps, or options transactions, or a combination thereof.

The mandatory use of the rupiah for a transaction’s currency is another hot regulatory topic in Indonesia. On 28 June 2011, the government issued Law No. 7 of 2011 on Currency (Mata Uang). Article 21(1) of Law No. 7/2011 provides that the Indonesian rupiah shall be used in every payment transaction, for the fulfilment of other monetary obligations or for other financial transactions within the Indonesian territory, with certain exceptions. In 2015, Bank Indonesia issued Regulation No. 17/3/PBI/2015 on the Mandatory Use of Rupiah within the Republic of Indonesia. The Regulation basically strengthens the Currency Law, and provides clearer guidance that the Law applies to both cash and non-cash transactions. The new Regulation also explains in details the five exceptions of the rule.

VII  EMPLOYMENT LAW

The Labour Law 5 provides the framework for the rights of employees and employers in the M&A context. Basically, since M&A are only related to the change in ownership or control over a company, it should not in any way affect employees’ status. In general, there are two possibilities with respect to an employee’s continuance in a company with new controlling shareholders (in an acquisition) or with a surviving company (in a merger), which could be either the extension or renewal of the employee’s term of employment. In the case of a renewal of employment, the employee will have his or her contract terminated from the previous company (before it was merged or acquired) and then be rehired by the surviving company under new terms and conditions. Accordingly, there is a requirement under the Company Law for boards of directors of companies undergoing M&A transactions to publish a summary of a proposed merger or acquisition in at least one newspaper, and to announce it in writing to the employees of the surviving or acquired company no later than 30 days before the invitation of shareholders to the general meeting of shareholders.

Should an employee not wish to maintain his or her employment with the surviving company, then he or she has the right to refuse the new employment. Thus, the employee can resign from the company and demand a special severance payment, long-service payment package and accrued compensation (such as untaken annual leave or housing allowance, if applicable) as set out in the Labour Law, Article 163(1). It should be noted that the Labour Law does not specify the percentage of ownership that triggers these entitlements, but simply refers to a change of ownership. There is a risk that the employees or their union (if any) will take the position that any change of ownership will qualify under Article 163(1), even where there is less than a 50 per cent change in shareholding. Any substantial change in management and employment policies, however, could also trigger Article 163(1), even though the new shareholder is not a controlling shareholder, as this may directly or indirectly affect the employees.

However, under Article 163(2) of the Labour Law, employers (both the buyer and the seller) also have the right to terminate an employment in the event of a change in a company’s status, a merger or a consolidation, subject to the payment of severance and long-service payment as set out in Article 163(2), which is set at a higher level than those under Article 163(1) mentioned above.

In addition to the above, the rights of employees in M&A transactions are also governed by the provisions relating to M&A transactions in a collective labour agreement entered into by and between the company and the company’s labour union. In the event of inconsistency between the provisions of the Labour Law and the collective labour agreement, the provisions that are more favourable to the employees will prevail.

VIII TAX LAW

i Corporate income tax in mergers

As in other jurisdictions, the accounting method used in mergers is generally a pooling of interest method and a book value transfer approach.

Article 1(3) of Minister of Finance Decree No. 43/PMK.03/2008 of 13 March 2008 on the Use of Book Value for Transfer of Assets in Relation to Merger, Consolidation or Spin-off (MOF Decree 43/2008) defines a business merger as a merger of two or more taxpayer entities with capital divided into shares in a manner that maintains the existence of one of the companies having no residual loss or having a smaller residual loss.

Furthermore, Article 2 of MOF Decree 43/2008 provides that taxpayers conducting a merger using book value must fulfil the following requirements: submission of an application to the Director General of Tax including the reason and purpose for conducting the merger or spin-off; payment of all tax owed by each of the companies involved; and fulfilment of requirements of the business purpose test (described below).

In addition, Article 3 of MOF Decree 43/2008 provides that a taxpayer conducting a merger using the book value approach may not compensate the loss or residual loss of the merged taxpayer.

In general, one could conclude that there will be no capital gains tax (corporate income tax) if the Directorate General of Taxation has issued an approval for a merger with book value. In the event that a transfer of assets using book value is not approved by the Directorate General of Taxation, then the transfer of assets shall be valued at the market price, and the difference between the book value and the market value (capital gains) will be subject to corporate income tax at a rate of 25 per cent (flat rate).

ii Value added tax

A transfer of assets is subject to VAT at 10 per cent of the market value, pursuant to Articles 4(1) and 7(1) of the VAT Law.6

The VAT should be imposed by a taxable business entity on the delivery of assets, the initial purpose of which is not to be traded, except assets on which the VAT cannot be credited because the acquisition of such assets has no direct relation to the business activity, and for the acquisition and maintenance of sedan or station wagon motor vehicles when made for a trading inventory or for rental purposes.

6 Law No. 42 of 2009 on Value Added Tax and Sales Tax on Luxury Goods.
iii  Tax on transfers of land

Government Regulation No. 41 of 2016 provides that the disposal of land and buildings is subject to final income tax at a rate of 2.5 per cent of the transfer amount that is stated in the deed, which is a reduction from the previous 5 per cent rate (the transferor's tax obligation). Moreover, the transfer of land or buildings in a merger is subject to land or building title acquisition duty (BPHTB) of 5 per cent of the taxable value (NJOP) (the surviving entity's tax obligation). The NPOP in the merger is the market value or the same as the NJOP.

The taxpayer who carries out the merger and obtains approval for the use of book value for the merger from the Director General of Taxation may apply for a 50 per cent reduction in the BPHTB.

iv  Sale of shares

Article 17 of Law No. 36/2008 provides that the maximum tax rate for individual taxpayers is 30 per cent and the tax rate for corporate taxpayers is a flat rate of 25 per cent. Public companies that satisfy a minimum listing requirement of 40 per cent along with other conditions are entitled to a tax discount of 5 per cent off the standard rate, giving them an effective tax rate of 20 per cent.

For transfers of shares in general, the difference between the acquisition of shares and the selling price of shares will be subject to capital gains tax at a rate of 30 per cent (maximum) if the seller is an individual and at a rate of 25 per cent (flat rate) if the seller is a corporate taxpayer in Indonesia.

If the seller of the shares is a non-Indonesian taxpayer, then the capital gains tax from the selling of the shares will be regulated based on the applicable tax treaty between the seller's country of domicile and Indonesia.

For transfers of shares of a publicly listed company, a final tax of 0.1 per cent of the transaction value will be applicable to the seller and 0.5 per cent tax on the founder shares (if the seller is holding the shares from the initial public offering).

IX  COMPETITION LAW

Certain provisions of the Antimonopoly Law deal specifically with M&A. Essentially, pursuant to Article 28 of the Antimonopoly Law, M&A transactions in Indonesia are prohibited if they result in monopolistic or unfair trade practices. Therefore, all efforts should be made to ensure that any contemplated M&A transaction does not give rise to a monopolistic or unfair practice.

The Antimonopoly Law uses a market share standard as a parameter for ascertaining the presumption of a monopoly (if a business player has more than a 50 per cent market share), for ascertaining the presumption of an oligopoly (if a group of business players has more than a 75 per cent market share) and for determining the dominant position (if a business player has more than a 50 per cent market share and, as a group, those business players have more than a 75 per cent market share unless the dominant position is not abused).

In July 2010, the government issued GR 57/2010, followed by various rules issued by KPPU. GR 57/2010 and the KPPU rules provide that companies conducting an M&A
A major and unprecedented shift of M&A deals dominated by the technology sector was seen in 2018, in contrast to 2016, during which the mining sector still dominated. Consistent political support by the government has led to new optimism regarding Indonesia’s potential growth; given its consumer market, there is massive untapped potential for M&A in Indonesia to cater to the needs of the rising middle class. Natural resources (coal, palm oil, natural gas, petroleum and mineral resources) remain an important sector, but telecommunications, retail, property, construction, technology, and financial services have proven to be the sectors that have led the market.

As a democratic country that has undergone significant reform in the past two decades, challenges still remain. Bureaucratic red tape and corruption have become the main obstacles to the country’s sustainable growth. However, several reform initiatives have been introduced to restore confidence in the country’s business climate. Investors are still waiting for the impact of new procedures introduced by Government Regulation No. 91 of 2017, and the subsequent BKPM regulation at the end of 2017 to streamline business process. Financial and securities regulations, as well as corporate governance rules, have been set up to provide a more sophisticated and modern regulatory environment for foreign investors.
In light of the foregoing, it appears that recent economic developments show market confidence that the government will continue to maintain and improve transparency, the certainty of stakeholders’ involvement, fair competition and a more foreign investment friendly environment.
Chapter 26

ITALY

Mario Santa Maria and Carlo Scaglioni

I  OVERVIEW OF M&A ACTIVITY

In 2018, the Italian M&A market saw an increase of approximately 21 per cent in the number of transactions compared to the previous year (around 1,000), amounting to around €94 billion in value. The M&A market trend was characterised by two major transactions, *Essilor/Luxottica* and *Atlantia/Abertis*, amounting to around €41 billion. Some relevant transactions were also completed in the first quarter of the 2019.2

II  GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A of unlisted joint-stock companies, limited liability companies and limited partnerships are regulated by the Italian Civil Code (Civil Code). The rules applicable to listed companies are set forth in the Civil Code and in the Italian Securities Act3 and implemented by secondary regulations adopted by the Italian Securities and Exchange Commission, the public overseeing authority of mergers and takeovers, and the Italian Stock Exchange (Borsa Italiana), the private company in charge of the management of the Italian securities market.

Listed companies may also adhere to the Code of Corporate Governance issued by Borsa Italiana, which, for the signatories, follows the comply or explain model.

Certain transactions are subject to merger control clearance, which, depending on the nature of the companies involved and the sector in which they operate, is issued by the Bank of Italy, the Italian Antitrust Authority (IAA) or the Insurance Regulation Authority.

In terms of structure, M&A transactions can come in the form of acquisitions of companies through share (and quota) deals, asset deals, leveraged buyouts, tender offers, turnarounds, equity carveouts, mergers and demergers, or combinations of these.

The main forms of transactions covered by Italian law are asset deals, share and quota deals, and mergers and demergers. The choice of one structure over the others entails different consequences in terms of legal implications and tax consequences.

1 Mario Santa Maria and Carlo Scaglioni are corporate partners at Greenberg Traurig Santa Maria Law Firm. The authors would like to acknowledge the contributions of fellow partner Edoardo Gambaro, senior associates Alessandra Boffa, Caterina Napoli and Elisabetta Nicolì and associate Pietro Missanelli.


3 Italian Securities Act (Legislative Decree No. 58/1998).
i  Asset deals

Asset deals concern the direct transfer of a business (inclusive of employees, assets, know-how, contracts, etc.). The Civil Code, as a rule, provides for the continuity of such business – agreements related to the activity are automatically transferred, except for those having personal connotations, pursuant to Article 2558 of the Civil Code, and the seller remains jointly and severally liable with the buyer for debts accrued before the transfer pursuant to Article 2560 of the Civil Code. Depending on the number of employees involved, prior notice of the transfer of a business to the union representing its employees is required (while such notice is not required in a stock deal). An advantage of asset deals lies in the possibility to choose the perimeter of the business to transfer, with the option of expressly excluding certain assets while including others, and of excluding certain liabilities. This may represent an advantage, for example, to the buyer, who may so be protected from risks connected to the previous management of operations by excluding their transfer.

As to the transfer itself, an asset transfer agreement must be executed before a notary public and registered at the relevant company register.

A potential disadvantage in choosing an asset deal is the application of stamp duties in proportion to the value of the business; on the other hand, the buyers may enjoy a step-up in the value of the transferred assets (see Section VIII).

ii  Share and quota deals

In share and quota deals, the underlying business is the indirect object of the transfer, which, instead, directly concerns the shares or quotas. Thus, no specific protection is given by the Civil Code on a company’s assets and on the continuity of the business activity unless specific representation, warranties and covenants are carefully drafted in the stock purchase agreement.

Italian case law now tends to admit that the duration of the contractual representations and warranties may exceed the duration of the shorter annual statutory guarantees related to sale and purchase agreements provided by law.\(^4\)

As to the transfer itself, share certificates representing the capital of joint-stock companies must be transferred through an endorsement before a notary public, whereas if the transfer involves the quotas of limited liability companies, the agreement must be executed before a notary public and registered at the company registry to be validly enforced towards third parties.

iii  Newco share deals

Recent trends in business transfers have included the use of an M&A structure consisting of the creation of a wholly owned newco on the part of the seller to which the latter transfers, by means of a contribution in kind, a business, with the subsequent transfer of the shares or quotas of the newco to a buyer. Setting aside the tax effects (see Section VIII), compared to an asset deal, such structure allows for a clear separation of the business on the part of the seller and its direct dealing with employees and other stakeholders (creditors, suppliers, customers) prior to closing. On the other hand, in the case of a breach of agreement and a refusal to close

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\(^4\) Italian Supreme Court decision No. 16963/2014.
by either party, the enforcement and specific performance of the M&A agreement, with the transfer of the business by judicial order, might be more difficult, leaving an option to claim for damages.

iv Mergers and demergers

The Civil Code regulates mergers (Article 2501 to Article 2505 quater) and demergers (Article 2506 to Article 2506 quater). Mergers can be in the form of mergers by acquisition or mergers by incorporation. In both cases, pursuant to the principle of continuity set forth by Article 2504 bis Civil Code, the company resulting from the merger assumes the same rights and obligations as the companies participating in the merger. Despite the above principle, in reality, real estate assets falling into the realm of a merger still require registration for tax purposes, pursuant to Article 4 of the attachment to Legislative Decree No. 347/1990; and a cadastral transfer pursuant to Article 1, Paragraph 276 of Law 244/2007.

The merger procedure set out by the Civil Code entails:

a the drafting of a merger project by the directors of the companies participating in the merger;

b approval of the merger project by the relevant shareholder assemblies (for unlisted companies, with a majority of at least one-third of the outstanding share capital also in a second call of the assembly);

c the drafting of financial statements;

d directors’ reports describing the economic and legal reasons underlying the merger project;

e an expert’s appraisal of the exchange ratio of the shares or quotas of the company resulting from the merger to be attributed to the shareholders; and

f the execution of the merger deed before a notary public.  

Article 2501 bis Civil Code expressly provides for mergers by means of a leveraged buyout. Before the introduction of this provision in 2003, the implementation of this type of transaction was heavily jeopardised by the provision of Article 2358 of the Civil Code, which, at that time, did not allow for a company to provide securities or issue loans for the purchase of its own shares.

As to the limits, companies that are in a winding-up procedure may not participate in a merger if the distribution of their assets has already begun, pursuant to Article 2501 of the Civil Code. Such limit only concerns joint-stock companies.

A delicate aspect to consider in mergers and demergers is the protection of the minority shareholders, if present. To this end, the exchange ratio, which represents the price of the transaction and is determined by the directors of the companies participating in the merger, is a crucial aspect of the merger itself. It is important to note that such ratio has to be described by the directors in their report pursuant to Article 2501 quinquies Civil Code and appraised by an expert appointed by the court pursuant to Article 2501 sexies Civil Code. Minority shareholders might challenge the validity of a merger until the deed of merger is registered. Thereafter, their claim is switched to a claim for damages.

5 If a merger is carried out by incorporation in a company that is totally owned (or 90 per cent owned) by the other merging company, the procedure may be simplified with the omission of some of the above-mentioned documents.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Recently, new measures have been introduced to accelerate credit recovery procedures of non-performing loans and facilitate the issuance of new credit, also to the benefit of M&A transaction financing, and new provisions have been adopted aimed, inter alia, at favouring the business continuity of insolvent or distressed companies. Among the most significant innovations are the following.

i Business Crisis and Insolvency Code

Legislative Decree No. 14 /2019, setting forth the new Business Crisis and Insolvency Code (CCI), was published in the Italian Official Gazette on 14 February 2019 and will enter into force on 15 August 2020. The CCI shall apply both to natural persons (consumers, professional and entrepreneurs) and to legal persons, and consequently all types of debtors, with the exception of the state and public entities.

The main changes set forth in the CCI with respect the current Insolvency Law are the following:

a certified restructuring plans (Article 56): this procedure now has its own specific regulation within Article 56 of the CCI; the restructuring plans shall set forth the milestones to check the actual implementation of an insolvency plan and the actions to be taken in the event that these are not accomplished;

b debt restructuring agreements (Articles 57–64): the CCI confirms the need for distressed debtors to finalise a debt restructuring agreement with creditors that represent at least 60 per cent of the total amount of claims, and introduces a facilitated debt restructuring agreement (Article 60 CCI), reducing the creditor threshold from 60 to 30 per cent. The facilitated debt restructuring agreement can be used only in cases where the distressed debtor is granted no delay for the payment of creditors who have not signed such agreement, and no temporary protective measures have been requested by the debtor towards the creditors;

c the composition of creditors (Articles 84–120): the CCI maintains the already existing two-scheme structure of liquidating all assets or preserving a business as a going concern, which can be carried out directly (by the debtor) or indirectly (by third parties). The CCI introduces a series of restrictions on the composition of creditors based on the liquidation of a company’s assets, thereby preserving the continuation of a business. A significant change from the current system is that the court will be required to also assess the economic feasibility, and not only the legal maintainability, of the plan supporting the proposal of the composition of creditors (Article 47);

d judicial liquidation (Articles 121–283): the term bankruptcy has been replaced by the term judicial liquidation (and all bankruptcy-related words have been modified accordingly), but the change is purely lexical, since a judicial liquidation maintains the same nature of the current bankruptcy proceedings;

e compulsory administrative liquidation (Articles 293–316): an exclusive insolvency procedure for banking, fiduciary and insurance companies; and

f a single proceeding to enter judicial restructuring and liquidation procedures: the CCI also establishes a single judicial process to ascertain an insolvency, applicable to all debtors irrespective of the nature of the ensuing insolvency proceedings, which shall precede the possible insolvency procedures (Articles 40–53).
In addition, the CCI has introduced a new out-of-court procedure providing for a newly non-jurisdictional composition body, the OCRI, which will be set up within the Chambers of Commerce. According to this new procedure, the OCRI will be in charge of a consultation procedure to help distressed companies return to solvency through agreements with creditors or resorting to a restructuring or insolvency procedure. In the event that this procedure fails, and a distressed debtor remains in a state of insolvency, the OCRI shall send a report to the Public Prosecutor, who can then decide to proceed with the filing of a judicial liquidation before the court (Articles 16–18).

Finally, the CCI also introduces a set of rules (Articles 284–292) for the management of the insolvency of groups of companies according to which it is possible to establish a single procedure for different companies of a group, on the basis of a single restructuring plan, maintaining a separation of assets and liabilities.

ii Privacy and data protection

The new EU General Data Protection Regulation (GDPR), aimed at unifying the privacy policies of Member States with the purpose of ensuring stronger and broader protection of data, entered into force on 24 May 2016. From 25 May 2018, the GDPR applies directly in all Member States. Legislative Decree No. 101/2018, which entered into force on 19 September 2018, has been adopted to align the national rules to the GDPR.

iii Transfer of title over real estate assets upon default

Law No. 119/2016 introduced Article 48 bis to the Banking Law, which provides financial institutions with a more direct, less costly, out-of-court enforcement procedure of guarantees on loans by allowing banks to satisfy their credits over a debtor's real estate by means of a direct transfer of such security to the creditor upon default of the borrower. Such transfer had previously been admitted by Italian courts only with reference to specific transactions, as an exception to the general rule pursuant to Article 2744 of the Civil Code. In particular, this new legal provision admits that loan agreements executed between banks or other financial institutions authorised to issue credit and entrepreneurs may be guaranteed by a registered transfer of title over the debtor's real estate assets, conditioned to the breach of his or her obligations pursuant to the loan agreement, and complies with Italian law principles through the provision of the *patto marciano* (Article 48 bis Paragraph 2 of the Banking Law). The latter allows a lender, for loans secured by property, to obtain the transfer of such property upon default by the borrower, but requires that the creditor, in the event that the appraised value of a real estate security exceeds the relevant outstanding debt, shall have to correspond to the debtor the difference in value directly in his or her bank account. Under certain conditions, this transfer procedure may also apply if a court enforcement is initiated, and if the debtor undergoes bankruptcy.

iv New security interest over movable assets

As a general rule, Article 2786 of the Civil Code provides that a security interest over movable assets is executed by delivering the relevant asset to the secured creditor, with a few relevant exceptions (such as a pledge over financial instruments pursuant to Legislative Decree No.

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6 EU General Data Protection Regulation No. 2016/679.

170/2004 and the special privilege pursuant to Article 46 of the Banking Law). To render credit transfers more flexible, in line with other jurisdictions, Article 1 of Law Decree No. 59/2016 introduces the possibility for entrepreneurs to grant a pledge over non-registered, movable company assets to creditors without losing the right to trade or use the relevant movable asset. The entrepreneur is expressly allowed to dispose of the secured asset (e.g., by transforming or selling it), and the assets deriving from such use will be subject to the same security interest without having to carry out any formality for the constitution of a new security.

IV  FOREIGN INvolvement IN M&A Transactions

With respect to cross-border transactions, inbound deals amounted to 23 per cent of the total value of deals in 2018, whereas outbound deals increased with respect to the previous year, representing 60 per cent of the total value in 2018. The main foreign investors in Italy are still the United States and France, although China has still significantly increased its investments.8

V  Significant Transactions, Key Trends and Hot Industries

In 2018, the consumer market sector alone represented around one-third of the Italian M&A market in value, instead of financial services, which have suffered a slowdown and represented only 9 per cent of the Italian M&A market in terms of value. This was followed by the support, services and infrastructure sector at 30 per cent, energy and utilities at 7 per cent and industrial markets at 6 per cent.9

Among the most relevant deals of the past year are the following:

a  in the consumer market sector, Essilor and Luxottica, the world's largest lens and frame manufacturers, successfully completed a €48 billion merger and formed a holding company named EssilorLuxottica. The merger was officially completed after Luxottica's major shareholder, Delfin, contributed its entire 62.42 per cent Luxottica stake to Essilor;

b  Atlantia SpA, a company operating in the field of infrastructure and mobility networks, indirectly acquired a participation in Abertis equal to 50 per cent by means of the incorporation of Abertis Partecipaciones SA, whose entire share capital is in turn held by a Spanish newco, Abertis HoldCo, 51 per cent of which is owned by Atlantia, 30 per cent by ACS and 19 per cent by Hochtief. Abertis Partecipaciones SA acquired 98.7 per cent of the entire share capital of Abertis for an amount equal to €16.2 billion. In the same transaction, Atlantia also acquired a 23.9 per cent participation in Hochtief through a transfer of shares by ACS for a total value of €2.4 billion;

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9 According to the recent 2018 M&A presentation ‘Il mercato M&A in Italia: trend e prospettive’, with the cooperation of KPMG and Fineurop Sodicitic, and sponsored, among others, by Università Commerciale Luigi Bocconi and AIFI.
a consortium of investment funds controlled by CVC Capital Partners acquired the entire share capital of Fimei, the holding company that holds around 51.8 per cent of the Recordati pharmaceutical group, for an amount of around €3 billion;
d the American Global Infrastructure Partners fund acquired the entire share capital of Italo-Ntv, the second company operating in the road and infrastructure field on the Italian territory, for around €2 billion; and
e in the financial services sector, banking groups continued their strategy to sell and outsource some of their non-core activities: among others, Banca Carige SpA completed the transfer of its majority shares of Creditis Servizi Finanziari SpA to the investment fund Chenavari Investment Managers.\textsuperscript{10}

\section*{VI \quad FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS}

Bank loans still represent an important instrument in M&A financing. In 2018, the stock of non-performing loans was smaller, both as a result of bad loan sales and because fewer defaults occurred. Expansionary monetary conditions contributed to a reduction in funding costs, which fell to very low levels in historical terms.\textsuperscript{11}

The issuance and refinancing of debt have also increasingly grown as means of M&A financing, along with the issuance of straight equity (although this is generally more expensive for the company) and shareholders’ loans. The latter are usually subordinated to bank financing.

Recent changes in the above-described rules governing the granting of security, aimed at facilitating the enforcement of mortgages and pledges, might increase the amount of asset-based financing in the near future in connection with M&A transactions.

\section*{VII \quad EMPLOYMENT LAW}

On 11 August 2018, the Dignity Decree\textsuperscript{12} was adopted by the recently established government, and was subsequently converted into law and published in the Official Gazette.

The Dignity Decree, inter alia, enacts significant changes concerning fixed-term employment contracts aimed at reducing the precariousness of workers under such contracts. These changes are pursued through several innovations, including:
a a reduction of the duration of such contracts;
b the introduction of a requirement to justify the reasons for entering into fixed-term contracts;
c a reduction in the number of permitted extensions of such contracts;
d an increase in the contributions payable by employers in connection with each contract renewal; and
e a new cap for temporary agency workers in terms of percentage.

\textsuperscript{10} Santa Maria Law Firm assisted the purchasers in both transactions.
\textsuperscript{11} See Bank of Italy’s Annual Report dated 31 May 2019.
\textsuperscript{12} Dignity Decree No. 87 of 12 July 2018.
In particular, a fixed-term contract can be entered into without a justifying reason only if its duration does not exceed 12 months. In the case of a longer duration (as well as in the case of renewal for an overall duration of more than 12 months), a justifying reason is always required.

The reasons for an employer to enter into a fixed-term contract must be as follows:

a to meet temporary and objective needs beyond a business’s ordinary activity;
b to meet a need to temporarily replace other workers; or
c to meet a need related to temporary, significant and non-programmable increases in ordinary activities.

In the absence of valid reasons justifying a fixed-term contract exceeding 12 months (or in the case of renewal an overall duration exceeding 12 months), the employment will be automatically converted into an open-term employment starting from the expiry of the first 12 months.

The overall duration of a fixed-term employment contract cannot exceed 24 months, including all extensions, with the exclusion of seasonal employment contracts and possible longer durations set forth by the applicable collective labour agreements.

The maximum number of permitted extensions is four; in the event of a fifth extension, an employment contract is immediately and automatically converted into an open-term contract, irrespective of the overall duration of the employment.

Staff leasing is governed by the same rules applicable to fixed-term contracts. To the exclusion of certain specific categories, the total number of temporary agency workers and fixed-term employees cannot exceed 30 per cent of the number of open-term employees as of 1 January of the year in which each worker is hired, unless collective labour agreements set forth otherwise.

As to the increase in social contributions, upon each renewal of a fixed-term employment contract, a 0.5 per cent increase becomes due by the employer, in addition to the standard contribution, for the entire duration of the renewal.

VIII TAX LAW

i Asset deals and mergers

In terms of tax implications, asset deals are generally characterised by:

a direct taxation on the seller’s capital gain (i.e., the difference between the sale price and the fiscal cost of a business). If the seller is a joint-stock company or limited liability company, the capital gain is subject to corporate income tax, with the application of the 24 per cent tax rate;
b exclusion from indirect taxation (no application of VAT); and
c application of stamp or registration duties in proportion to the value of the business.

Contributions of going concerns, mergers and demergers allow for a step-up in the tax basis of the target’s underlying assets13 and goodwill14 through the payment of a sum ranging from 12 to 16 per cent, thus reducing the taxable income by means of deductions and depreciations.

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13 See Law No. 244/2007.
14 See Law Decree No. 185/2008.
The buyer of a going concern, pursuant to Article 14 of Legislative Decree No. 472/1997, is jointly and severally liable, with the seller, for the tax liabilities concerning the transferred assets. However, these liabilities (due taxes and penalties) are limited to:

a. the value of the assets;
b. those relating to the two fiscal years prior to the year of transfer and the year of transfer itself; and
c. those audited in the two fiscal years prior to the year of the transfer or in the year of the transfer itself, even if the liabilities relate to previous years.

These limitations do not apply in cases of tax fraud.

Furthermore, a buyer’s liabilities may be further limited by the issuance of a tax certificate by the Tax Authority prior to the closing of the transaction.

Article 1, Paragraph 87 of Law No. 205/2017 amended Articles 20 and 53 bis of the Consolidated Stamp Duty Act with the intent of clarifying that deeds to be registered are not to be requalified on the basis of the overall economic effects achieved within a framework of several connected deeds. The new Article 20 provides that, for the purposes of correctly applying the stamp duty, the registered deed has to be interpreted by exclusively considering the deed in itself, without taking into account any external element such as, for example, connected deeds or other elements beyond the text of the deed at issue.

For example, deeds concerning a contribution of a going concern followed by a sale of the shares of the transferee company are not to be requalified as asset deals. Law No. 205/2017 also amended Article 53 bis of the Consolidated Stamp Duty Act in terms of enhancement of the powers of the Financial Administration with reference to the abuse of stamp, mortgage and cadastral duties.

Share and quota deals are instead characterised by:

a. the participation exemption, applicable subject to certain conditions, with reference to 95 per cent of the capital gain obtained by the sale by joint-stock companies or limited liability companies (or less);
b. the application of a flat rate registration duty; or
c. a VAT tax exemption.

However, if a deal concerns the shares of a joint-stock company resident in Italy, a Tobin tax of 0.2 per cent applies, with the exception of shares of listed companies whose average market capitalisation in November of the year prior to the transfer was less than €500 million.

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16 The conditions of the application of the participation exemption are the participation has been owned continuously for at least 12 months prior to the sale; the participations were classified as financial fixed assets in the financial statements relating to the first tax period of uninterrupted ownership; the subsidiary company is resident for tax purposes in a white list country; and the subsidiary is actually carrying out a business activity.
17 See Law No. 228/2012 Paragraphs 491 et seq.
iii Newco share deals

The M&A structure by which the seller constitutes a newco to which he or she transfers, by means of a contribution in kind, a business, with the subsequent transfer of the shares or quotas of the newco to a buyer, is expressly admitted by Article 176 Paragraph 3 of Presidential Decree No. 917/1986 and is qualified as non-elusive of direct taxes. As for indirect taxes (VAT, register, or both), recent case law has confirmed the non-elusive effects.18

IX COMPETITION LAW

Except in specific circumstances, under Law No. 287 of 10 October 1990 (Law), the filing of a request for the clearing of a concentration (e.g., a merger, a joint venture or an acquisition of control over another company) before the IAA is mandatory when two cumulative turnover thresholds are met. Said thresholds were recently modified by the Yearly Competition Act19 and subsequently updated. As a result of these changes, Section 16(1) of the Law requires prior notification of all M&A involving undertakings whose aggregate turnover in Italy exceeds €498 million, and where the aggregate domestic turnover of each of at least two of the undertakings concerned exceeds €30 million.

Concerning the above-mentioned requirements, prior to the reform of January 2013, the turnover thresholds were alternative rather than cumulative. As a result, the number of concentrations assessed by the IAA dropped considerably (only 73 in 2018). In 2018, out of 730 concentrations the IAA opened proceedings only in six cases. In addition, the reform also abolished the filing fees to be paid upon the filing of a transaction and replaced them with an annual tax on the turnover of all corporations based in Italy. However, the revision of the turnover thresholds by the Yearly Competition Act was precisely aimed at broadening the scope of merger control by the IAA, with particular reference to joint ventures and acquisitions of joint control over targets with a low turnover.

The filing of a transaction must precede execution. The IAA may also consider receivable notifications that concern non-binding agreements insofar as they are supported by solid documentary evidence. It would therefore be possible to notify a concentration on the basis of a memorandum of understanding or preliminary agreement. The deadline for the notification is the closing of an operation.

Contrary to what occurs under Regulation (EC) 139/2004, Italian merger control law does not impose an automatic standstill obligation on parties. Therefore, in theory it would be possible to realise a concentration after filing but before authorisation, while accepting the risk of a de-concentration order from the Authority. However, the absence of an automatic standstill obligation does not exclude the possibility that the IAA will directly require the parties to suspend their concentration following a specific decision.20 With the aim of facilitating the evaluation of an assessment by the IAA and reducing risks that could delay the duration of the procedure, the IAA suggests a discussion of possible issues related to an operation even before notification of a concentration (pre-notification phase).

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18 Italian Supreme Court decision No. 2054/2017.
19 The Yearly Competition Act, Law No. 124/2017.
20 Note that the scope of the obligations arising from interim covenants, which are concluded by the merging parties to regulate their relationship during the period from the signing to the closing, are currently under the scrutiny of the European Court of Justice in case C-633/16, Ernst & Young.
Once a request for the clearance of a transaction is filed before the IAA, the procedure continues in two distinct phases, a first (necessary) step and a second (possible) step. The first step begins with the filing and shall end within 30 days. At the end of this phase, the IAA may decide to clear the transaction, or to initiate a more in-depth investigation in the event that it considers that an operation is likely to be prohibited. The delay is suspended if the parties communicate inaccurate or false information and will begin again only from the reception of additional information (stop the clock). For the same reason, the IAA may decide to postpone the opening of a second phase beyond the delay of 30 days. The second step begins with the IAA notifying parties of a decision to initiate proceedings. This second phase has a 45-day duration and can be extended only once for a maximum duration of a further 30 days.

The IAA may authorise a concentration subject to commitments undertaken by the parties to address its concerns. Contrary to procedures before the European Commission, these commitments may be both proposed by the parties and prescribed directly by the Authority. In any event, commitments are generally available only in the second phase of the procedure, this being another difference from the procedure applied under Regulation (EC) 139/2004.

X OUTLOOK

In the first quarter of 2019, the number of transactions slightly decreased with a total value of €4.2 billion, thus highlighting a slowdown compared to the value seen in the first quarter of 2018. However, there are some interesting transactions envisaged that will be completed in 2019, among which are the sale of Magneti Marelli to the KKR Fund for €6.2 billion, the sale of Generali Leben (part of the Generali Group) and the announcement of the Nexi SpA initial public offering for an equity value of €6.2 billion.21

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21 According to the recent 2018 M&A presentation ‘Il mercato M&A in Italia: trend e prospettive’, with the cooperation of KPMG and Fineurop Soditic, and sponsored, among others, by Università Commerciale Luigi Bocconi and AIFI.
I  OVERVIEW OF M&A ACTIVITY

M&A transactions are an active and consistent presence in the Japanese market. The aggregate number of M&A transactions in which Japanese companies were involved, whether domestic, inbound or outbound, was 3,850 in 2018, according to Recof’s analysis, representing an increase of approximately 26 per cent from 2017.

i  Domestic transactions

In 2018 the number of domestic M&A transactions in the Japanese market was approximately 2,800, a record high. Most Japanese companies regard M&A as one of the most important business strategies to achieve growth and operating efficiency. In addition, many traditional Japanese large-scale (involving conglomerates) companies, such as Hitachi and Toshiba, are actively divesting non-core businesses (whether in subsidiaries or affiliates), and aiming at emphasising their core businesses, in the hope that their return on equity (ROE) can increase. In the past, most Japanese companies were severely criticised by, particularly, foreign investors for their low ROEs as compared with those of US and European companies; however, this has been much improved by the increasing number of Japanese companies divesting non-core businesses, and a focus on corporate ROE has been one of the objectives of the economic strategy under the Abe administration (Abenomics). As a result, private equity (PE) funds have been prominently featured as key buyers of divested businesses and operations, having access to low financing costs through the Bank of Japan’s ongoing quantitative and qualitative easing monetary policies and investors’ appetite for better returns in the low interest rate environment. It was reported that the number of domestic M&A deals involving PE funds, whether Japanese domestic or global, was approximately 750 in 2018, which also was a record high.

ii  Inbound transactions

Although the number of inbound transactions in Japan where foreign buyers, whether strategic or financial, acquire Japanese target companies is not as numerous as either purely domestic or outbound transactions, because many traditional Japanese companies are having difficulties increasing their ROE and others are facing challenges to their survival without...
injections of capital or other support, the number of inbound transactions has grown steadily in recent times. Approximately 260 transactions were reported in 2018, which represented an approximately 30 per cent increase from 2017. Among notable inbound transactions were:

- the acquisition of Toshiba Memory, Toshiba’s subsidiary, by Bain Capital, an active US PE fund, and its consortium (which comprised international investors, including a Korean competitor) for approximately US$18 billion;
- the acquisitions of Hitachi Kokusai Electric and Hitachi Koki, subsidiaries of Hitachi, by KKR, for approximately US$2.2 billion (inclusive of dividends, US$2.8 billion); and
- the acquisition of Asatsu-DK (ADK), the third-largest and a traditional advertising agency company in Japan, also by Bain Capital, for approximately US$1.35 billion.

iii Outbound transactions

Because of the shrinking of the Japanese market caused by the aging society and declining population, Japanese (particularly, listed) companies are obliged to seek to expand their businesses overseas, as domestic organic growth can no longer be expected. Many Japanese companies have expressly announced that they intend to seek to engage in outbound M&A transactions and to increase their investment into foreign markets. In 2018, the number of outbound M&A transactions was reported to reach a record high. Among others, the acquisition of Shire plc (see Section V.i) by Takeda Pharmaceutical is the largest acquisition by a Japanese company in market history in terms of purchase price (approximately £46 billion). As a result of this and other transactions, the aggregate transaction value of outbound deals significantly rose in 2018, reflecting an approximate 150 per cent increase from the previous year.

On the other hand, the acquisition of a foreign company can be operationally and culturally challenging for any purchaser, whether Japanese, US or European. Consequently, it has been reported that many Japanese companies that closed acquisitions in outbound M&A transactions have struggled during the period following post-merger integration (PMI), and several companies have had to write off significant amounts of goodwill in their acquisitions under the International Financial Reporting Standards. In response, the Ministry of Economy, Trade and Industry (METI) established a study group of Japanese companies’ M&A transactions overseas, and released a report in March 2018 reflecting various issues and providing suggestions and also some guidelines for Japanese companies in conducting outbound M&A deals. Nevertheless, despite these operational and other issues, the increasing trend of outbound M&A transactions is expected to continue as Japanese companies (are obliged to) seek to increase their growth and future prospects.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

It is generally stated in Japan that an M&A transaction is defined as a transaction where control of a target company is transferred in any manner. In this regard, M&A transactions can generally be grouped into three categories: stock transfers, business transfers, and statutory mergers and other corporate restructuring transactions.
i  Stock transfers

This structure is the most frequently utilised in Japanese M&A deals and the best known. A stock transfer agreement, or stock sale and purchase agreement (SPA), is based on an agreement regarding the transfer of the stock in a target company between a seller and a buyer and is basically governed by the Civil Code of Japan. While no formality including a stock transfer form is required for an SPA to be effective in Japan, recent transactions in Japan using a SPA have been negotiated with reference to deal styles employed in the US market; provided, however, that the perfection of the transfer of the stock in the target company requires a change of the stockholder’s name in the records of the target company from the seller to the buyer, which is not subject to the payment of or submission of an exemption from stamp duty as is the case in the United Kingdom. Although stock acquisitions in the US can include a feature where the target company newly issues shares that give the buyer (who subscribes for these newly issued shares pursuant to a share subscription agreement) a control right with respect to the target company, in Japan the use of a share subscription agreement is generally regarded as being a different category from SPA transactions, as share subscriptions are governed by the Companies Act of Japan.

For a buyer to obtain control of a target, it is generally thought in Japan that the buyer only has to purchase a (simple) majority of the target’s outstanding shares. However, as the Companies Act provides that a two-thirds vote is required for certain major corporate actions to be adopted as a resolution at a general shareholders’ meeting of the target company (as a special resolution), it is sometimes said that the purchase of the majority of outstanding shares of a target is not sufficient, but rather two-thirds is required. In this regard, generally speaking, for a buyer to acquire one-third or more of the outstanding shares of a listed target company, the buyer is obligated to make a tender offer or use takeover bid procedures provided in the Financial Instruments and Exchange Act of Japan, known as a ‘mandatory TOB procedure’ and based on the UK and European regulatory approach. Furthermore, if a buyer intends to purchase two-thirds or more of the outstanding shares of a listed target company through the TOB procedure, the buyer is obligated to purchase all shares tendered and offered by the shareholders of the listed company, even if the buyer expressly announces an upper limit of the number of shares that the buyer intends to purchase (referred to as the ‘mandatory obligation to purchase all of the offered shares in the TOB procedure’), as is also the case with UK and European regulations. Except for these two mandatory points, the TOB procedure in Japan is similar to the tender offer process in the US market.

ii  Business transfers

A business transfer agreement (which is governed by the Companies Act) was often utilised in Japan so that a buyer succeeds to a transferred business of a seller. However, for the business transfer to be perfected, any and all registrations, licences, permissions, etc., have to be perfected in light of any and all assets (including real estate, intellectual property rights, licences, permissions), and the process for the closing of a business transfer was therefore very tedious and time-consuming.

Accordingly, a company split agreement, which was adopted in the Companies Act relatively recently, is now often used instead of the business transfer structure. In a company split, the process generally entails a transferring company (namely, the seller) splitting a portion of its business following a resolution adopted at a shareholders’ meeting, and the split business is automatically transferred to a succeeding company (namely, the buyer), that is, an
effect of universal succession. As a practical matter, a company split is much more convenient and efficient as compared to the business transfer structure, and this form is therefore often used these days.

**iii Statutory mergers and other corporate restructuring transactions**

**Statutory mergers**

A statutory merger in Japan is almost equivalent to that seen in the United States and European countries. In a statutory merger, generally speaking, the disappearing company is merged into the surviving company, as a result of which those two companies will be integrated into one merged company. Tax and accounting impacts usually determine which company (namely, the buyer or the seller) is the disappearing company and which is the surviving company.

**Stock exchanges**

A stock exchange agreement is a very efficient and straightforward transaction so that a target company automatically becomes a 100 per cent subsidiary of a buyer if both the target and the buyer obtain a special resolution (i.e., two-thirds approval) at a general shareholders’ meeting. In this process, no mandatory requirements relating to the TOB procedure are necessary even if the target is a listed company.

**Stock transfers**

A stock transfer is a unique process under the Companies Act, and is not a simple transfer of stock (or shares) of a target company. The process was originally introduced in order for a company to newly incorporate a 100 per cent parent company (i.e., for a holding company of one or more existing companies to be created). However, in the context of M&A transactions, a stock transfer is utilised in a situation where two companies intend to integrate their businesses in an umbrella structure of one holding company; namely, if shareholders of the two companies adopt a resolution at a general shareholders’ meeting approving the joint-stock transfer agreement, a joint holding company will be newly established, and the two existing companies will be 100 per cent subsidiaries of the joint holding company. As it may not be clear which company from among such two companies is the buyer (or the target) and this ambiguity is suitable to mores in Japanese business society, this structure has been used in various deals in the Japanese market where the transaction was intended to act as an integration of equals rather than being considered a takeover of one company by another (such as the Isetan/Mitsukoshi and Dwango/Kadokawa combinations, and recent business integrations of regional banks, including the Concordia group).

However, this approach may minimise successful PMI and lead to entrenched redundancies rather than increased efficiencies if the two operational subsidiaries remain as sister companies after closing. Stock transfers have been recently criticised on the basis that unless and until the actual integration of the two subsidiaries is conducted, the effect of the transaction as a successful M&A transaction is questionable.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Significant recent statutory amendments and proposals

First, while cash-out mergers have been legally possible in Japan, this transaction type requires numerous technical procedures, including special approval at a general shareholders’ meeting and court procedures, for such a merger to be effective. The Companies Act was amended relatively recently so that a shareholder holding 90 per cent or more of a target company can force the other shareholders to sell their shares in the target to the acquirer with the approval of the target’s board of directors. As a result, in many cash-out transactions of publicly held companies where bidders seek to obtain all of the outstanding shares of the target, bidders have stated in their TOB announcement that they would seek to exercise this right if they were able to acquire 90 per cent or more of the target’s outstanding shares through the tender offer.

Secondly, although bidders are allowed to use shares as consideration in tender offers in Japan, in practice, only cash has been so far utilised as the offered consideration because of certain procedural obstacles in the Companies Act and the resultant tax treatment (namely, a capital gains tax is imposed on the selling shareholders, and carrying-over is not permitted). An amendment has been proposed, however, which if adopted would eliminate this procedural process and enable a Japanese stock company to more easily use its own shares as consideration in a tender offer to acquire more than 50 per cent of a target company’s (including a foreign target company’s) voting shares. The proposed amendment would also affect the tax characterisation so that any capital gain arising from the sale of shares can be carried over if certain requirements are satisfied. (This tax law change would apply more generally and not just in tender offers.) This is in addition to the already adopted amendments to the Industrial Competitiveness Enhancement Act and the relevant tax law (they became effective in 2018) that aim to facilitate transactions utilising own shares as consideration.

Thirdly, although still at the proposal stage, it is also planned that the Companies Act is to be amended to further promote corporate governance reforms. In this regard, the proposals include, among other things, requiring listed companies to appoint outside directors, determine and publicly disclose their remuneration policies, and electronically provide their business and other reports as well as the agenda of shareholders’ meetings online. The bill to amend the Companies Act containing these proposals is expected to be presented to the Diet in the latter half of 2019 or thereafter. While it is uncertain whether and how those amendments may affect M&A transaction activities involving listed companies, more input from and discussion with outside directors and shareholders are expected to stimulate the companies’ consideration of appropriate potential transactions.

IV RECENT LEGAL AND COMMERCIAL DEVELOPMENTS INVOLVING LISTED COMPANIES THAT AFFECT M&A TRANSACTIONS

i Soft law impacts

The Tokyo Stock Exchange adopted Japan’s Corporate Governance Code (CGC) in 2015, with an amendment thereto in 2018 in response to the increasing globalisation of the world economy and growing expectations for established rules of conduct for directors of Japanese listed companies. The CGC takes a comply or explain approach: namely, listed companies are not required to comply with each principle set out in the CGC, but they are required
to explain the reason if they do not comply with any of the CGC’s principles. Although the CGC is just soft law and is not legally required to be complied with, and nor is it enforceable by the courts, listed companies are obligated to comply with the CGC to continue their listing on the Exchange; as a result, adherence to the CGC has become an established custom by listed companies, and it is expected that the courts will recognise the CGC principles as appropriate rules of conduct applicable to directors of all Japanese listed companies.

In addition, the Council of Experts on the Stewardship Code, a council body set up by the Financial Services Agency of Japan (FSA), provided Japan’s Stewardship Code (JSC) in February 2014 and updated it in May 2017. The underlying philosophy of the JSC is to promote awareness of the fiduciary responsibilities that institutional investors owe to their investor clients, and to seek to encourage those institutional investors to engage in dialogue with their investee-listed companies to enhance the mid and long-term return on their investments. In Japan, similar to most other markets, institutional investors are major players in the stock market. The JSC also adopts a comply or explain approach, and expects institutional investors to voluntarily adopt principles and follow its suggested guidelines.

Increasing pressure from the market and clients have caused traditional institutional investors to more keenly recognise their responsibilities and accountability to clients, and this enhanced awareness has gradually changed the voting practices of investors, including votes concerning proposed M&A transactions. Although the JSC is addressed to institutional investors and does not bind investee-listed companies directly, it has played a substantial role in promoting enhancement of listed companies’ corporate governance through the improvement of the monitoring of corporate activities and results by institutional investor shareholders.

In March 2018, the FSA published a draft guideline for investor and company engagement, which became final and effective in June 2018. This guideline is intended to supplement the CGC and the JSC and encourages institutional investors and listed companies to particularly focus on their dialogue with each other. As a result, it was recently said in Japan that although directors of Japanese companies (including listed companies) do not legally owe any fiduciary or other duties directly to each shareholder, but only an indirect duty to shareholders through their direct statutorily prescribed duty of care of a prudent manager to the company, directors of listed companies now have become obliged to make business judgements as if they directly owed a fiduciary duty to their companies’ shareholders as result of the impact of the CGC and the JSC. Japan has been a very difficult market for a long time, particularly, for hostile takeovers and activists, and these developments may signal changes in this area.

There have been only very limited cases where shareholders have brought actions against directors who have rejected hostile takeovers, or put pressure on boards to obtain favourable acquisition prices or proposals from activists or other third parties seeking to increase a company’s return on equity, or sought to engage management seeking to increase the efficiencies of businesses. However, now that listed companies and their major shareholders (namely, institutional investors) are adopting the principles set forth in the CGC and the JSC, directors of listed companies face difficulty in rejecting hostile takeovers out of hand or without a reasonably justifiable basis that is in the best interests of the company and that of its shareholders. At the same time, institutional investors find it difficult to support a target management’s attitude without reasonable analysis and considering whether the management’s attitude promotes the best interests of the company and shareholders.
In this regard, although it is a controversy involving listed Japanese real estate investment trusts (J-REITs), as of the end of May 2019, Star Asia Group, through Star Asia Investment Corporation, a J-REIT, is trying to take over Sakura General REIT Investment Corporation, another J-REIT, in a hostile transaction by seeking to convene a unitholders’ meeting of the target so as to consider resolutions that would effect the takeover. Specifically, Star Asia Group has asked investors in Sakura General REIT Investment Corporation to call a unitholders’ meeting at which the cancellation of the existing asset management contract and the approval of a new asset management contract will be on the agenda: if these actions are taken, then management control of the target would change. Sakura General REIT Investment Corporation, however, has shown strong willingness to oppose this, and has called on investors to oppose Star Asia Group’s proposals. This has attracted much attention because, if successful, it would be the first hostile takeover of a J-REIT.

ii Change of circumstances involving listed companies in Japan

Traditionally, shares in Japanese listed companies were cross-held by their business partners, including their main banks, who acted as stable and management-supportive shareholders. It has been said that this system of cross-shareholding weakened the market discipline that should have been applied to listed companies and caused inefficiencies in the use of companies’ financial resources. Almost a decade ago, the law and regulations were amended to require listed companies to explicitly disclose, in their annual securities reports, the amount of shares held in other listed companies and the purpose of such share ownership. In addition, the CGC requests listed companies to disclose their policies with respect to cross-shareholdings. The updated CGC further requests listed companies to disclose various matters relating to their cross-shareholdings. With the strengthened emphasis on disclosure of cross-shareholding and increasing pressure from the market, many listed companies gradually have decreased the amount of their cross-shareholding, and now, listed companies have fewer passive and management-friendly or supportive shareholders, and increasingly face the discipline of and pressure from the stock market to improve their financial performance.

Moreover, with the growing global trend of shareholder activism and changes in the Japanese market environment, including enhanced corporate governance measures, activist funds are expected to increase their presence and seek to target more and more listed Japanese companies. Indeed, there have been several, albeit not many, large-scale or notable cases indicating the success, or at least the significant impact, of shareholder activism in the past few years. This trend will lead to increased market discipline being put on listed companies to improve their ROE.

In November 2018, the METI launched a new study group, the Fair M&A Study Group, so that best practices in handling conflicts of interest that can arise in M&A transactions can be followed in Japan. The Group is looking at, among other things, management buyouts and squeeze-outs by controlling shareholders and considering what changes, given the current environment surrounding Japanese listed companies, should be implemented. It is expected that the Guidelines for Management Buyout published in 2007 would be updated as a result of the Fair M&A Study Group’s report. This update is expected to reflect the accumulation of legal and practical discussions and the progress of corporate governance reform over the past few years.
V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

As noted earlier in Section 1, given Japan’s ageing society and declining population, which has put a strain on domestic organic growth, as a result of which the Japanese domestic markets are expected to continue to shrink, more and more Japanese companies intend to make or increase significant investments overseas. To do so, many will seek to engage in M&A transactions. A typical example is the unprecedented large-scale (i.e., the largest in history) acquisition of Shire plc, an Irish-headquartered corporation, by Takeda Pharmaceutical, a leading Japanese pharmaceutical company, with a purchase price of approximately £46 billion. As is often stated, the pharmaceutical and generics industries in Japan have to, and therefore are eager to, lay greater emphasis on expanding their business overseas to grow and expand their portfolios. It is generally said that the chemical and electric components (excluding semiconductors) manufacturing industries also are active in outbound M&A transactions.

While the Japanese economy has had stable growth for several years now because of Abenomics and the length of its favourable business climate has reached a record high (as in the United States), on the other hand, not all sectors of Japan’s economy has been favourably affected. For example, Japan’s regional banks are struggling due to the Bank of Japan’s continuous quantitative and qualitative easing policy (zero or negative-interest policy), and the FSA has pressured a number of these regional banks, generally those that have declared losses in their recent business years, to consider a business integration with other strong or creditworthy regional banks. As a result, there have been several prominent transactions in this sector, such as the establishment in 2016 of Concordia Financial Group, currently the second-biggest regional bank in Japan, by means of a merger between Yokohama Bank and Higashi Nihon Bank, and the formation in 2017 of Kansai Mirai (Future) Financial Group, Inc, the biggest regional bank group in the Osaka area, through the business integration of Kinki Osaka Bank, an affiliate of Resona Bank, and Kansai Urban Bank and Minato Bank, affiliates of Sumitomo Mitsui Banking Corporation. In addition to these notable integrations, there also have been various other recent business integration and M&A transactions involving regional banks. This trend is expected to continue given the severe environment surrounding Japanese regional banks.

In addition, as already referred in Section 1 as well, traditional and large-scale Japanese conglomerates that aim to focus more on their core businesses and to increase their ROE and efficiency have been actively divesting their non-core businesses, whether conducted directly or through subsidiaries and affiliates. Given this seller-side demand, supported by low funding costs and investors’ strong appetite for better returns in the extreme low interest rate environment, PE funds have played an important role as the key acquirers of those divested businesses.

In this regard, not only domestic PE funds but also foreign PE funds are very active in these divestiture M&A transactions. Some of these transactions have been very large in scale, such as the acquisition of Toshiba Memory by Bain Capital, a US PE fund, and its consortium, the acquisition of Asatsu-DK by Bain Capital, and acquisitions of Hitachi Kokusai Electric and Hitachi Koki by KKR, another US PE fund.
VI OUTLOOK AND CONCLUSIONS

Despite the unstable global economy, particularly given the trade war between the United States and the People’s Republic of China, and the existence of various geopolitical risks, it is expected that the M&A market in Japan will continue to be active, and most likely will expand even more. The trends of Japan’s ageing society and declining population will be challenging to change despite government policies seeking to do just that. The strong demands of shareholders and investors toward listed companies for higher ROE and return on investment are putting continuous pressure on those listed companies to continue to grow and to operate at higher and higher levels of efficiency.

Even if the Bank of Japan’s unprecedented easing policy were to be abolished and even if the strong stock market were to be weakened, there is no factor currently foreseen that will lessen Japanese companies from being involved in M&A transactions.
Chapter 28

KOREA

Ho Kyung Chang, Alan Peum Joo Lee and Robert Dooley

I OVERVIEW OF M&A ACTIVITY IN 2018

Korean M&A activity in 2018 showed a slowdown in deal value compared to the previous year, with 1,167 completed cases and a total value of US$52.8 billion (a 17.1 per cent decrease from 2017 in total deal value). While the number of transactions increased by 12.7 per cent from 2017, the total deal value declined. A rise in uncertainty in the global economy resulting from international trade disputes, Brexit and other factors seem to have led to a decline in larger-sized deals.

Domestic M&A activity involving Korean companies showed more mixed signals, with 570 acquisitions of Korean companies by other Korean companies (up from 514 in 2017) worth US$37.2 billion (down from US$46.0 billion in 2017). The increase in the number of domestic M&A transactions is generally credited to an increase in small-sized deals for business restructuring purposes. There was a particular increase in domestic M&A transactions among affiliates, recording the highest number in the past five years.

The number of transactions as well as deal value of inbound M&A (i.e., overseas companies acquiring Korean companies) declined conspicuously, with 37 transactions (down from 41 in 2017) worth US$4.3 billion (down from US$8.8 billion in 2017). More detailed discussion of foreign direct investment into Korea can be found in Section IV.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Acquisitions of private companies in Korea are primarily governed by the Korean Commercial Code (KCC), the Financial Investment Services and Capital Markets Act (Capital Markets Act) and the Monopoly Regulation and Fair Trade Act (MRFTA).

The KCC contains the main rules of corporate structure and governance, including requirements for, and limits on, mergers, share acquisitions, spin-offs and asset transfers. As such, the KCC will influence the transaction structure, and dictate corporate approval requirements, for both public and private companies. The KCC also governs directors’ fiduciary duties, regulations on self-dealing and other corporate conflicts of interest.

1 Ho Kyung Chang is a partner, Alan Peum Joo Lee is an associate and Robert Dooley is a foreign attorney at Bae, Kim & Lee LLC. The authors would like to thank their colleagues Ben Gu, Namwoo Kim and Eun Hong Lee for their significant assistance in preparing this chapter.
2 Thomson Reuters, Merger & Acquisitions Review Full Year 2018.
3 References to M&A activity in this chapter are based on the deals notified to the Korea Fair Trade Commission (KFTC) during 2018, and reported in the press release issued by the KFTC on 5 March 2019 providing merger notification data for fiscal year 2018 (KFTC’s 2018 M&A Review).
The Capital Markets Act applies to public companies listed on the Korea Exchange (KRX), which includes the KOSPI, KOSDAQ and KONEX markets. The Capital Markets Act imposes disclosure requirements and other restrictions on trading in KRX-listed shares. It also prescribes rules for tender offers. Further, M&A deals involving public companies are subject to KRX disclosure rules and scrutiny by the Financial Supervisory Service (FSS), the enforcement arm of the Financial Supervisory Commission (FSC). FSC, through FSS, generally administers the financial, banking and securities system in Korea.

Under the MRFTA, which is the main antitrust statute, acquisitions and other combinations involving companies satisfying certain revenue and assets thresholds will require antitrust review by the Korea Fair Trade Commission (KFTC).

The Foreign Investment Promotion Act and Foreign Exchange Transactions Act govern foreign direct investments and foreign exchange transactions involving foreign investors in Korea. Foreign investments generally require a report to a foreign exchange bank, which is in most cases a formality, and acceptance of the report is usually granted within a few days.

While foreign investors are in principle not prohibited from acquiring shares in a Korean company, there are prohibitions or limits on foreign ownership in Korean companies engaging in certain industries considered to be vital to the national interest, such as defence, broadcasting, telecommunications, publishing and public utilities.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Amendments to the KCC

Major amendments to the KCC were passed on 1 December 2015, and came into effect on 2 March 2016. The amendments were drafted with the explicit intention of invigorating the Korean M&A market by enabling the use of M&A structures previously unavailable in Korea.

The KCC amendments provide for triangular share swaps, reverse triangular mergers and triangular spin-off mergers. Under those structures, parent company shares can be offered as consideration. Specifically, parent company shares of the acquiring company are provided as consideration to target company shareholders in a triangular share swap or a reverse triangular merger, and parent company shares are provided to spun-off subsidiary company shareholders under a triangular spin-off merger. Those amendments are expected to facilitate more flexibility in M&A transactions by enabling cash-free mergers, as well as opening up new possibilities for structuring cross-border M&A transactions involving entities in overseas jurisdictions.

Further, the KCC amendments relax the threshold for small-scale share swaps (which can be approved by the board of directors, instead of the more onerous requirement of shareholder approval) from 5 per cent of total issued and outstanding shares to 10 per cent of total issued and outstanding shares.

Finally, the KCC amendments introduce the simplified business or asset transfer, where a transfer can be approved by a board of directors’ resolution if the counterparty to a transaction owns over 90 per cent of the transferring company’s shares.
ii Recent amendments to the Capital Markets Act

Amendments to the Capital Markets Act came into effect on 1 May 2018 to tighten the disclosure obligations for shareholding dilution. Before the amendments, if a listed company offered new shares other than by way of pro rata subscription by existing shareholders, entailing dilution of existing shareholders, an exemption from the usual requirement of two weeks’ prior notice under the KCC applied, which meant that most shareholders discovered the dilution after the fact. Under the amended Capital Markets Act, disclosure is required at least one week before the payment date in respect of the subscription price.

Before its expiration in 2018 due to the sunset clause in the Capital Markets Act, the Korea Securities Depository (KSD) was allowed to exercise the unused voting rights of the shares deposited in the KSD mirroring the actual votes exercised at the general shareholders’ meetings of listed companies. This shadow voting was allowed because minority shareholders usually did not attend general shareholders’ meetings, and it was a common occurrence that the quorum of 25 per cent of the issued and outstanding shares (required under the KCC) could not be satisfied. The difficulty in achieving a quorum is more serious in relation to the appointment of statutory auditors, as each shareholder’s voting right for the appointment of a statutory auditor is limited to 3 per cent, and even if the controlling shareholder holds more than 25 per cent of the shares, the quorum can only be satisfied if other minority shareholders exercise their rights to surpass the quorum threshold of 25 per cent. Yungjin Pharmaceuticals, a KRX-listed company, was actually unable to appoint its statutory auditor at its 2018 annual general shareholders’ meeting as only 9 per cent (out of minority holdings of 47.55 per cent) of its minority shareholders attended, and the quorum for appointing its statutory auditor could not be satisfied. Currently, the solutions being discussed for this issue are to introduce an electronic voting system for general shareholders’ meetings to facilitate minority shareholder participation, and to have companies more actively court minority shareholders to participate or grant proxies.

iii Recent amendments to the employment law, tax law and competition law

See Sections VII.i, VIII.i and IX.ii, respectively.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In 2017, foreign direct investment (FDI) into Korea reached an all-time high of US$229.4 billion (a 7.7 per cent increase from 2016), and FDI into Korea surpassed US$200 billion in each year during the three-year period from 2015 to 2017. However, in 2018, global economic uncertainty, in addition to soft economic conditions in certain countries that are major sources of inbound investment, led to a decrease in the number and value of inbound M&A deals, and while FDI figures for 2018 had not been compiled at the time of publication, FDI is also expected to show a decline.

Among the total FDI amount for 2017 above, which includes both M&A investments and follow-up investments by foreign investors in Korea, FDI by way of M&A was US$72.4 billion (a 15.4 per cent increase from 2016, on the basis of publicly filed information).

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4 In this context, FDI means the investment by foreign individuals or entities into Korean entities of more than 100 million won and representing 10% or more of the voting shares of the Korean entity.

As of June 2017 (half year basis), the major countries investing into Korea were as follows: 6

<table>
<thead>
<tr>
<th>Ranking</th>
<th>Country</th>
<th>Investment amount (US$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>United States</td>
<td>2,446</td>
</tr>
<tr>
<td>2</td>
<td>Singapore</td>
<td>1,181</td>
</tr>
<tr>
<td>3</td>
<td>Hong Kong</td>
<td>1,152</td>
</tr>
<tr>
<td>4</td>
<td>Japan</td>
<td>819</td>
</tr>
<tr>
<td>5</td>
<td>Philippines</td>
<td>505</td>
</tr>
<tr>
<td>6</td>
<td>China</td>
<td>479</td>
</tr>
<tr>
<td>7</td>
<td>Netherlands</td>
<td>431</td>
</tr>
<tr>
<td>8</td>
<td>United Kingdom</td>
<td>390</td>
</tr>
<tr>
<td>9</td>
<td>Germany</td>
<td>347</td>
</tr>
<tr>
<td>10</td>
<td>Ireland</td>
<td>323</td>
</tr>
</tbody>
</table>

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Significant transactions

Among others, notable significant transactions in the Korean M&A market announced in 2018 included the following.

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Industry</th>
<th>Deal amount (US$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hyundai Heavy Industries’ acquisition of Daewoo Shipbuilding &amp; Marine Engineering</td>
<td>Shipbuilding</td>
<td>1,834</td>
</tr>
<tr>
<td>SK Telecom’s acquisition of ADT Caps from Carlyle Group</td>
<td>Security</td>
<td>2,539</td>
</tr>
<tr>
<td>Shinhan Financial Group’s acquisition of Orange Life Insurance (former ING Life insurance)</td>
<td>Life insurance</td>
<td>1,957</td>
</tr>
<tr>
<td>Kolmar Korea’s acquisition of CJ HealthCare</td>
<td>Pharmaceutical</td>
<td>1,120</td>
</tr>
<tr>
<td>Acquisition of Magna International Inc’s global fluid pressure and controls by Hanon Systems</td>
<td>Auto parts manufacturing</td>
<td>1,181</td>
</tr>
<tr>
<td>Acquisition of Style Nanda by L’Oreal</td>
<td>Fashion</td>
<td>513</td>
</tr>
</tbody>
</table>

ii Key trends

One notable development in the Korean M&A market in 2017 and 2018 was the rapid growth in the participation of private equity fund (PEF) players, in comparison to more conservative activity by domestic conglomerates. Further, while PEFs in the Korean M&A market previously tended to focus on buy-outs to ensure short-term returns, PEFs are now starting to show interest in long-term investments in medium-sized firms, especially in consortium with strategic investors. Notable examples are the acquisition of Hyosung Packaging (a PET bottle company) by a Standard Chartered Private Equity consortium in partnership with Samyang Group and the acquisition of Tapex (a taping company) by an NH Investment & Securities consortium in partnership with Hansol Chemical.

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Another development is the increase in carve-out transactions, where the parent company spins off a subsidiary and sells a minority stake in the spun-off subsidiary to outside investors. Korean companies are utilising carve-out structures to achieve various goals, for example, to divest non-core business and focus on core businesses or to attract investments to certain particular business divisions, and it is expected that carve-out transactions will comprise a significant portion of the Korean M&A market in 2019. One recent example of a carve-out transaction was the sale of existing shares by Kakao Corp and the issuance of new shares by Kakao Mobility, which had been established by Kakao Corp by way of an in-kind contribution of its Kakao Taxi and other auto-related businesses to a consortium led by TPG. With the new capital raised from the consortium, Kakao Corp and Kakao Mobility strengthened their position to develop and launch new premium taxi app services.

Finally, inbound transactions in 2018 showed a volume decrease of 48 per cent compared to 2017, with an aggregate value of US$4.3 billion over 37 transactions. Notable inbound transactions in 2018 included Hillhouse Capital, Sequoia Capital and Singapore sovereign wealth fund GIC’s equity investment in Baedal Minjok, Korea’s leading food delivery service company (US$308 million).

### iii Hot industries
According to the KFTC’s 2018 M&A Review, in order to enhance the competitiveness of existing businesses as well as to build an engine for future growth, mega-sized M&A transactions in the subscription broadcasting services, video game, and shipbuilding industries are expected in 2019.

### VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

#### i Leveraged buyouts
Korean statutory law and court precedents prohibit certain forms of leveraged buyout (LBO) as illegal asset-stripping, and a clear-cut standard on whether a given financing structure is permissible for a given transaction structure has not been provided to date.

Based on recent court precedents, it is generally understood that LBO financing structures that directly utilise the target company’s assets as collateral are likely to be prohibited. However, a 2015 Korean Supreme Court judgment7 ruled that an LBO that involved establishing security on target company assets can be allowed considering, among other things, that:

- the acquiring company acquired 100 per cent of the target company, and as such no minority shareholders were harmed by the transaction;
- a critical portion of the funding for the transaction (approximately 43 per cent) was supplied by the acquirer;
- the acquiring company was not a paper company, but a listed company with substantive assets; and
- there was no substantive or procedural defect in the merger following the acquisition.

While this judgment does not seem to rule that LBO financing structures that utilise a target company’s assets as collateral are generally allowed, it can be seen that in certain cases such financing structures are permissible, depending on the entirety of the circumstances.

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7 Korean Supreme Court, 12 March 2015, 2012Do148 judgment.
On the other hand, indirect LBO financing in cases where the acquiring company (which borrowed the purchase price) is merged with the target company, or the target company provides funding to the acquiring vehicle by capital reduction, are likely allowed, assuming that the necessary corporate approvals and procedures are obtained and observed. Overall, LBO financing is being used more often in the Korean M&A market compared with previous years.

ii Total return swaps
A total return swap (TRS) is an instrument under which the total return payer (who will acquire a partial stake in the target company) agrees to pay the total return recipient the increase in the value of the stake, dividends, or both, derived from the stake; and in exchange, the total return recipient agrees to pay a fixed fee to the total return payer, any decrease in the value of the stake, or both.

Although it is arguable whether a TRS constitutes a true sale, M&A transactions utilising the TRS are being seen more commonly in the Korean M&A market. For the acquisition of KT Rental in 2015, Lotte Group financed approximately US$290 million (out of a total purchase price of US$1.1 billion) using the TRS structure.

VII EMPLOYMENT LAW
i Recent amendments to the employment law
Nearly four years after revisions to the law were first proposed, the Korean National Assembly passed a bill on 28 February 2018 to amend the Labour Standards Act (LSA) to reduce Korea’s maximum weekly working hours. The law reduces the maximum weekly working hours from 68 hours per week to 52. The law became effective on 1 July 2018. It currently applies to large companies, and will be rolled out in stages to smaller companies. Employers who fail to comply with this new law will be subject to criminal penalties of imprisonment for up to two years or a fine of up to 20 million won.

Reviewing the working conditions of target companies for compliance with the mandatory working hour regulations has become a routine part of due diligence.

ii Recent court decision
In Korea, the Act on the Protection of Dispatched Workers (Dispatched Workers Act) regulates the use of employees of another company by way of worker dispatch. Under the Dispatched Workers Act, worker dispatch refers to a system in which a dispatching company, while maintaining the employment relationship with its employee, causes its employee to work for another company under the supervision and direction of the receiving company in accordance with a dispatch agreement between the two companies.

Outsourcing is similar to worker dispatch in that the receiving company uses the employees of the outsourcing company for the work of the receiving company. However, there is a general distinction between outsourcing of work, which is not subject to the Dispatched Workers Act, and worker dispatch regulated under the Dispatched Workers Act, based on whether the employee is supervised or controlled by his or her own employer or the receiving company. If the employee is supervised or controlled directly by the receiving company for the performance of his or her work, he or she will be regarded as a dispatched worker under the Dispatched Workers Act.
In September 2017, as a result of a labour inspection conducted by the Ministry of Employment and Labour (MOEL), MOEL discovered that Paris Baguette had been retaining bakers at its franchise stores via illegal worker dispatch, and ordered Paris Baguette to directly hire 5,378 bakers. MOEL regarded Paris Baguette as a receiving company under the Dispatched Workers Act in relation to the bakers principally on the grounds that, among other things, Paris Baguette established and put into place uniform criteria for general management of personnel matters, including recruitment, promotion, evaluation and wage levels of bakers; and Paris Baguette’s quality manager managed the attendance time of bakers and generally supervised and directed the bakers in their duties. Moving forward, there is a strong possibility that MOEL will use the criteria applied in its determination of the Paris Baguette case to assess alleged cases of illegal worker dispatch in transaction structures similar to the above case.

In this regard, based on the foregoing, when entering into M&A transactions, buyers will need to confirm whether target companies are in compliance with the Dispatched Workers Act to avoid being ordered to hire any unexpected additional employees on a permanent basis after closing a transaction.

VIII TAX LAW

i Recent amendments to the tax law

The key features of the recent amendments to tax laws are as follows.

Relief from VAT for business transfers

Under the current law, a comprehensive business transfer is not subject to value-added tax (VAT). Where only selected assets or liabilities are transferred, the transaction is classified as an asset transfer and the transferor is required to issue valid VAT invoices and file a VAT return. However, from a practical standpoint, it is actually difficult for taxpayers to determine whether a transaction is a comprehensive business transfer or an asset transfer. There was a risk that input VAT would not be refundable if a transaction was treated by the parties as an asset transfer at the initial stage of the transaction and later was determined to be a comprehensive business transfer by tax authorities. Therefore, taxpayers had to obtain a ruling from the tax authorities to gain certainty as to the type of transaction. According to the amended tax laws, which became effective on 1 January 2014, a transferee is allowed to credit the input VAT on a proxy basis when VAT is paid to the relevant tax authorities by the 10th day of the following month after completion of the transaction.

Addition of employment succession requirements to satisfy tax-free merger and demerger conditions

Under the former law, a merger or demerger would be treated as tax-free if certain requirements, such as business purpose, continuity of interest and continuity of business, were met. Amendments to the tax law effective on 19 December 2017 impose the continuity of employment requirement as an additional condition for the tax-free treatment of a merger or demerger. Under the new requirement, 80 per cent or more of the employees of the transferred business must continue to be employed by the surviving entity until the end of the fiscal year during which a merger or demerger is registered.

However, a tax-free merger or demerger may become taxable upon the occurrence of certain trigger events within three years from the end of the fiscal year during which the
merger or demerger is registered. The trigger events include discontinuity of interest and discontinuity of business. The revised tax law added discontinuity of employment as a new trigger event. To maintain a tax-free merger, the total number of employees of the surviving entity must be 80 per cent or more of the combined total number of employees of both entities. Similarly, to maintain a tax-free demerger, the total number of the spun-off entity’s employees must be 80 per cent or more of the total number of those of the pre-demergent spun-off business.

Relief from tax-free in-kind contribution requirements
Previously, corporate income tax on capital gains arising from qualified in-kind contributions was deferred if all of the following conditions were met:

a the investing company is engaged in the business for five years or more;
b the investing company owns 80 per cent or more of the shares in the invested company, and continues to hold such shares until the end of the year in which the in-kind contribution is made;
c the invested company carries on the transferred business until the year end; and
d a separate and independent business division is transferred to the invested company.

It was not regarded as a transfer of a separate and independent business division if the investing company contributed only certain holding stocks and related assets and liabilities to the invested company.

The tax law as amended on 19 December 2017 abolished the fourth requirement with a view to facilitating corporate restructuring. On or after 1 January 2018, the tax-free in-kind contribution requirements will be met even if a investing company only contributes stocks, if the other three requirements are met.

Expansion of tax-free merger incentives
Under the former law, a vertical merger between a parent company and its 100 per cent-owned subsidiary was considered a tax-free merger without having to satisfy any further conditions. According to the tax law as amended on 19 December 2017, in addition, a horizontal merger between brother–sister entities that are 100 per cent held by the same parent company will be eligible for tax-free treatment without the need to satisfy any further conditions on or after 1 January 2018.

Capital gains tax on the transfer of small and medium-sized enterprise shares by major shareholders
Capital gains tax on the transfer of shares in small and medium-sized enterprises (SMEs) was previously imposed at 10 per cent, irrespective of the size of the shareholder’s stake. The tax law as revised on 15 December 2015 increases the capital gains tax rate on the transfer of SME shares owned by major shareholders from 10 to 20 per cent on or after 1 January 2016.

The original 2018 tax reform proposal included an increase in the tax rate from 20 to 25 per cent on the tax base exceeding 300 million won for capital gains earned by a large shareholder, which would be effective for share transfers from 1 January 2018. Under the bill approved in 2018, the application of the increased tax rate will be postponed until 1 January 2020 for the transfer of shares in SMEs. This trend of increase in the capital gains tax rate on the transfer of SME shares has led to an increase in M&A activity among private companies since 2018.
Recent court decision

In a recent case with respect to a share transfer, the Supreme Court decided in a recent case that cash bonus compensation (an M&A bonus) to employees of an acquired company should be an expense borne by the acquired company rather than the buyer of the acquired company. The acquired company paid an M&A bonus to its employees and deducted the M&A bonus in its corporate income tax return. However, the tax authorities denied deductibility of the M&A bonus on the basis of their assertion that the M&A bonus should have been an expense borne by the buyer of the acquired company’s shares as opposed to the acquired company itself.

The Supreme Court held that there was a reasonable basis for the acquired company to pay the M&A bonus considering the fact that the M&A bonus was paid to employees who served the acquired company, that the amount of the M&A bonus was reasonably decided in consideration of the operating income of the year, and that it was not out of the ordinary course of business for the acquired company to pay compensation to its employees to prevent or terminate strikes.

IX   COMPETITION LAW

i   Overview

According to the KFTC, companies notified the KFTC of 702 reportable transactions during 2018, which is a slight increase over the 668 transactions notified in 2017. The KFTC challenged and conditionally approved only two transactions in efforts to protect competition in industrial sectors including telecommunications (Qualcomm/NXP) and industrial gases (Linde/Praxair).

ii   Recent amendments to the competition law

During 2017, there were a couple of notable regulatory changes in the context of Korea’s merger control: an increase in the jurisdictional thresholds, and a curtailment of the review period for a transaction that is judged under a voluntary prior consultation as one that is unlikely to raise competitive concern. Additionally, in 2019, the KFTC has revised its merger filing guidelines to take into account information assets (including big data) and specialised merger review standards for digital economy companies (in which the criteria applied by the KFTC for the purpose of defining the relevant market are tailored for such companies).

The KFTC announced in October 2017 increased jurisdictional thresholds for merger notification under the MRFTA. Under the previous merger notification regime, a transaction was required to be reported if a party to the transaction incurred global revenue (or possessed global assets) of at least 200 billion won in the preceding fiscal year and the other party to the transaction had global revenue (or possessed global assets) of at least 20 billion won. These threshold amounts were increased to 300 billion won and 30 billion won respectively and came into force on 19 October 2017. Transactions entered into after 19 October 2017 are subject to the new thresholds. On the other hand, the domestic revenue threshold for foreign-to-foreign mergers, which refer to M&A involving non-Korean companies, has increased as well. For a foreign-to-foreign merger to be reportable, a foreign company involved in the foreign-to-foreign merger is required to have generated sales in or into Korea of at least 30 billion won in the preceding fiscal year in addition to satisfaction of the global...
revenue and asset thresholds noted above. Prior to the amendment to the MRFTA, the figure was 20 billion won. According to the KFTC’s 2017 M&A Review, the increased thresholds would likely reduce the number of merger notifications to the KFTC by 50 cases per year.

The other noteworthy change to Korea’s merger control law is an extension of the scope of the simplified review procedure. The benefits of the simplified review procedure, a short-form notification and a shorter waiting period (15 calendar days), have been extended to transactions that are evaluated under a voluntary prior consultation as competitively neutral transactions or transactions where procompetitive effects outweigh anticompetitive effects. The MRFTA allows the parties contemplating a potentially reportable transaction to request the KFTC’s preliminary or prior review even before signing a preliminary agreement in respect of the transaction. This voluntary prior consultation is often used to prevent unnecessary delay in merger review after a formal notification is submitted later following execution of a definitive agreement. In practice, if no competitive concern is found in the voluntary prior consultation, the proposed transaction usually passes the formal merger review without difficulty unless substantial changes are made to the deal structure that was notified to the KFTC in the voluntary prior consultation. However, in the past, the notifying party or parties still had to file a full-length notification for the subsequent formal merger review, which is a lengthy form that requires a significant amount of corporate and market data, and were obliged to wait 30 calendar days until the receipt of the KFTC’s final approval (although early approval was sometimes granted). Thus, the amendment to the MRFTA has established a consistent procedural approach to transactions that are not likely to raise competitive concerns.

iii Contemplated changes in the competition law

Apart from changes to the jurisdictional thresholds, the KTFC is contemplating an additional notification threshold for unicorn deals. The current approach is relatively straightforward but may not cover transactions involving highly valuable start-ups, which at the time of a transaction may not have significant revenues or assets meeting the thresholds, but whose deal valuation is relatively high in anticipation of its potential importance in the markets (unicorn start-ups). The United States, Austria, and Germany are a few countries that have introduced transaction-value-based thresholds. If adopted, the size-of-transaction test would intensify competition law enforcement in the era of the digital economy. However, this proposal is still under consideration and open for further discussion.

In addition, the KFTC appears to be considering the role of big data in merger review. On 30 January 2018, the KFTC responded in its testimony to the Congressional Special Committee for the Fourth Industrial Revolution that it will be mindful of likely adverse impacts on innovation in connection with its merger review of transactions in the big data-driven market. No indication of drastic changes to the analytical approach to competition issues regarding big data has been observed, but the KFTC has clearly voiced in its testimony that a company may be found to have dominant market power due to its ownership of and control over valuable data in spite of a low market share. Much has been said about big data-related theories of harm. The KFTC seems to be concerned that control over big data can create barriers to entry in particular in a situation where a company holds a unique dataset that cannot be replicated by its competitors without incurring substantial time and cost. Thus, the KFTC is likely to actively monitor big data’s impact on fostering competition in relevant markets.
X OUTLOOK

In 2019, considering the relatively moderate growth of the Korean economy (2.6 per cent real GDP growth forecast\(^8\)) and the global economy (3.3 per cent GDP growth forecast\(^9\)), it is anticipated that the Korean domestic M&A market, as well as inbound and outbound M&A activity, will be stable throughout 2019. However, continued geopolitical uncertainties, potential global trade wars and increased government regulation may reduce M&A activity.

For the domestic M&A market, it is expected that PEFs will continue their active participation in the market, fuelled by plentiful liquidity, and carve-out transactions by companies seeking to strengthen their core business areas will increase. For the inbound and outbound markets, a general global recovery is expected to contribute to increased M&A activity, but considering the Korean economy’s global connectedness, the Korean M&A market will be highly exposed to global economic and regulatory risks.

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\(^8\) Bank of Korea forecast, January 2019.

\(^9\) IMF World Economic Outlook, April 2019. Projected at 3.7 per cent in January 2018, reduced to 3.5 per cent in January 2019, then adjusted again in April 2019.
Chapter 29

LUXEMBOURG

Philippe Hoss and Thierry Kauffman

I OVERVIEW OF M&A ACTIVITY

M&A activity remained relatively strong in Luxembourg in 2018, with less activity in the first half of 2019 due to a global slowdown caused by the remaining uncertainties resulting from Britain’s decision to leave the European Union and ongoing trade wars between the United States and several of its trading partners, including China and the European Union. Some of the reasons for Luxembourg’s continuing attractiveness are its regulatory and legislative framework, its legal and political stability and its domestic market, in particular its fund industry and financial sector.

Luxembourg remains the largest investment funds centre in Europe, and the second-largest in the world behind the United States. At the close of April 2019, the net assets under management in Luxembourg amounted to €4.405 billion. Hence, the investment funds industry continues to play a major role in stabilising the Luxembourg market. Luxembourg continues to be ideally placed to implement tax-efficient M&A transactions and hence to be a key platform for M&A and private equity activity. One reason for this is that the relevant legislation continues to be adapted and modernised to be as attractive and flexible as possible: this includes new forms of companies, namely the special limited partnership and the simplified stock company, which offer additional solutions for economic actors, including those of the private equity world. Funding instruments and methods created and used by practitioners over past decades, such as the use of tracking shares or the issuance of hybrid instruments, have been confirmed by the legislator and codified in the law of 10 August 2016 amending the law of 10 August 1915 on commercial companies (1915 Law), hence creating additional legal certainty.

Luxembourg remains one of the leading European hubs for vehicles investing directly or indirectly in European real estate. It is also worth noting that a lot of actions are being undertaken by the government to make Luxembourg a leading hub in the areas of information and communication technology, fintech and space technology.

In general, Asian dealmakers and investors continue to set their sights on European targets in a bid to reduce reliance on their domestic market. North American investors on the other hand may feel more inclined to stay at home, as there may be new opportunities in a less regulated and lower tax US environment as promised by the US President. This tendency might be accentuated by the ongoing trade wars.

1 Philippe Hoss and Thierry Kauffman are partners at Elvinger Hoss Prussen.
2 CSSF press release 19/20 of 3 July 2019.
With a number of promising drivers and deals in place, we anticipate a relatively active M&A market in the second half of 2019, although not as exceptional as 2018. Low costs of funding, the continued desire to expand geographic reach and innovation capabilities speak in favour of an active year. On the other side, key global elections, heightened regulatory scrutiny, in particular of Chinese investors, and speculations around Brexit may result in a slowdown in M&A activities. Despite the strong concurrent bids from other leading European hubs, investors and companies fleeing Brexit seem to find Luxembourg an adequate alternative, and particularly the insurance and asset management sectors, which noticed the establishment of many newcomers in the Luxembourg market.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Luxembourg Civil Code, notably the provisions governing contracts, and the Luxembourg Commercial Code provide the statutory framework and form the legal basis for the purchase and sale of corporate entities in Luxembourg.

Statutory mergers, including cross-border mergers with EU or non-EU entities, demergers, splits and spin-offs, as well as contributions of branches of activities, or of part or all of the assets and liabilities of Luxembourg undertakings, are mainly governed by the 1915 Law, which implemented the EU Cross-Border Mergers Directive.3

In addition, the law of 5 August 2005 on collateral agreements, which provides legal certainty to lenders, is commonly used in M&A transactions irrespective of the location of the target to secure financing. In that context, it should be noted that Luxembourg continues to offer a legal environment more favourable to lenders than any other European jurisdiction.

In the case of an offer for the acquisition of a target whose shares are admitted to trading on a regulated market in one or more Member States, the law of 19 May 2006 transposing the Takeover Law4 will apply in cases where the target is a Luxembourg company or where its shares are admitted to trading on the regulated market of the Luxembourg Stock Exchange (LSE). If the target is a Luxembourg company and its shares are listed on the regulated market of the LSE, all aspects of the offer will be governed by the Takeover Law (even if the shares are additionally listed on other regulated markets in the EU or the EEA). If the target is a Luxembourg company but its shares are listed only on a regulated market in the EU or the EEA outside of Luxembourg, a split jurisdiction regime will apply, with the law of the listing jurisdiction being applicable for the offer, and Luxembourg law being applicable for corporate law matters, the legality of measures by the target that could defeat the offer as well as information to be provided to employees of the target. With respect to Luxembourg companies, Luxembourg law will also be competent to determine the control threshold, the crossing of which may trigger the obligation to make a mandatory offer, and the exemptions from such obligation. Luxembourg law will also provide for the sell-out and squeeze-out rules following a successful offer.

If a bidder does not achieve the necessary threshold for a squeeze-out as a result of an offer under the Takeover Law, but reaches that threshold at a later stage, such bidder may be in a position to squeeze-out minority shareholders under the law of 21 July 2012 on the mandatory squeeze-out and sell-out of securities of companies currently admitted or

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3 Directive 2005/56/EC.
4 Directive 2004/25/EC.
previously admitted to dealing on a regulated market in the European Union or having been offered to the public. Conversely, minority shareholders may have the right under that law to cause the majority shareholder to purchase their shares.

Public offerings on the Luxembourg territory and admissions to trading on the Luxembourg regulated market of securities are governed by the EU Prospectus Regulation\(^5\) and by the Luxembourg prospectus law of 16 July 2019 (Prospectus Law), and the Financial Sector Supervisory Commission (CSSF) is the supervisory and regulatory authority competent to oversee these operations.

For companies whose securities are admitted to trading on the regulated market of the LSE, and whose home Member State will be Luxembourg, a certain number of additional Luxembourg laws (mainly deriving from the implementation of relevant European directives) may apply, in particular the Luxembourg law of 11 January 2008, as amended, implementing the Transparency Directive (Transparency Law)\(^6\) and the Luxembourg law of 26 December 2016 on market abuse (Market Abuse Law) implementing the Market Abuse Directive II.\(^7\)

The law of 24 May 2011, as amended, on the exercise of certain rights of shareholders in general meetings of listed companies will also apply to Luxembourg companies whose shares are admitted to trading on a regulated market in the EU (Shareholder Rights Law).

The Takeover Law, the Prospectus Law, the Transparency Law and the Shareholder Rights Law, and those provisions of the Prospectus Law supplementing the Prospectus Regulation, are not applicable to Luxembourg or foreign companies whose shares or other securities are admitted to trading on the Euro multilateral trading facility (MTF) market of the LSE.

The Market Abuse Regulation (MAR),\(^8\) relevant implementing and delegated regulations of the European Commission and the Market Abuse Law will apply with respect to companies whose securities are admitted to trading on the regulated market or the Euro MTF of the LSE.

Moreover, there may be specific legislation to be considered depending on the sector involved in the transaction (e.g., credit institutions, insurance or reinsurance companies, companies operating in the telecommunication business, MiFID firms) and, in particular, prior regulatory approvals or notifications will then be necessary.

Additional regulations will also apply if a purchase, sale or merger of a Luxembourg undertaking involves the transfer of staff.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Modernisation of Luxembourg company law


Although the New Company Law brings a lot of significant changes, the contractual freedom of shareholders remains the key feature. The New Company Law mainly aims

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\(^5\) Regulation (EU) No. 2017/1129/

\(^6\) Directive 2004/109/EC.

\(^7\) Directive 2014/57/EU.

\(^8\) Regulation No. 596/2014/EU.
at integrating some innovations already existing in foreign jurisdictions to offer new legal instruments to investors, to harmonise rules applicable to the different forms of companies and to formally recognise the validity of legal solutions previously developed by Luxembourg practitioners.

The New Company Law contains new opportunities but also certain additional constraints. As a result, the impact of such legislation should be carefully analysed not only for new entities but also for existing structures.

Below is a summary of some of the key changes resulting from the New Company Law. Some of these may require specific actions, including appropriate provisions to be inserted in articles of association or shareholders’ agreements:

a Key changes applying to a public company limited by shares (SA), a partnership limited by shares (SCA) and a private limited liability company (Sàrl):

• agreements governing voting rights are now formally recognised (with certain limits);
• the New Company Law now contains a list of cases where a decision of shareholders or bondholders may be declared void;
• a shareholder of an SA, Sàrl or SCA may validly undertake not to exercise all or part of his, her or its voting rights either temporarily or permanently;
• management may, if so authorised by the articles of association, suspend the voting rights of a shareholder that is in default of its obligations under the articles of association or a shareholders’ agreement or the relevant shareholder’s undertakings;
• the change of nationality of a Luxembourg company will no longer require a unanimous decision by the shareholders (and bondholders); and
• recognition of provisions where current or future shareholders organise the transfer or acquisition of shares.

b Key changes pertaining only to a private limited liability company:

• the majority requirement applicable to the transfer of shares in a Sàrl to a non-shareholder may be reduced from 75 to 50 per cent of the share capital in the articles of association. If the proposed transfer of shares is not approved, the remaining shareholders may propose alternatives within three months of this refusal to the leaving shareholder, allowing it to transfer its shares, and if no solution has been found, the leaving shareholder is authorised to transfer its shares to the third party initially identified;
• the foregoing is without prejudice to the pre-emption and tag-along rights agreed among the parties;
• abolishment of the double majority requirement (majority of shareholders representing 75 per cent of the shares) for extraordinary shareholder decisions. A 75 per cent majority of the shares is now sufficient;
• the possibility for managers to pay an interim dividend;
• the possibility to issue redeemable shares; and
• the possibility to provide for an authorised share capital.

c Key changes pertaining only to a public company limited by shares and a limited partnership by shares:

• the validity of lock up clauses in the articles of association is formally recognised, with the consequence that any transfer made in breach of such clauses is expressly null and void;
prior consent clauses and pre-emption clauses relating to shares provided for in
the articles of association are formally declared as being valid as long as such
clauses do not prevent the leaving shareholder from transferring its shares for
more than 12 months;
the issuance of non-voting shares is no longer limited to 50 per cent of the share
capital, and non-voting shares do not necessarily need to receive a preferred
dividend; and
an auditor’s in kind report is no longer required for the contribution to a company
consisting in a claim against or receivable issued by the same company (under
certain conditions).

On 15 December 2017, the Grand-Ducal Regulation (Regulation) coordinating the 1915
Law was published in the Luxembourg official gazette and applies from 19 December 2017.
The Regulation does not further amend the 1915 Law, but it significantly reorganises
the numbering of its articles and sections. From 19 December 2017, all references to the
1915 Law shall take into account the new numbering. The constitutional documents of
Luxembourg companies in force before 19 December 2017 do not need to be amended, and
reference to an old number will automatically be deemed to refer to the corresponding new
number of an article or a section.

i  Creation of a register of beneficial owners
The 4th EU AML Directive,9 as amended by the 5th EU AML Directive,10 requires each
Member State of the EU to, inter alia, establish a register of beneficial owners (RBO) in
respect of corporate and other legal entities incorporated or formed within its territory.
The Luxembourg Law of 13 January 2019 creating a register of beneficial owners (RBO
Law) entered into force on 1 March 2019. Within six months from such date (i.e., before the
end of August 2019) all in-scope Luxembourg entities (e.g., commercial companies, special
limited partnerships and investment funds, including common funds) will have to comply
with the provisions of the RBO Law.
In particular, Luxembourg entities will be required to provide the RBO with relevant
information on their ultimate beneficial owners (UBOs) as defined by the AML Law.11
All UBOs are concerned, irrespective of whether they are Luxembourg nationals or
residents or not. As an exception, companies listed on EU-regulated markets or on regulated
markets established in a non-EU jurisdiction that has similar transparency rules shall merely
provide the RBO with the name of the relevant regulated market.

ii  Amendments to the Shareholder Rights Law
The Shareholder Rights Law will be amended in 2019 pursuant to bill of law 7402.12
The Shareholder Rights Law, as it will be amended by bill of law 7402, will require
intermediaries (custody banks and other professionals providing securities safe-keeping and

11 Luxembourg Law of 12 November 2004 on the fight against money laundering and terrorist financing, as
amended.
12 Bill of law 7402 on the exercise of certain rights by shareholders in general meetings of listed companies
has, at the time of writing, been voted but not yet published in the Luxembourg legal gazette.
securities accounts services) to communicate information regarding shareholders’ identities on request and without delay to listed issuers so that they may identify their shareholders. These requirements apply to all intermediaries that might be part of a holding chain, including non-EU intermediaries. Intermediaries must also facilitate the exercise of their rights by shareholders, in particular the right to participate and vote at general meetings.

The law will provide for increased transparency on subjects such as the remuneration policy and related party transactions of listed issuers and as regards the shareholder engagement policy of institutional investors and asset managers, the investment strategy of institutional investors and certain information regarding the arrangements with the asset manager appointed by them. Asset managers will need to report to their institutional investor clients how their investment strategy and the implementation thereof complies with their mandate, and on certain other matters. There will also be certain disclosure obligations on proxy advisers with respect to their research, advice and voting recommendations.

iii Parliamentary bills of law not yet adopted

Current ongoing legislative activities relevant to M&A activity are quite limited, with the most important being bill of law 6539 regarding the preservation of enterprises and aiming to modernise the legal framework for insolvency law and assimilated procedures.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Luxembourg is the second-largest investment fund centre in the world after the United States, the premier captive reinsurance market in the European Union and the premier private banking centre in the eurozone. The financial sector is the largest contributor to the Luxembourg economy.

Moreover, Brexit has had a positive impact on the Luxembourg insurance sector with the establishment in Luxembourg of about 10 insurance companies such as AIG, Liberty Mutual, Sompo International and Britannia.

A number of asset management and private equity firms have also pledged to move activities to Luxembourg, including Fidelity, M&G, Standard Life Aberdeen, Columbia Threadneedle, Blackstone, T Rowe Price and Wells Fargo.

Luxembourg’s success is founded on its social and political stability, and on a modern, efficient, flexible and business-friendly legal and regulatory framework that is continuously updated. Banks, insurance companies, investment fund promoters and specialist service providers from all over the world have been attracted to Luxembourg. M&A transactions are not subject to any particular restrictions.

A large part of M&A activity in Luxembourg consists of the involvement of Luxembourg vehicles in the acquisition of foreign targets or assets. In particular, the number of Luxembourg holding structures through which real estate is held has continued to increase in past years.

Luxembourg’s neighbours, France, Belgium and Germany, are considered to be the main players in the Luxembourg market, and they have a noticeable presence in Luxembourg through their financial institutions. While other European countries have a strong presence, the establishment of some of the main international financial institutions and banks from non-European countries, in particular from China, over the course of the past few years
is notable. Indeed, several Chinese banks have incorporated their European headquarters in Luxembourg, and Luxembourg has become the leading European jurisdiction for international renminbi business.

Luxembourg is a location that many foreign investors and international groups consider, particularly for the establishment of investment funds or the structuring of cross-border acquisitions and intragroup structuring, mainly due to Luxembourg’s stability, its pragmatism and flexibility, and its openness to new businesses.

One of the advantages of Luxembourg’s legislation is that when implementing the provisions of the EU Cross-Board Mergers Directive in the 1915 Law, Luxembourg law covers not only national mergers and mergers between Luxembourg companies and EU companies of sociétés anonymes, but also mergers between Luxembourg companies and non-EU companies of any legal form, contrary to the legislation of most other Member States.

It is further possible in Luxembourg to express the share capital of a Luxembourg undertaking in a currency other than the euro or to have the legal documentation directly drawn up in English, with the exception that some documents (i.e., notarial deeds) must be followed by a French or German translation.

As further set forth above, the law of 5 August 2005 on collateral agreements, as amended, is commonly used in M&A transactions involving a Luxembourg entity to secure financing and continues to offer a legal environment more favourable to lenders than other European jurisdictions.

In addition, the migration of companies to Luxembourg with the continuation of their legal personality and without the need for reincorporation has always been recognised and is a common occurrence.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In November 2018, Luxembourg-based ArcelorMittal completed the acquisition of Italian steel producer Ilva in a deal worth €1.8 billion. The main assets of Ilva notably include its steel plant in Taranto, Italy, which is Europe’s largest single-site integrated flat carbon steel plant. Both companies are significant producers in Europe of hot rolled, cold rolled and galvanised flat carbon steel. To obtain the approval of the European Commission for the deal, ArcelorMittal was required to sell a large package of steel plant assets, including integrated steelworks in Romania and the Czech Republic, as well as finishing plants in Italy, Belgium, Luxembourg and North Macedonia, all of which were sold to London industrial and metals company Liberty House.

Luxembourg remains heavily involved in major international deals structured through Luxembourg. Hence, assistance on Luxembourg law aspects was required in, inter alia, the following major deals:

a the investment of Technology Crossover Ventures and CPPIB through a Luxembourg joint venture company in SportRadar AG, which provides sports-related live data and digital content services, for €2.1 billion;
b the acquisition by Foncière des Murs of 14 four and five-star hotels in the UK for £858 million from American investment firm Starwood Capital;
c the acquisition by Silver Lake, the global leader in technology investing, of the property platform ZPG Plc for US$3 billion;
the cross-border merger of Nets and Concardis Group to form a leading European payment player, as Nets was a market leader in the Nordic payments industry and Concardis a leading merchant payment service provider in the DACH region;

the sale by CVC Capital Partners of Belgian food group Continental Foods to Agrofim;

the sale of a 40 per cent stake in Belron, a leader in glass repair and replacement, to funds managed by Clayton Dubilier & Rice;

the acquisition by China Southern Power Grid of a stake in Encevo, a leading utility company in Luxembourg; and

the sale by residential real estate specialist BGP Investment Sàrl of all its real estate assets (approximately 16,000 residential and commercial units) to certain funds belonging to the ZBI Group.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

In addition to financing by cash resources, Luxembourg law and existing practice in Luxembourg provide for a large range of financing possibilities and instruments. It is possible to gain financing, inter alia, through an issue of shares, securities and other financial instruments carrying specific financial or voting rights such as preferred dividend rights, tracking securities, subordinated loans or securities, securities with arrangements ensuring multiple voting rights, convertible instruments, securities or loans with profit-participating elements.

On the equity side, we see contributions to a company’s equity account with or without the issue of shares by the company to be financed. In the latter case, the contribution is made to the freely distributable account (account 115) of the company, which is termed a ‘contribution to equity capital without issue of shares (capital contribution)’ pursuant to the Grand Ducal Decree dated 10 June 2009 on the presentation and content of a standard chart of accounts, this being a sub-account of the share premium account of a company. Alphabet shares, tracking shares and shares with differing par values are also possible, and are now recognised by the New Company Law.

On the debt side, entities are financed through loans that may be interest-bearing, profit-participating, convertible or tracking. However, transfer pricing rules must be complied with, and payments must be at arm’s length.

More complex and hybrid instruments also exist, such as preferred equity certificates (which can be interest free, tracking, convertible, etc.), notes, and bonds that can be issued by an entity in addition to shares and that are governed mainly by their contractual terms. It remains to be seen to what extent these hybrid instruments will continue to be used under ATAD 213 (which is further discussed in Section VIII).

The New Company Law has introduced a great deal of flexibility or has confirmed the flexibility of previously existing techniques: tracking shares are now formally recognised, the public or private issuance of bonds is now possible for all types of entities vested with legal personality, shares of a société anonyme can be issued below par value under certain conditions and shares can be issued with different nominal values.

Third-party financing usually takes the form of senior or mezzanine loans (whether syndicated or not). That said, alternative lenders are becoming more attractive in the debt financing market given that they often offer more flexibility than traditional bank lenders.

For a number of reasons (including the low minimum share capital, less regulation by the 1915 Law and its closed character), the private limited liability company is the preferred corporate vehicle for Luxembourg-structured acquisitions. For more complex structures, the limited partnership by shares may be interesting in particular for an initiator who wants to retain total control of its management. Some additional company types have become available over the past few years such as the special limited partnership, the simplified private limited liability company and the simplified stock company. The special limited partnership regime is inspired by the UK and US common law concept of a limited partnership. It provides considerable flexibility and offers additional onshore structuring solutions. Investors have demonstrated significant interest in these partnerships, as evidenced by the high number of incorporation of this company form over the past few years. The simplified stock company available in Luxembourg since the New Company Law is a company inspired by French law that has seen great success in France, and has begun to be used in Luxembourg as an alternative to the private limited liability company.

VII EMPLOYMENT LAW

Where a merger or an acquisition results in a transfer of an undertaking based on the territory of the Grand-Duchy of Luxembourg defined as a ‘transfer of an economic entity which retains its identity, meaning an organised grouping of resources which has the objective of pursuing an economic activity, whether or not that activity is central or ancillary’, Articles L127-1 and following of the Luxembourg Labour Code apply.

As a consequence, the rights and obligations of the transferor arising from employment contracts or existing employment relationships on the date of the transfer shall, by virtue of the law, be transferred to the transferee. The transferee is obliged to maintain all the essential elements of the employment contracts of the transferred employees.

Transferors and transferees shall be jointly and severally liable in respect of obligations that arose before the date of a transfer from an employment contract or an employment relationship existing on the date of the transfer.

The transfer of an undertaking shall not in itself constitute a valid ground for dismissal for the transferor or the transferee. Dismissals on the basis of real and serious grounds linked to an employee’s behaviour or on the basis of economic reasons not linked to the transfer remain possible. However, additional restrictions with respect to the termination of employment contracts following a transfer of an undertaking may be foreseen in collective bargaining agreements, such as the collective bargaining agreements applicable in the banking and insurance sector. The collective bargaining agreement of the banking sector prohibits terminations based on economic reasons for a period of two years following a transfer unless expressly agreed on by staff representatives. The collective bargaining agreement for the insurance sector does not provide for such exception.

Following a transfer, the transferee is furthermore obliged to maintain the provisions of a collective bargaining agreement that had been applicable to the transferor. Transferred employees will continue to benefit from the provisions of the collective bargaining agreement until its termination or expiry, or until the effective date of its replacement. However, pursuant to recent Luxembourg case law, in cases where a clause of a transferred employment contract
Luxembourg

refers to the application of a collective bargaining agreement, the provisions of such collective bargaining agreement shall continue to apply to the transferee even after the termination or expiry of the collective bargaining agreement in force the day of the transfer or the entry into force of its replacement. If so, the application of the collective bargaining agreement can be ended either by mutual consent or by a unilateral decision of the employer, provided a specific procedure is followed.

In the context of the transfer of an undertaking, the transferor must inform the transferee in due time about all rights and obligations transferred to the extent that these rights and obligations are known by the transferor at the time of the transfer. The transferor and the transferee shall furthermore inform in due time prior to the effective date of the transfer staff representatives or, in the absence of staff representatives, the employees concerned in the transfer regarding the date and the reasons of the transfer, as well as the legal, economic and social implications for the employees and any measures envisaged towards the employees. Finally, should the transferor or the transferee envisage taking measures involving the employees due to the transfer, their respective staff delegations must be consulted on those measures in due time with a view to reaching an agreement. The respective staff delegates of the transferor and the transferee shall also be informed and consulted in advance about all decisions that are likely to entail important modifications in the work organisation or in employment contracts, and the respective staff delegates shall be informed about and consulted on any economic or financial decision that may have a substantial impact on the structure of the undertaking or on the level of employment in undertakings counting at least 150 employees. This applies in particular in the case of a transfer of undertaking. As regards cross-border mergers, the law of 3 June 2016 amending, inter alia, Article L.426-14 of the Labour Code guarantees to employees that benefitted before the merger from a more favourable employee participation system than the one foreseen in Luxembourg the maintenance of their participation in such system.

VIII TAX LAW

i Statutory framework

In general, Luxembourg corporate taxpayers may be subject to corporate income tax (CIT) at a rate of 18 per cent, on which a 7 per cent solidarity surcharge is added, leading to an effective corporate income tax rate of 19.26 per cent, plus municipal business tax (MBT), which varies from one municipality to another.14

Moreover, corporations are generally subject to an annual net worth tax (NWT), levied at a rate of 0.5 per cent on their unitary value (i.e., taxable assets minus liabilities financing such taxable assets) as at 1 January of each year.15 A reduced tax rate of 0.05 per cent applies to the portion of net wealth exceeding €500 million. Corporations having their registered office or their central administration in Luxembourg for which the sum of financial assets, transferable securities and bank deposits, receivables held against related parties or shares or units in tax-transparent entities exceed 90 per cent of their total balance sheet and €350,000 are subject to a minimum NWT of €4,815.

14 In Luxembourg City, the municipal business tax is 6.75 per cent and the overall combined rate of corporation taxes in Luxembourg City is of 26.01 per cent.

15 For corporations having a financial year corresponding to the calendar year.
Participation exemption on dividends, liquidation proceeds and capital gains

Under the Luxembourg participation exemption, dividends, liquidation proceeds and capital gains realised by a fully taxable Luxembourg-resident company from shareholdings in resident or non-resident corporations may be exempt from CIT, MBT and NWT, provided certain minimum holding conditions are met.

Withholding taxes

The standard withholding tax rate stands at 15 per cent for dividend payments to both resident and non-resident shareholders. Reduced rates or withholding tax exemptions may be available under applicable double tax treaties. Moreover, a full withholding tax exemption may be available under Luxembourg tax law provided certain conditions are met.

No withholding tax is due in Luxembourg on a full or partial liquidation of a fully taxable company, regardless of the tax residence or tax status of a shareholder.

In addition, there is no withholding tax on royalty payments and fixed or floating rate interest payments made to corporate lenders or to non-residents generally.

Recent developments

Intellectual property tax regime

On 17 April 2018, a new intellectual property (IP) tax regime was enacted, which is applicable as from fiscal year 2018.

An 80 per cent tax exemption on eligible net income for qualifying IP rights is available under the new regime. This new IP tax regime is based on the modified nexus approach developed by the OECD in the final BEPS report on Action 5.

Ruling of the Luxembourg Administrative Court No. 39193C of 23 November 2017

The Luxembourg Administrative Court issued an interesting ruling in November 2017 on the tax treatment of share redemptions by a company.

The Court held that the price paid to a shareholder upon the redemption by the company of all or part of his or her shares should qualify as a sale of the shares (rather than a dividend distribution) regardless of whether the shares are cancelled thereafter or not, provided however that the sale price corresponds to the net asset value of these shares. As a consequence thereof, no withholding tax should apply on such redemption. If the shares are redeemed at a price exceeding the net asset value, the excessive portion of the price may be considered as a hidden dividend distribution (which may be subject to a 15 per cent withholding tax) unless there are exceptional economic reasons justifying a redemption above net asset value.

Exchange of information


16 Luxembourg has currently 81 double tax treaties in force.
17 Cf Article 147 of the law on income tax.
administrative cooperation in the field of taxation and of 25 November 2014 (2014 Law) on
the procedure applicable to the exchange of information in tax matters, with respect to the
Charter of Fundamental Rights of the European Union.

The ECJ ruled in substance that a party has the right to appeal against a request
for information, which the aforementioned laws had denied. As a consequence thereof,
Luxembourg restored the information holder’s right of a judicial review of the legality of
the request by the law of 1 March 2019 amending the exchange of information procedure
as laid down in the 2014 Law (Amending Law). In particular, the Amending Law obliges
the Luxembourg tax authorities to make a high-level review of the foreseeable relevance of
an incoming request for information before sending an order to the information holder. The
information holder will be entitled to seek the annulment of the Luxembourg tax authorities’
order by the Luxembourg Administrative Courts. The claim (which has a suspensive effect)
must be filed with the Administrative Tribunal within one month of the notification of the
information order.

**Multilateral Instrument**

On 7 June 2017, Luxembourg signed the Multilateral Instrument (MLI) as one of 68 initial
signatories.

The MLI addresses the double tax treaty (DTT) changes proposed in the base erosion
and profit shifting (BEPS) action final reports and in the 2017 OECD Model Tax Convention.

In Luxembourg, the ratification process has been achieved through the law of
7 March 2019 and the deposit of the ratification instrument with the OECD on 9 April 2019.
As a consequence, the MLI entered into force on 1 August 2019, but only if the contracting
state of a covered tax agreement (CTA) has also ratified the MLI. CTAs cover the DTTs that
have been designated by Luxembourg as being subject to amendments by the MLI. In this
respect, Luxembourg has listed 81 DTTs as CTAs.

MLI provisions can be classified into three categories: minimum standards that cannot
be opted out of; provisions that apply unless one or both contracting jurisdictions make a full
or partial reservation against them; and provisions that have to be expressly opted into by the
signing jurisdictions to be applicable.

Luxembourg’s notable choices can be summarised as follows: Luxembourg opted for
full reservations with respect to Article 4 (dual resident entities), Article 8 (dividend transfer
transactions), Article 9 (capital gains from the alienation of real estate-rich companies),
Article 10 (permanent establishment triangular cases), Article 11 (savings clause), Article 12
(commissionaire arrangements) and Article 14 (splitting-up of contracts).

With respect to Article 3 (transparent entities), Luxembourg has made a partial
reservation, deciding not to apply Article 3(2), Article 3(1) addressing treaty benefits to be
granted to income ‘derived by or through an entity or arrangement that is treated as wholly
or partly fiscally transparent under the tax law of either Contracting State’.18

With respect to Article 5 (method for the elimination of double taxation), Luxembourg
has chosen option A, providing for a switch-over clause under which the residence state
must grant a credit, rather than an exemption, for the taxes levied in the other contracting
jurisdiction.

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18 Article 1(2) of the 2017 OECD Model Tax Convention.
With respect to Article 7 (prevention of treaty abuse), Luxembourg chose to apply the principle purpose test (PPT) in contrast to the application of a simplified limitation on benefits (LOB) alongside a PPT, or the fully fledged LOB.

Once entered into force, the MLI will be applicable for a specific CTA with regard to the matching provisions only (which include, in any case, the minimum standards).

**Anti-Tax Avoidance Directive**

The Anti-Tax Avoidance Directive (ATAD) lays down rules against tax-avoidance practices that directly affect the functioning of the internal market. ATAD is the European response to the OECD and G20 BEPS action plan set out in 2013 to address tax avoidance, ensuring that multinational companies pay their fair share of taxes where economic activities generating profits are performed and where value is created.

In Luxembourg, ATAD has been implemented by the law of 21 December 2018. It introduced five legally binding measures to clamp down on aggressive tax planning, namely the controlled foreign companies rules, the interest deduction limitation rule, the anti-hybrid rules, exit taxation and the general anti-abuse rule. These rules are applicable from 1 January 2019 except for the exit tax provisions, which will be applicable as from 1 January 2020. While most of them should have no major impact on Luxembourg, the interest deduction limitation rule (IDLR) raises more concerns.

The IDLR limits the ability of taxpayers to deduct excess borrowing costs to the highest of 30 per cent of its EBITDA (taxable earnings before interest, tax, depreciation and amortisation) or €3 million. Borrowing costs are in excess when they exceed the 'taxable interest revenues and other economically equivalent taxable revenues that the taxpayer receives'. Practical issues for the application of the IDLR result from a lack of details regarding the concepts used in the IDLR (i.e., borrowing costs and interest revenues) leaving room for interpretation. In this context, the IDLR may have negative tax consequences, especially for securitisation companies investing into distressed debt. Additional clarifications through one or several administrative circulars have been announced by the Ministry of Finance but are currently still pending.

ATAD has in the meantime been amended by ATAD 2, which extends the scope of the EU hybrid mismatch rules to a wider variety of mismatches and to third countries. ATAD 2 has not been implemented yet into Luxembourg law, but its implementation deadline is 31 December 2019.

**IX COMPETITION LAW**

The amended law of 23 October 2011 on competition (Competition Law), which reflects Articles 101 and 102 of the Treaty on the Functioning of the European Union, prohibits agreements between undertakings, decisions by associations of undertakings, and concerted practices having as their object or effect the prevention, restriction or distortion of competition as well as the abuse of dominant market positions. Such law does not provide for an approval mechanism for mergers by the Luxembourg Competition Council (Competition Council).
Where a transaction has an EU dimension within the meaning of EU competition law, EU merger control rules will apply exclusively and the European Commission will be solely competent to review the transaction.

Where a transaction is below the EU merger notification thresholds, no pre-merger filings or prior notification requirements exist in Luxembourg law, but the referral mechanism in EU merger control law may allow the European Commission to review transactions below the EU merger notification thresholds under certain conditions. In any event, the cooperation mechanism in EU merger control law allows the European Commission to exchange information with the Competition Council when investigating an M&A transaction involving a Luxembourg entity or affecting the Luxembourg market, or both.

Given that the Luxembourg national market is small, and that most M&A transactions with a Luxembourg connection deploy their competitive effect on a global or EU scale, or mainly in other jurisdictions, most of such M&A transactions do not raise any antitrust issues in Luxembourg. Even though the Competition Law does not provide for pre-merger filings with or prior notification requirements to the Luxembourg Competition Council, on 17 June 2016, the Council asserted its competence to scrutinise and sanction M&A transactions that create or strengthen a dominant position in Luxembourg in its *Utopia* decision. Through this decision, it affirmed its authority to exercise *ex post* control of mergers by using, in the absence of a specific merger control regime at the national level, the provisions prohibiting the abuse of a dominant position. In its recent *Féderation des Artisans* decision, the Competition Council confirmed its case law in this respect and carried out *ex post* control of that transaction.

Finally, the law of 15 November 2016 on certain rules governing actions for damages for competition law infringements and amending the amended law of 23 October 2011 on competition (Private Damages Law) implements Directive 2014/104/EU of 26 November 2014 on antitrust damages actions. The Private Damages Law reflects the objectives of the Directive, improving the effectiveness of private enforcement as to infringements of EU and national competition law, and fine tuning the interplay between private damages actions and public enforcement by the European Commission and national competition authorities.

On the one hand, the Private Damages Law facilitates actions for damages through the introduction of certain specific procedural rules:

- *a* their exercise is simplified by a set of irrebuttable and rebuttable presumptions with respect to the existence of an infringement of competition law and its effects;
- *b* access to evidence, essential for competition law-based claims, is facilitated through certain disclosure rules;
- *c* the joint and several liability of undertakings that have infringed competition law through joint behaviours allows an injured party to require full compensation from any of them until it has been fully compensated; and
- *d* the Private Damages Law refers to the Luxemburgish general procedural law principles that provide for a 10-year limitation period for commercial claims.

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20 Decision 2016-FO-04.
21 Decision 2019-R-01.
22 In that matter, the complaint, which qualified as an acquisition of shares as an abuse of a dominant position, was dismissed.
On the other hand, the Private Damages Law encourages consensual dispute resolution. In accordance with the Directive, it provides for the suspension of the limitation period to bring an action for damages for the duration of the consensual dispute resolution process and the suspension of the proceedings relating to the action for damages during a maximum period of two years.

X OUTLOOK

We remain cautiously optimistic that the outlook for M&A activities is positive, and that the market will continue to grow and attract interest from investors both domestic and abroad. The forecast for 2019 regarding domestic M&A in Luxembourg is still relatively good, although less so than one year ago, and confirms the global resilience in this field. Moreover, the impact of legislation from the new US administration is still limited on the global market, and the US market shows a good performance that will probably have positive consequences on the European and Luxembourg markets. This positive effect might, however, be cancelled out, or even outweighed, by the effect of the tensions surrounding the potential escalation of trade wars on the global markets. While Brexit has not yet had a negative impact on the Luxembourg M&A market, there is uncertainty as to whether there will be hard or an orderly Brexit. In addition, the terms of the relationship between the EU and the UK post-Brexit remain to be negotiated. It seems clear that some economically significant areas such as merger clearances, cross-border taxation and transfers of employees will be affected. We see industry players and strategic buyers continuing to be active in Luxembourg (and in other countries by using structures through Luxembourg), increasingly expensive financing, fluctuating exchange rates and a legal and regulatory environment that is getting ever-more complex.
I OVERVIEW OF M&A ACTIVITY

Despite a weak start to 2019, the Mexican M&A market’s performance has been relatively stable compared to previous years.

Certain assets have become more difficult to price due to concerns about the policy-making of the current administration, and therefore some transactions have been temporarily put on hold; however, other participants in the market continue to push forward with their transactions, in some cases as a preventive measure against Mexico’s current political and economic environment. Transactions in the M&A space represent, for some family-owned businesses, a key avenue to monetise a life’s or multiple generations’ work that could otherwise face stagnant or limited growth if it were to rely solely on pure organic growth. This phenomenon, in turn, yields opportunities for investors or strategic buyers who have cash available.

A weakened yet relatively stable peso continues to provide attractive investment return opportunities in several industries including financial services, insurance, real estate, consumer products, health and pharma, manufacturing and industrial.

The number of transactions during 2018 was similar to that of recent previous years. The busiest sectors were technology, financial services and insurance, followed by real estate, industrial and consumer products. Another key industry that has seen continuous action is the infrastructure M&A space, both in social infrastructure such as hospitals and prisons, as well as traditional toll road, waste water treatment plants and renewable energy.

The private equity industry continues to be a key driver for M&A activity in Mexico, led by several established international and local firms, as well as family offices, which are steadily taking a more active role in investments, and thus are leaving behind their role as a silent partner in established funds and are moving in to acting as standalone funds themselves.

Data also provides evidence that the venture capital (VC) industry continues to grow at significant rates, and it is expected to continue doing so in the future. For example, Softbank announced in 2019 a US$5 billion fund dedicated to Latin American investments, and has begun to deploy such fund in companies such as Rappi and PayClip, which have significant operations in Mexico. Such announcement has sparked enthusiasm in the VC and entrepreneurship ecosystem, and is expected to attract other international VC funds to participate in transactions in Mexico.

On the public exit front, although the initial public offerings market has historically lagged behind other emerging financial markets, there is still optimism that increasing exit
opportunities through the public offering of securities will be available to investors in the near future as the Mexican pension funds (AFORES) investment regime continue to become more sophisticated and diverse, thus freeing up capital to be allocated to public offerings. As described in more detail in Section VIII, the government has taken steps to incentivise initial public offerings in the coming years through tax incentives. It remains to be seen if these incentives will have the desired effect.

II  GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Depending on the target’s activities and the industry in which the target operates, any M&A transaction in Mexico will probably be subject to several statutes. For example, during the due diligence investigation of the target or during the structuring of the transaction, laws ranging from the broad mercantile, labour and employment, tax, environmental, insurance and anticorruption statutes to the more industry-specific ones such as those regulating, inter alia, financial services, fintech, cannabis, telecommunications, oil and gas, transportation and healthcare, will all provide guidelines and parameters within which all M&A transactions have to be structured.

In an effort to increase Mexico’s attractiveness for investors, the federal government has consummated several changes to statutes that were perceived to be outdated during the past few years. Certain commercial statutes (e.g., the Mexican Commercial Companies Statute and the Mexican Securities Market Statute) have been amended to incentivise M&A activity by allowing parties to, inter alia, freely agree on customary governance and liquidity provisions required for investors (particularly of an institutional nature) to attain a higher level of certainty on governance and exit provisions. Through the liberalisation effort led by former President Peña Nieto’s administration (2012 to 2018), the Mexican Foreign Investment Law has been subject to several amendments to decrease (or remove) foreign investment restrictions in, inter alia, the telecommunications and oil and gas industries.

III  DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

While the statutes relating to corporate and takeover law have remained relatively untouched, changes in respect of certain capital market products are sure to have a significant effect on the M&A landscape in Mexico.

By way of background, AFORES are still restricted regarding the investments that they are allowed to undertake in accordance with their investment regime, which is set forth by law. As of today, AFORES are not yet permitted to invest directly in privately held companies, but only in publicly listed companies and other publicly listed investment vehicles. However, amendments to such investment regime are currently being reviewed and discussed in Congress. If such amendments were to pass, AFORES will be able to invest directly in privately held companies, which will certainly broaden their investment opportunities and alternatives but would also put significant pressure on their analysis and risk management capabilities.

The current AFORE investment regime, spurred some years ago the creation of publicly traded vehicles that are managed by a general partner and that serve as platforms to carry out investments in various sectors (CKDs), including the private equity, infrastructure,
renewable energy and real estate sectors. The existence of the CKD market in Mexico has caused M&A transactions in various fields and sectors to take off, as pension funds put their cash to work through fund managers in acquisitions and similar investments.

There are four similar products worth discussing that complement the CKD market in Mexico. The first is the creation of real estate investment trusts (FIBRAs), a vehicle that invests in or acquires a real estate asset portfolio and is created through the issuance of a public offering and ultimately listed on the Mexican Stock Exchange. The Mexican real estate market has historically been quite active. However, since the creation of FIBRAs, M&A activity in the real estate sector has increased significantly given that the creation of a FIBRA typically entails the bundling or acquisition of real estate assets that will become part of the FIBRA. The sponsors that manage FIBRAs have additional firepower from the amounts raised in a public offering or in follow-on offerings to acquire additional assets for a FIBRA’s portfolio, and FIBRAs present a great take-out opportunity for real estate developers and other stakeholders of real properties.

The second product created the equivalent of a master limited partnership, the FIBRA E, which is an investment vehicle for energy and infrastructure projects and is listed on the Mexican Stock Exchange. One key feature is the tax benefits provided to investors in a FIBRA E, as the investment vehicle and the portfolio companies through which investments are held in the infrastructure and energy assets are deemed transparent from a tax perspective. Despite current volatility in capital markets generally, there is a robust pipeline of FIBRA E projects for the future. It is uncertain how many of the FIBRA E projects will effectively materialise. While a strong impact on M&A activity is not evident yet, there is an expectation that transactions in the energy and infrastructure space will continue to increase.

The third product is the special purpose acquisition company (SPAC), which is an investment vehicle listed on the Mexican Stock Exchange that obtains funds from the public offering through which it is created to invest and acquire a company, which may or may not be identified at the time of the public offering. Essentially, it provides a sponsor with sufficient funds to conduct an M&A transaction within the 24 months following its creation. Recent SPAC offerings, such as the one made by Promecap, indicate a acceptance of these types of investment vehicles in the Mexican market, but only time will tell if that acceptance continues. Recent tax incentives described further below also seek to foster the creation of SPAC and M&A transactions related thereto. To the extent that more SPACs are issued in the market, they should certainly result in a positive effect on the M&A market in Mexico.

The fourth product is the CERPI, which is a derivative of the CKD, but with two key differences: the first is a management and governance structure that more closely resembles a traditional private equity fund, in which limited partners are expected to have a very limited role in management and governance; the second, and the one that has really triggered a spur in the use of this product, is that up to 90 per cent of the proceeds raised in a CERPI may be deployed outside Mexico. This has led many international fund managers to seek to fundraise in Mexico, as they can use it now as a regional platform to invest not only in Mexico but outside of Mexico as well. This development is certainly expected to raise the level of M&A activity as these funds begin to deploy the funds they raise.

Another important recent legal development, was the enactment of the Fintech Law and its regulations, which have provided a legal framework for companies operating crowdfunding, wallet and crypto businesses. The Fintech Law has attracted a lot of attention and focus on technology-based solutions for the financial system, and will eventually lead to M&A activity as those participants begin to consolidate.
FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

As noted in previous sections, the participation of international and global companies in the Mexican market continues to be attractive. The level of cross-border transactions remains significant, and the long-term view of many global institutional investors continues to drive their desire to invest in Mexico and benefit from current opportunities in the market.

It is important to note that the United States continues to be the country that represents the most foreign investment activity in Mexico. Other principal countries carrying out substantial foreign direct investment in Mexico are Canada and Spain.

Given the manufacturing infrastructure and capabilities that Mexico has developed through the years, the steadily growing middle class and the increase in consumerism, certain sectors continue to be ripe for foreign investment, as has been evidenced through recent M&A transactions, and these are expected to continue to attract foreign investment. It is expected that foreign investment will continue to drive a significant portion of the large and complex M&A transactions in Mexico.

In September 2018, Mexico, the United States and Canada announced an agreement to modernise the North American Free Trade Agreement (NAFTA), which will be known as the United States–Mexico–Canada Agreement (USMCA). The new agreement includes significant revisions to the agreement signed in 1994. Regarding foreign investment, USMCA largely replicates the protections provided under the 1994 NAFTA that are typically afforded by bilateral investment treaties such as:

- a minimum standard of treatment, which includes fair and equitable treatment and full protection and security;
- national treatment;
- most-favoured nation treatment; and
- transfers and protections in the case of direct or indirect expropriations.

Under USMCA, such protections may be claimed only by American and Mexican companies working in the oil and gas, energy, telecommunications, transportation and infrastructure sectors, provided that they hold a government contract or carry out activities related to one of these sectors. Neither Canadian companies with investments in Mexico or in the United States, nor Mexican or American companies with investments in Canada, shall have access to arbitration under USMCA. Companies that do not participate in any of the above-mentioned sectors will only be able to submit to arbitration violations involving national treatment or most-favoured nation treatment, which require the government’s implementation of a measure intended to discriminate against a company by reason of its nationality, and violations involving a direct expropriation. Any other treaty violations must be submitted before the national courts. USMCA provides a specific chapter for financial services, which also sets forth an investment arbitration mechanism that is limited to the above-mentioned narrower scope of protections. USMCA significantly limits the protection offered to foreign investment by making claims involving violations of fair and equitable treatment and indirect expropriation not subject to investment arbitration. In the absence of such protections, investors will not be able to resort to arbitration to defend against government harassment, abrupt regulatory measures or the unjustified termination of any agreement or permit.

The USMCA has yet to be ratified by the US Congress, Canada’s Parliament and Mexico’s Congress. However, the Mexican Senate, which is controlled by Lopez Obrador’s political party, is expected to ratify the USMCA soon.
V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

As noted in the Section I, Mexican M&A performed strongly throughout 2018. There is a trend of consolidation and a high volume of activity in certain sectors, such as the technology, pharmaceutical industry, real estate, food and beverage, distribution and retail.

M&A activity in the real estate sector is driven in large part by FIBRAs, as discussed in Section III. Transactions mainly involve the acquisition of real estate portfolios. The acquisition story driven by FIBRAs has not slowed since then.

The infrastructure (e.g., toll roads) and soft infrastructure (e.g., government-concessioned hospitals, schools and prisons) space continues to attract international institutional investors, such as the Canadian pension funds.

The pharmaceutical industry remains fragmented and filled with attractive targets ripe for consolidation or participation by international participants.

In the aerospace and automotive sectors, we continue to see significant M&A activity, mostly on the basis of cross-border transactions effected by global players but also in respect of which Mexican operations will still have a significant role.

The airline industry has also supported developments that have led and may continue to lead to M&A activity. Recent amendments allowing a greater participation (up to 49 per cent) of foreign investment led, for example, Delta Airlines to acquire a substantial additional stake in Aeromexico.

Finally, there has also been a trend for a higher volume of transactions in the VC and technology space, which still may not represent significant M&A volume at this stage but should have an impact in the short to medium term as these ventures mature and the marketplace becomes more sophisticated. Increased valuations for technology companies has spurred significant activity in the growth stage of these companies, and should lead to future M&A activity as well.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Mexican corporate law does not impose restrictions on financial assistance, and thus a Mexican target company’s ability to secure acquisition financing with its own assets makes financing alternatives relatively more available for M&A and private equity transactions. Mexican banks are actively participating in the market, and this has opened the door to other types of lenders, such as credit opportunities funds created by global institutions.

There is no particular trend regarding bank and mezzanine debt in Mexican M&A and private equity transactions. As in other markets, a decision about the type of acquisition financing is based upon several factors, including the target company’s sector and its growth plans and needs.

In those M&A and private equity transactions that include bank debt, Mexican banks are normally pressed to incorporate US terms in their loan documents, including material adverse change (MAC) provisions that match the acquirer’s right to withdraw from a potential acquisition and provisions that seek to limit the conditions of the financing as regards the conditions applicable to the closing of the acquisition. Owing to the absence of financial assistance restrictions and a conservative approach to lending, Mexican banks very rarely accept covenant-lite loans, which thus turns the negotiation of the financing terms and conditions and the implementation of the relevant collateral packages into a substantial part of the legal work relating to the closing of a transaction.
When an M&A or private equity transaction involves financing, including going-private transactions, one of the most controversial sections of loan documents is the one relating to the conditions for a drawdown, and specifically the material adverse effect (MAE) or MAC condition that directly affects the certainty of funds. It is hardly ever the case that the definition of a MAE or MAC in a purchase agreement matches the definition in the loan documents, and therefore the gap is generally a risk that the acquirer or investor is asked to assume. In the context of a cross-border deal, the definition of a MAE or MAC becomes even more complex when negotiating political or national risk language within an agreement, especially in light of Mexico’s current political environment and Trump’s discourse on US–Mexico relations. Having said that, we see that sponsors in private equity transactions are generally more comfortable with the legal and related risks involved. Increasingly, investors focus more on returns and less on country risk.

With respect to leveraged buyouts (LBOs), the main consideration in structuring such transactions depends on the ability of target companies to pay dividends and make distributions to their shareholders regularly to service acquisition loans. Hence, when structuring LBOs in Mexico, it is paramount to incur the acquisition financing at the level of the operating target companies, or to somehow restructure the debt after the closing so that the operating entities can actually service the debt without having to deal with the tax and other timing restrictions applicable to dividends under Mexican law. In addition, in pricing acquisition financing, investors have to consider both the applicable withholding taxes on interest payments made to foreign lenders (and the potential incremental cost they represent in terms of gross-up provisions) and fraudulent conveyance issues under the Mexican Insolvency Law that are mitigated through due diligence, representations, warranties and, ultimately, indemnities.

VII EMPLOYMENT LAW

Employee subcontracting regimes are common in Mexico and, consequent to relatively recent amendments to tax and employment laws, thorough diligence is crucial for identifying existing liabilities to avoid or reduce any labour or tax contingencies.

A subcontracting regime exists whenever employees of an entity (i.e., a contractor) perform tasks or provide services to another entity (i.e., a client). In view of the foregoing, whenever there is a subcontracting regime in place, it is crucial to verify whether it complies with the following conditions set forth by the Mexican Federal Labour Law:

a. it cannot cover all the activities or those activities, similar or alike as a whole, that are performed at the workplace;
b. services to be rendered must be justified because of their specialised nature; and
c. subcontracting may not involve similar or the same activities as those performed by the other employees in the contracting party.

Failure to comply with the specific conditions will not only result in joint and several liability between the contractor and the client, but also in the direct obligation for the client to be liable for the costs of employment and social security obligations, including profit sharing.

Earlier this year, the Senate approved an overhaul of the country’s federal labour law. The changes include workers’ right to vote through secret ballots on unions and their labour contracts, which normally does not occur in Mexico. The labour reform seeks to ensure that workers will finally be represented by their unions.
VIII TAX LAW

Transfer pricing reporting obligations contained in Mexican law have an impact on tax filings for pre-closing, post-closing and straddling periods, as the buyer and seller will have to agree on the terms and conditions under which these obligations will be complied with on behalf of the target. Compliance with these obligations is particularly sensitive as it provides information related to the organisation and operation of the group worldwide, which, needless to say, the seller will not be willing to share with the buyer; thus, strong confidentiality provisions would have to be negotiated as well.

The imminent approval by Mexico of the OECD’s multilateral instrument will limit access to certain tax treaties to which Mexico is a party. This is particularly important in light of the structuring work that needs to be performed prior to any M&A transaction taking place, because any structuring analysis will need to address additional limitations.

There are also new obligations within the Mexican legislation related to the issuance of digital invoices that are now applicable for, inter alia, stock purchases and payments made to non-Mexican residents. The tax authorities continue to enhance all the regulations pertaining to the issuance of digital invoices, which now apply to certain transactions that were not considered to be affected in the past. Accordingly, stock purchase agreements have to provide some detail in this regard to define which tax documents will be issued by whom at closing, thus avoiding any discussions, as these rules are numerous and detailed.

Earlier this year, the Tax Administration Service published the rules for the application of tax incentives for corporate bonds and initial public offerings (Rules). The Rules are the result of an open dialogue between the Ministry of Finance and Public Credit, various financial industry associations, the licensed securities exchanges in Mexico and their legal advisers. The tax incentive for initial public offerings, in summary, allows for Mexican-resident individuals and non-Mexican tax residents to apply a rate of 10 per cent to capital gains derived from the sale of shares issued by Mexican-resident corporations in licensed securities exchanges in Mexico during 2019, 2020 and 2021, provided that certain requirements are complied with. The tax incentive for bond offerings, in summary, allows Mexican tax-resident issuers of corporate debt outside of Mexico to apply a zero per cent withholding rate (as opposed to 4.9, 10 or even 35 per cent, in some cases) subject to compliance with certain requirements such as having the debt instruments listed in Mexico.

In such regard, the Rules clarify that the total equity value of the issuer shall not be greater than 25 billion pesos and shall be computed prior to the initial public offering (IPO); the tax incentive is also applicable when a sale is done through the exercise of over-allocation options (greenshoe) or follow-ons; the tax incentive will also be applicable to whomever sells shares to a SPAC or sells shares issued by a SPAC obtained as a result of an initial business combination; with respect to the exception provided for the divestment process of a private equity investment trust (FICAP), the exception shall also be applicable to non-residents; the 20 per cent minimum participation of the FICAP shall be computed prior to the IPO; and the participation of a FICAP shall be computed taking into account not only the shares acquired by the FICAP but also those acquired by certain foreign legal arrangements that are related to the FICAP or its manager.
IX  COMPETITION LAW

Enforcement by Mexico’s antitrust agency has been particularly active in recent years. Several ongoing investigations and the imposition of substantial fines in many sectors of the economy indicate the agency’s new more active and aggressive stance. On the antitrust clearance front, the outcome of many M&A transactions has become more difficult to predict, especially in borderline cases for which preemptive planning of an intelligent approach to the agencies has become more important. Similarly, pre-closing integration efforts now need to be conducted with more sensitivity to antitrust requirements.

X  OUTLOOK

According to recent polls, President Andrés Manuel López Obrador, having held office for less than a year, continues to be popular and has substantial support. It is still early to estimate the President’s effects on the economy, the business sector and particularly on inbound M&A.

The President has consistently attacked the energy reform enacted by Peña Nieto’s administration, and while there continues to be no indication of a major shift in the applicable regulatory framework, there is no optimism regarding new projects in the oil, gas and power sector.

In general, Mexico’s regulatory framework and macroeconomic outlook has made most economic analysts maintain their view that the Mexican economy continues to be experiencing a period of slow expansion.

After an election year and with USCMA discussions in the ratification stage of the respective chambers of Congress, the expectation was that a good portion of the uncertainty affecting the M&A market during 2018 would have subsided considerably. However, in addition to global economic uncertainty, Trump’s constant tariff threats towards Mexico and the rating agencies’ recent revisions of the outlook for Mexico and Pemex (Mexico’s state-controlled oil company) have not helped address such uncertainty.

CKD listings are on hold: while there are close to 30 listing filings in process, no listing has been made during 2019. There is more than one reason for such impasse, but one of them is the uncertainty as to the AFORES new investment regime.

Mexico’s demographic trends continue to show an economy less dependent on exports, a growing middle class and increased consumerism (with more access to consumer credit), which suggests ample investment opportunities in sectors serving domestic consumption such as financial services, technology, healthcare, retail, pharma, education, dwellings and agro-industry.
Chapter 31

NETHERLANDS

Meltem Koning-Gungormez and Hanne van ’t Klooster

I OVERVIEW OF M&A ACTIVITY

The Netherlands again saw a strong year of M&A activity, with a total increase in transactions of 11.4 per cent as compared to 2017, resulting in the highest amount of transactions in 11 years.2

Most M&A transactions in 2018 were conducted within the service industries branch, but the educational, healthcare and trading sectors also significantly contributed to M&A activity. M&A activity was also high in the technology sector, in which Dutch companies continue to attract the interest of international companies. For the most part, larger corporates acquire tech startups and invest in innovative companies to speed up technological development and keep up with market demands.

The popularity of the use of warranty and indemnity insurance continued steadily in 2018. Notable regarding this year’s M&A activity is that it was very much a seller’s market in the Netherlands, with a large amount of transactions conducted as auctions.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Dutch transactions are generally structured as a transfer of the shares or (specific) assets of a company or by way of a legal merger. The main principles governing the legal framework of these transactions are set out in the Dutch Civil Code.

Parties are free to enter into contracts and to negotiate the terms of contracts. According to case law dating back to 1981, not only the wording of the agreement should be considered for interpretation thereof, but also the intentions of the parties and what they can reasonably expect from each other. This means that contractual clauses are to be interpreted in line with the meaning that the parties under the given circumstances could reasonably attribute to them and that they could reasonably expect from each other.3

Over time and because of foreign involvement, contracts have become more extensive and more Anglo-American. An example of this is the use of the entire agreement clause, which is now standard practise in transactions, although case law indicates that the use of an entire agreement clause does not simply preclude the significance of the parties’ statements or conduct before the entry into an agreement. Under Dutch law, the actual meaning of the

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3 Supreme Court 13 March 1981 (Haviltex).
clause still depends on the specific circumstances of a case. 4 Recent case law does indicate that depending on the circumstances, a linguistic interpretation could become increasingly important, for example if it concerns a commercial agreement entered into by professional parties, if the agreement was extensively negotiated, or if the parties were assisted by legal advisers or lawyers.5

Under Dutch corporate law, the stakeholder model is predominant. This model entails the board of a company having a duty to act in the best interests of a company and all the stakeholders involved, thereby focusing on creating long-term value. The Enterprise Chamber, a specialised division within the Amsterdam Court of Appeal, is the court of first instance in disputes involving mismanagement and similar corporate issues, and the appellate court in certain corporate litigation disputes. The Enterprise Chamber is often addressed by foreign shareholders to challenge the parameters of the Dutch stakeholder model, for instance in a recent case in which shareholder Elliott wanted to intervene in the strategy of AkzoNobel in order to enter into negotiations with PPG Industries for the acquisition of AkzoNobel.

i Negotiations and pre-contractual good faith
In the pre-contractual phase, parties are obligated to behave in accordance with the requirements of reasonableness and fairness and, in doing so, they must also have their behaviour determined by the legitimate interests of the other parties. Although in theory all parties are free to break off negotiations, it can be unacceptable to do so because one party may be justified in its expectation that an agreement will be concluded, or because of other circumstances. In that event, that party could be entitled to compensation, or could request an injunction requiring the other party to continue negotiations. The justified interests of the party that breaks off negotiations, the manner in and the extent to which that party has contributed to the other party’s expectation, and whether any unforeseen circumstances have occurred in the course of the negotiations, among other things, should be taken into account.6

ii Anti-takeover structures
In the event that a shareholder requests an agenda item that may lead to a change in a company’s strategy (such as a takeover), the management board can invoke, pursuant to the Corporate Governance Code, a response time of a maximum of 180 days for further deliberation and constructive consultation. Furthermore, it is possible to place preference shares at a different entity, such as a foundation that is serving the interests of the company and its stakeholders. By granting this entity a call option that can be exercised during an imminent takeover, the equity interest that a hostile party accrues will dilute. Consequently, this entity is able to ensure that the company will continue to focus on creating long-term value. The issuance of priority shares with specific (voting) rights or depositary receipts instead of shares is also a possibility. In the latter case, the votes on the shares will stay with a foundation that is friendly to the board of the company.

4 Supreme Court 5 April 2013 (Lundiform/Mexx).
5 Supreme Court 29 June 2007 (Derksen/Homburg).
6 Supreme Court 12 augustus 2005 (CBB/JPO).
Before effecting a transaction in the Netherlands, the works councils of the parties involved may have to be notified and consulted under the Works Council Act and a notification may have to be sent to the Social and Economic Council of the Netherlands (SER) Merger Code Committee and the trade unions in question under the SER Merger Code 2015. Obtaining clearance from the Netherlands Authority for Consumers and Markets and the European Commission regarding possible competition concerns may also be required. Furthermore, sector-specific notifications may be necessary, such as to the Dutch Central Bank.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Ultimate beneficial ownership register
A legislative proposal introducing the ultimate beneficial ownership register (UBO Register) in the Netherlands was submitted to the House of Representatives on 3 April 2019. The proposal is an implementation of the (amended) Fourth Anti-Money Laundering Directive, which seeks to prevent the use of financial systems for money laundering or terrorist financing by means of, among other things, introducing an UBO Register. The UBO Register will be part of the Dutch Trade Register, and as such it will be administered by the Chamber of Commerce. Part of the information included in the register will be publicly accessible, but provisions have been made to ensure the privacy of UBOs. The UBO Register must be set up at the latest by 10 January 2020.

ii Act on management and supervision of legal entities
A legislative proposal for the management and supervision of legal entities was submitted to the House of Representatives on 13 June 2016. The aim of the proposal is to achieve greater uniformity among the various Dutch legal entities (i.e., private limited liability companies (BVs) and public limited liability companies (NVs), foundations, associations, cooperatives and mutual insurance associations). This uniformity mainly concerns the applicable board models – so both the one-tier board model and the two-tier board model – rules regarding conflicts of interests of board members, and rules regarding the duties and responsibilities of board members. Two memoranda of amendment were submitted on 8 November 2018 and 15 February 2019, respectively. Originally, the legislative proposal included uniform rules applicable to all legal entities in the general part of Book 2 of the Civil Code. This approach has now been abandoned. In the amended legislative proposal, the provisions are repeated for each legal entity, taking into account the differences between them. In addition, some changes with regard to content have been made. One example is the restriction with regard to multiple-vote rights of management board or supervisory board members. This restriction has been removed from the proposal (since the restriction was already applicable to BVs and NVs, the removal only concerns the other forms of legal entities).

iii Corporate Governance Code 2016
The Corporate Governance Code 2016 entered into effect on 1 January 2017, replacing the first Corporate Governance Code of 2008. The Code of 2016, applicable to Dutch listed
companies and also to non-listed companies if they opt for its application, is based on the principle of comply or explain. Directors must report on compliance with this principle in the annual accounts. The most important difference from the Code of 2008 is that long-term value creation is now a central aspect of the Code. The management board has to develop a strategy relating to the creation of long-term value, taking into account, among other things, the interests of all stakeholders. The supervisory board has to monitor the management board in this. In addition, the management board is required to create a culture within the organisation that is focused on long-term value creation, under supervision of the supervisory board. As with the Code of 2008, the Corporate Governance Monitoring Committee will report annually on compliance with the Code.

iv Proposed regulation on hostile bids and takeover activities
Discussion about whether Dutch listed companies are sufficiently protected against hostile bids and takeover activities led to a draft legislative proposal, which was published on 7 December 2018 for consultation until 9 February 2019. The proposal indicates that setting up the policy and strategy of a company is the authority of the management board. In addition, under the proposal the management board has a cooling-off period of up to 250 days if a shareholder proposes the dismissal, appointment or suspension of a member of the management of the supervisory board, or if a non-approved offer on the shares has been announced or made. In the opinion of the management board, these acts must be contrary to the interests of the company. Shareholders may request an early termination of the cooling-off period of the Enterprise Chamber.

In addition, on 5 March 2019 a legislative proposal on telecommunications parties was submitted to the House of Representatives as a reaction to the attempted takeover of KPN by América Móvil in 2013. The proposal gives the Minister of Economic Affairs and Climate the authority to prohibit the acquisition or exercise of predominant control over parties in the Dutch telecom sector if this would lead to a threat with regard to national security or public order.

v Directive on long-term and transparent engagement by shareholders
Directive (EU) 2017/828 (amending Directive 2007/36/EC) regarding the encouragement of long-term and transparent engagement by shareholders of listed companies had to be converted into national law by the Member States by 10 June 2019. The Directive contains requirements relating to the remuneration of directors, the identification of shareholders, the facilitation of shareholders’ rights, the transmission of information, transparency for institutional investors, asset managers and proxy advisers, and related party transactions.

The legislative proposal implementing the Directive was submitted to the House of Representatives on 18 October 2018 and adopted on 2 April 2019. Some provisions with regard to the remuneration of board members also apply to non-listed NVs.

vi Act on the protection of trade secrets
On 23 October 2018, the Dutch Trade Secrets Act, implementing Directive (EU) 2016/943, entered into force. The Act contains provisions to enforce trade secrets and remedies against infringing goods. Under the Act, the court has the authority to award full (reasonable and proportionate) costs to the winning party (similar to intellectual property cases).
vii Regulation on screening of foreign direct investment

At the EU level, a protectionist attitude can be observed as well. On 10 April 2019, EU Regulation 2019/452 establishing the framework for the screening of foreign direct investment officially entered into force. The Regulation will fully apply to Member States from 11 October 2020. The new framework will, among other things, allow the EC to issue opinions if an investment poses a threat to the security or public order of more than 1 one Member State or if it could undermine a project or programme of interest to the EU.

viii Directive on cross-border conversions, mergers and divisions

On 31 January 2019, the EU ambassadors reached an agreement on the Council’s position on the draft directive with regard to cross-border conversions, mergers and divisions. The directive will allow companies to benefit from the EU single market. Extensive procedures are introduced for cross-border conversions and divisions, and additional rules for cross-border mergers of capital companies established in different Member States. The directive contains, among other things, procedures that ensure that cross-border transactions are consistent with all relevant national legal systems and that employees and shareholders are properly informed of the effect of transactions. The presidency of the Council will now start negotiations with the European Parliament with the aim of adopting the draft directive.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Although foreign involvement has been present in the Dutch M&A market for a long time, there seems to have been a decrease in the proportion of cross-border deals. This trend cannot be explained by inbound M&A activity (which only decreased slightly). During 2018, there were numerous (both successful and unsuccessful) efforts by foreign companies to take over Dutch businesses. One striking example was the acquisition of the chemical branch of AkzoNobel for €10.1 billion by the American investment company Carlyle and the Singaporean investment company GIC, which generated the highest deal value on the Dutch M&A market in 2018. Carlyle and GIC won a bidding battle against three other parties, including the Dutch company HAL Investments.

Another public bid that has stirred feelings since 2016 is Qualcomm Inc’s bid for Dutch chip manufacturer NXP Semiconductors NV. In March 2018, Qualcomm announced it was extending the period of its cash tender offer made pursuant to the purchase agreement of October 2016. However, the deal collapsed after the non-extendable deadline passed for obtaining Chinese regulatory approval.

Other examples include the acquisition of Dutch stroller company Bugaboo by global investment firm Bain Capital Private Equity and Dutch theater company Stage Entertainment by the US media company Advance Publications Inc (both for undisclosed sums).

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In 2018, M&A activity in the Dutch IT branch continued to grow, attracting the interest of both foreign companies with strategic motives and private equity parties. One notable transaction was the acquisition of the Dutch software company Mendix by Siemens for US$730 million. Mendix is in a position to help Siemens, primarily known for its
industrial manufacturing and therefore not a self-evident takeover party with the digital transformation of the company. It is expected that non-traditional strategic parties will play an increasingly important role in M&A activity in this branch.

In addition, 2018 was a good year for takeovers of Dutch startups. Besides the acquisition of Mendix, notable examples are the acquisition of the Dutch cybersecurity company Security Matters by the Israeli cybersecurity company Forescout Technologies for an amount of US$113 million, and the acquisition of the Dutch gaming server hosting provider i3D.net by French gaming company Ubisoft for an undisclosed amount.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Cash has remained the preferred means of funding M&A deals. Private equity and venture capital funding are runners-up as sources of funding for most transactions. Bank loans are also attractive in view of the low interest rates. A relatively new form of funding is the initial coin offerings, whereby startups using blockchain technology raise capital through coin offerings. The Dutch regulatory authorities are watching these developments closely, as they may trigger money laundering and fraud.

VII EMPLOYMENT LAW

i The Work and Security Act

With the introduction of the Work and Security Act in July 2015, employment law has been amended substantially. The Act regulates most aspects, such as entering into an employment agreement, employment conditions and the termination of employment agreements.

Under the Act, an employer can only terminate an employment contract on a limited number of grounds. In the event of the long-term illness of an employee or if an employer can demonstrate sufficient economic reasons, the Employee Insurance Agency will grant permission for an employer to terminate a contract. If the grounds are more personal (such as inadequate performance or a damaged working relationship), permission to terminate an employment agreement must be obtained from the courts. In all cases (except for a serious imputable act by the employee and summary dismissal), an employee who has been employed for 24 months or longer is entitled to a statutory severance payment (transition fee).

ii The Balanced Labour Market Act

Changes in employment law are forthcoming. The Balanced Labour Market Act will enter into force on 1 January 2020. The Act contains amendments to Dutch employment law with the objective of narrowing the gap between employees with a permanent employment agreement and flexible workers. Some of the most important changes are the following:

a A new ground for dismissal will be introduced in addition to the existing limited grounds for dismissal: the cumulation ground. This ground offers employers the option to combine several incomplete grounds for dismissal into one successful ground. In the case of a cumulation of grounds, the court may award an employee an extra fee to a maximum of half the statutory transition fee on top of the transition fee (and fair compensation, if any).

b Under the Balanced Labour Market Act, employees will be entitled to a transition fee from the first day of their employment agreement (including the probationary period). Currently only an employee who has been employed for more than 24 months
is entitled to the statutory transition fee. The way of calculation will also change. For the first 10 years, the statutory transition fee amounts to one-third of a monthly salary. Further, the temporary measures with regard to the transition fees, lower payments for small employers and extended accrual for older employers will lapse.

c  The sequence system for successive fixed-term employment contracts will be extended to three years. An employment contract will be deemed permanent in the event of a fourth consecutive contract or if the duration of employment exceeds three years. It will be possible to deviate from this rule through collective labour agreements if the work requires this (for instance, in the case of temporary work).

d  Payroll workers will be entitled to the same terms and conditions of employment as employees employed by the hirer, as well as an adequate pension scheme.

iii  Pre-packaged insolvencies and transfers of undertaking

In 2017, the European Court of Justice (ECJ) ruled that pre-packaged insolvencies (pre-packs) are not excluded from Directive 2001/23 on the transfer of undertakings (Directive). Based on the Directive – and the implementation thereof in the Civil Code – the employees of a transferring undertaking remain entitled to their employment and all rights and obligations from that employment. In this event, the acquiring undertaking must also take over these employees.

If an undertaking is declared bankrupt, its employees are not protected by the Directive or the Civil Code. A pre-pack is a transfer of the assets prepared before the declaration of bankruptcy with the consent of a prospective insolvency administrator, appointed by the court, and is put into effect by that administrator immediately after the declaration of bankruptcy.

The ECJ has ruled that the Dutch pre-pack procedure does not qualify as bankruptcy proceedings within the meaning of the Directive because its purpose is for the continuation of a company, not its liquidation. Therefore, it is not justified that employees lose the protection of the Directive. The consequence is that all employees will automatically transfer to the acquiring company while retaining the employment conditions of the bankrupt company. To clarify and strengthen the position of these employees after a transfer, the government has proposed measures that are detailed in the Transfer of Undertaking in cases of Bankruptcy Bill. In principle, all employees of a undertaking will transfer to a new undertaking, and they will remain entitled to their employment and all rights and obligations from that employment. Only if jobs become redundant because of sufficient economic reasons will an employee not be obliged to take over employees. The Bill was presented for consultation on the internet on 29 May 2019.

iv  Self-employed workers

The government is working on a replacement for the Assessment of Employment Relationships (Deregulation) Act to clarify the position of self-employed workers. It is often the subject of dispute whether a self-employed person is in fact employed by a contracting party.

In the Coalition Agreement 2017–2021, the coalition proposes an alternative to the model agreements that the Dutch Tax Authority is currently approving. The use of these approved models reduces the risk of meeting the requirements of an employment relationship with all its obligations (such as taxes, but also protection under Dutch dismissal law). The proposed alternative contains, for example, a minimum rate for independent contractors and the introduction of a declaration of commissioning. Those elements contribute to security
and clarity for independent contractors about their position. With its vote in favour of the Balanced Labour Market Act, the Senate also voted in favour of the motion. The main reason for this motion is the fear that employers will start to use temporary workers and self-employed persons in stead of payroll employees as soon as the Balanced Labour Market Act enters into force. It is not clear yet if a minimum rate will be introduced or if other measures will be taken. The government has announced that new legislation will be in place as per 1 January 2021, so more clarity is expected during the course of 2020.

v Legislative proposal aiming to increase awareness of equal pay for women

On 7 March 2019, the legislative proposal aiming to increase awareness of equal pay for women was submitted to the House of Representatives. This proposal aims to increase awareness of equal pay for women and strengthen the control thereof. The proposal aims to ensure that:

a companies that are required by the Civil Code to publish an annual report are obliged to include figures on the remuneration ratio between men and women, and an explanation for the possible difference in pay between men and women and of the policy they are pursuing to promote equal pay;

b companies that have at least 50 employees are required to apply for a certificate that states they have equal pay for men and women. The certificate is valid for a period of three years. Smaller companies can apply for this certificate on a voluntary basis;

c there will be a public register to check which companies received a certificate and which requests have been declined or withdrawn;

d companies without a certificate are deemed to be paying unequal remuneration for man and women. Employers will be obliged to prove this is not the case;

e every employee has the right to file a complaint with the Netherlands Institute of Human Rights about unequal pay; and

f the Inspectorate SZW will be charged with the supervision of equal pay and is authorised to impose fines of up to a maximum of €83,000.

It is unclear whether the proposal will be adopted (in this form). Some employer organisations have already criticised this proposal. If the proposal is adopted, there will be a two-year transition period.

VIII TAX LAW

i OECD Base Erosion Profit Shifting

The public debate on corporate tax planning continued, and on 7 June 2017, the Multilateral Instrument (MLI) proposed following the OECD’s Base Erosion Profit Shifting (BEPS) Action 15 was signed by more than 70 countries, including the Netherlands. Pursuant to the MLI, BEPS Actions — such as agreed minimum standards to counter treaty abuse — can be implemented in bilateral tax treaties without countries having to renegotiate and amend all such treaties. One of the measures of the MLI is the introduction of a principle purpose test (PPT), pursuant to which a treaty benefit may be denied if obtaining that treaty benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting the benefit in the relevant circumstances would be in accordance with the object and purpose of the relevant treaty. Considering that the PPT is an agreed minimum standard against treaty shopping, and that
all countries that signed the MLI have opted for at least the implementation of the PPT, it is likely that this anti-abuse rule will be implemented in many of the Netherlands’ bilateral tax treaties. In abusive situations, it will then become much easier for the Netherlands to deny treaty benefits to foreign recipients of Dutch source income.

ii Dividend tax
A recent change in tax regulation has had an immediate effect on the structure of M&A transactions. The Act regarding the dividend withholding tax obligation for holding cooperatives and the expansion of the dividend withholding tax exemption came into effect on 1 January 2018. Under previous Dutch law, a cooperative was not subject to dividend withholding tax, unlike a BV and an NV. In light of the increasing importance of cooperatives in international structures (as a possible means for international tax evasion) and the state aid risk, a dividend withholding tax obligation for qualifying membership rights in holding cooperatives has been introduced. A holding cooperative is defined as a cooperative whose actual activity in the year preceding the distribution consisted primarily (i.e., for 70 per cent or more) of the holding of participations or the direct or indirect financing of affiliated entities or natural persons. A qualifying membership right of a holding cooperative is defined as a right that entitles the holder to at least 5 per cent of the annual profit or at least 5 per cent of what is paid out on liquidation. Furthermore, under the new Act, the dividend withholding tax exemption is extended from distributions made to qualifying BV and NV shareholders within the European Union and the European Economic Area (EEA) to distributions made to qualifying BV and NV shareholders and qualifying holding cooperative members located in the European Union, the EEA or in a country with which the Netherlands has concluded a treaty that contains a tax provision for the prevention of double taxation. The exemption is subject to an anti-abuse rule. Although the dividend withholding tax will be abolished altogether in 2020, the government expressly chose to introduce the Act because of the state aid risk and the fact that it can serve as a basis for new legislation.

iii Withholding tax on interest
Under the current law, the Netherlands does not levy a withholding tax on interest. However, the government recently announced plans to introduce a withholding tax on interest in abusive situations as from 1 January 2021 to avoid the Netherlands being used for payments to low tax jurisdictions through Dutch conduit entities. No details of this new withholding tax are yet known. In principle, a Dutch company engaged in financing activities will be taxed on the difference between the interest income and expenses (spread). For intragroup financing companies, there are minimum equity and substance requirements that should be reviewed and discussed in more detail.

IX COMPETITION LAW
On 26 October 2017, the General Court of the European Union annulled the EC’s decision dated 10 October 2014 whereby it approved the merger between Dutch cable companies UPC and Ziggo (following the acquisition of Ziggo by Liberty Global, the US parent company of UPC) on the basis of a complaint by Dutch cable company KPN. On 30 May 2019, after reassessing the transaction, the EC, subject to certain conditions, has confirmed its earlier approval. The outcome of this case remains uncertain, as this decision has again been appealed against by KPN.
At the beginning of 2017, Liberty Global and Vodafone combined their Dutch businesses into the joint venture VodafoneZiggo. This merger was approved by the EC on 3 August 2016. KPN appealed against this approval as well. On 23 May 2019, the General Court rejected KPN’s complaint and concluded that the EC was right in approving the merger. The EC’s approval was subject to the condition that Vodafone would sell its fixed-telecom division in the Netherlands. In December 2016, both the EC and the Netherlands Authority for Consumers and Markets cleared the acquisition of this division by telecom provider T-Mobile Netherlands (for an undisclosed fee), paving the way for the joint venture.

In addition, on 27 November 2018 the EC gave unconditional clearance to the acquisition of Dutch telecom provider Tele2 Netherlands by its rival, T-Mobile Netherlands. The Netherlands Authority for Consumers and Markets supported this decision. In the opinion of the EC, the acquisition would not raise any competition concerns in the EEA or any substantial part of it.

X OUTLOOK

We are cautiously optimistic with regard to Dutch M&A activity in 2019. On the one hand, funds are easily accessible due to a solid economy and low interest rates. On the other, growing protectionism and increasingly complex regulations call for caution. Businesses remain eager to do deals, whether these are transformational strategic deals, technology-driven transactions or initial public offerings. We expect technology to continue to be a key driver in Dutch M&A transactions during this year.
I OVERVIEW OF M&A ACTIVITY

There was a marked increase in M&A activity during the year in review.

The banking and financial services sectors were quite active, with several significant transactions. These included the merger of Diamond Bank and Access Bank Plc and the acquisition by Polaris Bank Limited of Skye Bank Plc, a Nigeria-based retail bank. In another deal, One Finance Limited acquired Amplified Payments Ltd, a fintech company that builds and facilitates payment solutions and digital financial transactions in Nigeria. Another notable transaction was the acquisition of Primera Africa, a top-ranked brokerage house in Nigeria by EFG Hermes, a leading financial services corporation, as part of EFG Hermes’ strategy to penetrate frontier and emerging markets. LeapFrog Investments, an emerging market-focused private equity fund, has taken up a stake in ARM Pension managers, one of Nigeria’s foremost pension management companies.

In the manufacturing sector, the Coca-Cola Company recently completed the acquisition of a 100 per cent stake in CHI Limited, one of Nigeria’s foremost fruit juice and drinks manufacturers.

Other significant transactions include Jiji’s acquisition of its rival in the online marketplace sector, OLX, in a bid to extend the company’s footprint in Africa, and Helios Investment Partners’ acquisition of Axxela Limited, a Sub-Saharan African gas and power company.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The laws that regulate M&A activity in Nigeria are the Investments and Securities Act (ISA), the Companies and Allied Matters Act, the Rules and Regulations of the Securities and Exchange Commission (SEC) and, more recently, the Federal Competition and Consumer Protection (FCCP) Act. Amendments were made to the SEC Rules and Regulations in 2017 and 2018.

Prior to the enactment of the FCCP Act, the role of the SEC was to review proposed M&A transactions to ascertain whether a proposed transaction would result in substantial restraint of trade. The implications of the new Act are discussed in Section 3. The Nigerian Stock Exchange also plays a significant role in M&A involving publicly quoted companies that are required to comply with its listing requirements.
Sector-specific laws also regulate M&A transactions in certain sectors. For example:

- the Banks and Other Financial Institutions Act and the Central Bank of Nigeria’s Guidelines and Incentives on Consolidation in the Banking Industry are relevant to M&A in the banking sector;
- the Nigerian Communications Act regulates the telecommunications sector;
- the Electric Power Sector Reform Act regulates the electricity sector; and
- the National Insurance Commission Act regulates the insurance industry.

These sector-specific laws operate in addition to the provisions of the ISA, the Companies and Allied Matters Act, the FCCP Act and the SEC Rules and Regulations.

The Companies Income Tax Act also requires the consent of the Federal Inland Revenue Service (FIRS) for a proposed merger or acquisition in relation to the capital gains tax payable. Common law applies to the extent that there is no relevant provision in the statutes.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

The SEC was the primary regulator with powers of oversight over all M&A transactions involving both private and publicly quoted companies. However, in January 2019, the Federal Competition and Consumer Protection Act 2019 entered into force. The Act repealed the Consumer Protection Council Act, dissolved the Consumer Protection Council and established the Federal Competition and Consumer Protection Commission (FCCPC) in its stead. Consequently, the SEC’s powers of oversight and approval of M&A are now vested in the Commission. Rules and regulations governing M&A under the new Act have not been released, and it is unclear whether the extant SEC rules will continue to be applicable during the transition period.

There are some concerns regarding how the FCCPC proposes carrying out its oversight functions over M&A activities in Nigeria. For example, guidance is required as to how the new provisions relating to registration of indirect transfers would be implemented. There are also concerns regarding the role of the Federal High Court under the Act.

On a positive note, the Corporate Affairs Commission, which is the main regulatory body for corporate organisations generally, has introduced various measures to make the companies’ registry more efficient, including the creation of the Companies Registration Portal to facilitate online registration of companies. Additionally, the National Assembly has passed a bill to amend the current Companies and Allied Matters Act; the Bill is currently awaiting presidential assent. Highlights of the Companies and Allied Matters Bill include the introduction of single member companies, which allows for the formation of private companies with only one member. Under the Bill, small companies can carry on business with only one director, and are exempted from the requirement to appoint a company secretary and to hold annual general meetings.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

M&A activity in the past was fuelled by investors’ desire to participate in Nigeria’s rapidly developing economy. However, recent uncertainty surrounding the foreign exchange regime, coupled with slower economic growth and the emergence of other frontier markets, led investors to become more cautious with Nigerian investments. More recently, interest in
investment in Nigeria has been revived. This is partly connected to the devaluation of the naira, which enabled foreign concerns to acquire Nigerian interests at a much cheaper rate. The increasing stability of the foreign exchange regime has also had a positive effect on portfolio investment and foreign direct investment.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

Arguably the biggest deal for the period under review was the acquisition of Primewaterview Holdings Nigeria Limited, a large-scale holding company with interests in real estate, oil and gas, health and power, for US$1 billion by Milost Global Incorporated in conjunction with, Isilo Capital Partners (its African subsidiary). This was reported to have been the largest deal in Sub-Saharan Africa in the first half of 2018. The year under review also saw the completion of 9mobile’s acquisition by Teleology Holdings Limited after the Nigerian Communications Commission, the regulator of the Nigerian telecommunications sector, approved the transaction.

Other significant deals include the acquisition of Mimee Noodles, the food division of May and Baker Limited, by De-United Foods Industries Limited, makers of Indomie noodles, in a 775 naira million deal. Another notable transaction was the acquisition of a 75 per cent stake in Forte Oil Plc by Ignite Investments and Commodities Limited, a subsidiary of Prudent Energy and Services Limited.

In the e-commerce sector, Zinox Technologies acquired a 99 per cent stake in Konga, the largest online mall in the country. Shortly thereafter, Konga merged with Yudala to form what is now the largest online mall in Africa.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

The cost of locally sourced debt funding for acquisitions is very high, with interest rates typically above 20 per cent. As a result, the vast majority of acquisitions in Nigeria are funded using cash reserves while the rest are funded with equity or debt, especially foreign-sourced debt.

VII EMPLOYMENT LAW

There have been no recent changes to employment law that are relevant to M&A. The statutes governing this are the Labour Act, the Pension Reform Act and the Personal Income Tax Act.

The Labour Act provides that the transfer of any contract from one employer to another shall be subject to the consent of the worker and the endorsement of the transfer of the contract by an authorised labour officer.

VIII TAX LAW

Although the legal regime has not necessarily changed, it should be noted that during the year under review there was increased activity by the FIRS, indicating the government’s intention to widen the tax net and increase revenue generated from taxes. This development would also mean increased scrutiny over M&A transactions to ensure that the applicable taxes are properly assessed and paid. Thus, potential investors would have to undertake thorough due diligence exercises to ascertain the amounts of back taxes for which a target asset is liable.
No merger, takeover of any form or acquisition should be undertaken by a company without obtaining prior direction as to the manner of assessment of its taxable income. Directions are obtained from the FIRS.

The tax considerations will depend on the manner in which a combination is structured. If a transaction involves an asset acquisition, the company disposing of the asset would be liable to pay capital gains tax of 10 per cent on the gains realised on the disposal. If the combination is effected by an acquisition of shares, no capital gains tax will be payable, because the Capital Gains Tax Act exempts gains accruing on the disposal of stocks and shares from tax. For tax purposes, the value of an asset transferred between connected companies is deemed to be the amount equal to the residue of the qualifying expenditure. Clearance should also be obtained from the FIRS with respect to any capital gains tax that may be due and payable as a result of the business combination.

Another relevant tax, stamp duties, is charged at a flat rate of 0.75 per cent of the value of any newly issued capital.

IX COMPETITION LAW

The Federal Competition and Consumer Protection Act received presidential assent in early 2019. The Act aims to promote competition, curb restrictive trade practices and protect the interests of consumers. The Act establishes the FCCPC, which is now responsible for the approval of M&A. The Act divides mergers into small and large mergers, but does not set a threshold for determining which mergers fall into these categories. The newly established FCCPC is responsible for setting the thresholds for each category by regulation but is yet to do so.

The FCCPC is expected to issue regulations that would replace the SEC Rules and Regulations to provide further guidelines for the M&A space in Nigeria.

X OUTLOOK

We expect to see more M&A deals in sectors with a high potential for growth, especially the financial services, retailing and fast moving consumer goods sectors. Additionally, we expect to see continued activity in the technology, media and telecommunications space, as well as the financial technology sector, which appears to be a fast-developing area. The e-commerce space also shows a lot of potential for M&A activity in the wake of Konga’s acquisition by Zinox Group and the subsequent merger with Yudala.

The National Association of Securities Dealers (NASD) provides a platform for trade in the securities of unlisted public companies, thereby allowing companies to raise capital without being listed on the Nigerian Stock Exchange. The platform provided by the NASD is instrumental in improving liquidity and facilitating private equity exits. FMDQ OTC Securities Exchange, registered by the SEC, is a securities exchange for debt capital, foreign exchange and derivatives. Its focus is on deepening the financial market and acting as a self-regulatory organisation for over-the-counter markets.

The Central Bank of Nigeria has made moves to mitigate the effects of persistent foreign exchange challenges. The most recent of these moves is the introduction of the investors’ and exporters’ FX window in a bid to improve liquidity. Transactions under this window are to be determined on a ‘willing buyer, willing seller’ basis. Experts believe this policy will encourage foreign investment in the equity and bond markets and, on this basis, we anticipate new deals.
across several sectors. The reappointment of the Central Bank of Nigeria governor for another five-year term suggests that investors can expect some consistency in the monetary policy and foreign exchange regime in the years to come.

In July 2018, the President of Nigeria signed an executive order aimed at preventing persons found guilty of corruption from continuing to control assets acquired from the proceeds of corrupt activities. Additionally, the Presidential Enabling Business Environment Council introduced several initiatives geared towards improving the business environment in Nigeria. Such initiatives include the introduction of simplified registration procedures for new businesses and the development of an online platform for payment of stamp duties. We expect that, following the general elections, recent regulatory changes and the government’s commitment to improving the business environment, investor confidence will improve, and with that, M&A activities will continue to increase.
I OVERVIEW OF M&A ACTIVITY

After an all-time high for M&A in 2017 easily topping even the pre-financial crisis level, the Norwegian M&A fell back throughout 2018, although deal volumes still reached the second-highest level ever recorded, only surpassed by 2017. In terms of the number of transactions, 2018 ended approximately 21 per cent down as compared with 2017.

There were 61 M&A transactions announced in Norway in Q1 2019, which is a 9.84 per cent increase in volume compared with Q1 2018. The strong Norwegian deal volume comes despite a decline in global deal volumes observed in Q1 2019. The total reported deal value for Q1 2019 ended at €2,982, which is also significant increase from the total reported deal value for Q1 2018 of €1,050 million.

The deal pipeline continues to be fairly strong, with an increasing number of respondents planning divesting parts of their business operations in the next couple of years. We also continue to see strong deal drivers, such as technological innovations and digital disruption both in Norway and the global markets in general. There were a few notable transactions during Q1 2019, in particular Nasdaq’s €687 million voluntary offer to acquire Oslo Børs VPS Holding ASA, a Norwegian group that offers marketplaces for listing and trade in securities, registration of ownership and settlement of securities in Norway, market data and online solutions.

Eight of the 10 largest disclosed Norwegian M&A deals in 2018 had industrial or strategic investors on the buy side. The private equity (PE) transaction volume for 2018 declined (9.7 per cent compared with 2017’s figures) but we witnessed an increase in new investments and add-ons compared with 2017, while the number of PE exits was down.

Transaction data from Mergermarket for the first four months of 2019 reveal that the volume of Norwegian transactions continues to increase compared with the same period in 2018. As at the end of April 2019, 79 transactions with a total value of €6.65 billion had been reported, whereas for the same period in 2018 there were 68 transactions with a total reported value of €1.23 billion. During April 2018, the Norwegian market also witnessed a few additional notable M&A deals, of which Hg Capital’s acquisition of an additional stake in Visma AS, from Cinven and Canada Pension Plan Investment Board for €750 million is among the most notable. Partners Group Holding AG’s acquisition of CapeOmega AS for €1.2 billion is also worth mentioning.

During the past few years, a large part of Norwegian deal volume has come from inbound cross-border deals, and during the first four months of 2019, inbound cross-border
Norway

deals comprised 49 per cent of the total number of transactions. This is a slight increase in percentage compared with inbound cross-border transactions in the first four months of 2018, which accounted for 47 per cent of the total deal volume. This shows that many Norwegian businesses possess technology and knowledge that foreign investors continue to consider attractive, in particular from a bolt-on acquisition perspective.

There has not been much change in the market for M&A deals. Nevertheless, large auction processes continue to be slightly less common than they were 48 months ago. In the past two to three years, we have observed an increase in the use of more tailored sales processes, particularly within the oil and gas segment, involving one or a very limited number of participants rather than full auction processes.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Limited Liability Companies Act (1997), the Public Limited Liability Companies Act (1997) and the Partnership Act provide the fundamental statutory framework and, with the Contract Act (1918) (which applies to almost any kind of contract) and the Norwegian Sales of Goods Act (1988), form the legal basis for the purchase and sale of corporate entities.

Public companies whose securities are listed on the Oslo Stock Exchange (OSE) or another regulated market in Norway are additionally regulated under the Securities Trading Act (2007) (STA) and the Securities Trading Regulation (STR). These rules regulate prospectus and information requirements, establish a regime to prevent market abuse and insider dealing, and set out more detailed regulations with respect to tender offers involving listed shares under Norwegian law. These statutes are supplemented by, inter alia, guidelines and recommendations issued by the OSE, and the rules and regulations of the OSE. Mergers and takeovers of private companies and unlisted public companies have no equivalent regulations. Anyone familiar with M&A transactions in most other parts of Europe will find the Norwegian landscape relatively familiar, in particular with respect to public takeovers. Norway is part of the European Economic Area (EEA) and has therefore implemented the EU regulations of relevance to companies with publicly traded securities, including the Prospectus Directive, the Takeover Directive, the Transparency Directive, the Market in Financial Instruments Directive (MiFID) and the Market Abuse Directive.

The Competition Act (2004) gives the Norwegian Competition Authority (NCA) the power to intervene against anticompetitive concentrations. Companies that are active in the Norwegian market (generally in larger transactions) must also abide by the merger control provisions set out in the EEA agreement; however, the one-stop shop principle prevents duplication of the competence of the European Commission, the European Free Trade Association (EFTA) Surveillance Authority and the NCA.

The remainder of this section describes the key rules applicable to public takeovers and certain particular issues arising under Norwegian law.

i Stakebuilding in public traded companies: disclosure obligations

No limits exist regarding the speed at which a stake can be built. Norwegian law contains a limited set of provisions governing stakebuilding, but insider dealing rules, disclosure requirements and mandatory bid rules must also be observed.

Any persons owning shares in a company whose securities are listed on a Norwegian regulated market (OSE or Oslo Axess) must immediately notify the company and the OSE if their proportion of shares or rights to shares in the company reaches, exceeds or falls
below any of the following thresholds: 5, 10, 15, 20 or 25 per cent, one-third, 50 per cent, two-thirds or 90 per cent of the share capital, or a corresponding proportion of the votes, as a result of acquisitions, disposal or other circumstances. Specific rules apply with regard to the calculation of voting rights and share capital. Breaches of these disclosure rules will frequently result in fines, which are increasing in severity.

Certain types of convertible securities, such as subscription rights and options, are counted when calculating whether a threshold requiring disclosure has been reached; however, see Section III.i with regard to certain proposed changes in this regard. It is possible, and to some extent customary, to seek irrevocable undertakings or pre-acceptances from major shareholders as well as from key or management shareholders during a stakebuilding process, prior to announcing a mandatory or voluntary bid. Such irrevocable undertakings are typically either drafted as soft irrevocables or hard irrevocables. The latter are irrevocable undertakings to sell the shares regardless of whether a subsequent competing higher bid is put forward. Soft irrevocables will normally be limited to a commitment to accept the offer provided that no higher competing bids are made. There are no particular disclosure requirements for such undertakings, other than the general disclosure obligations and the disclosure obligations regarding options and similar instruments as part of stakebuilding, which, however, may imply early disclosure of the undertakings owing to the low thresholds set out by law. In Norwegian legal theory, it has so far been assumed that the disclosure requirements will not be triggered by properly drafted soft irrevocable undertakings.

Notification must be given as soon as an agreement regarding acquisition or disposal has been entered into. Crossing one of these statutory thresholds requires disclosure even if it is passive (i.e., caused by changes in the share capital of the issuer where the person crossing the relevant threshold does not acquire any shares or rights to shares or to dispose of any shares). In such cases, notification must be given as soon as the shareholder becomes aware of the circumstances causing the shareholder’s holdings in the company to reach, exceed or fall below the relevant thresholds. Consolidation rules apply, and require the consolidation of shares held by certain affiliates and closely related parties. Hence, the combined holdings of the acquirer or the disposer, or of both, and of a party’s close associates, are relevant when deciding whether any disclosure obligations have been triggered.

**Mandatory offers**

If a stake of one-third or more of the votes is acquired (directly or indirectly, or through consolidation of ownership) in a Norwegian target company whose shares are listed on a Norwegian regulated market, but also in, inter alia, foreign companies listed in Norway but not in their home country, a mandatory offer to buy the remaining shares must be made. Certain exceptions do apply, the most practical of which is when the shares are acquired as consideration in mergers and demergers. In practice, a mandatory offer usually follows a voluntary offer, triggered by the voluntary offer reaching the mandatory offer threshold. The offeror is further obliged to make subsequent mandatory offers when, as a result of an acquisition, the offeror passes a threshold of 40 or 50 per cent of the voting shares of the company.

Regarding consolidation rules, note that certain derivative arrangements, such as total return swaps, may be considered as controlling votes for the purpose of the mandatory offer rules. A voluntary offer will also be subject to certain provisions of the mandatory offer
requirements if the offer – if accepted – may take the offeror above the thresholds for a mandatory offer. This means that a voluntary offer document for all the shares in a listed company must, inter alia, be approved by the OSE before the offer is made public.

After entering into an acquisition agreement that will trigger a mandatory offer, the acquirer shall immediately notify the target company and the OSE about whether it will make an offer or sell the shares. It is possible to avoid the obligation to make an offer if the acquirer sells the shares that exceed the relevant threshold within four weeks. After announcing that an offer will be made, the announcement may not thereafter be changed to an announcement of sale.

The offeror must then prepare an offer document to be approved by the OSE before it is issued. In practice, the approval procedure takes one or two weeks, or longer if there are difficult issues to deal with or if the OSE finds errors within the offer document. In a mandatory offer document, the offeror must give a time limit of between four and six weeks for acceptance by the shareholders.

The share price offered in a mandatory offer must be equal to the highest price paid by the offeror (or agreed to be paid by the offeror) for shares (or, under the relevant circumstances, rights to shares) in the target company during the previous six months. According to the STA, the takeover authority may invoke that the offer must be based on market price if it is clear that the market price at the time the offer obligation was triggered was higher than the highest share price the bidder paid or agreed to pay. However, a 2010 EFTA court ruling found that this rule did not comply with the EU takeover rules, as it does not provide sufficient guidance on the method concerning how the market price is to be calculated. It has been assumed that the Norwegian legislator is most likely to seek to revise the relevant provision of the STA to meet the requirements of the EU takeover rules. However, this provision has not yet been amended.

A mandatory offer must be unconditional and apply to all issued shares in the target company, and the consideration needs to be in cash; however, it is possible to offer alternative forms of consideration under a mandatory offer (e.g., shares in the offeror) provided that an option to receive the total offer price in cash is also made, and this option is at least as favourable as the alternative consideration. The consideration offered must be unconditionally guaranteed by either a bank or an insurance undertaking authorised to conduct business in Norway.

If the offeror acquires more than 90 per cent of the shares and the capital of the target company, squeeze-out rights will be available.

### Voluntary offers

In a voluntary tender offer (VTO) or exchange offer for a listed company, there is in general no limitation under Norwegian law as to which conditions the offer may contain. A VTO may be launched at the offeror’s discretion. The offeror may also choose to make the offer to only some shareholders. Conditions such as a certain level of acceptance from existing shareholders (90 per cent or two-thirds of the shares and votes), regulatory or competition approvals, completion of satisfactory due diligence and a no material adverse change clause are regularly included in Norwegian VTO documents. To complete the transaction quickly or to avoid competing bids, in some cases the offeror may decide to include very few conditions. In other cases, an offeror may decide to include more extensive conditions. In a VTO, the offeror can offer consideration in shares or other non-cash forms, or a combination, also with
Norway

cash as an element. In principle, it is also possible to make a voluntary offer conditional upon financing, but the offer document must include information on how the acquisition is to be financed.

There are no provisions regarding minimum consideration in a VTO under Norwegian law, but in general a shareholder may expect to achieve a premium of 20 to 40 per cent compared with the current share price. In recent years, there has been considerable variation in the level of premiums offered in VTOs, with some examples of premiums of around 60 per cent compared with the average in the preceding 30 days.

If a VTO is accepted and brings the offeror control over voting rights so that it triggers an obligation to issue a subsequent mandatory offer, several of the obligations relating to mandatory offers will also apply, including an obligation of equal treatment of shareholders. Under these circumstances, the VTO document must first be approved by the OSE, but the offeror is still free to decide which conditions the voluntary offer may contain. The mandatory offer requirements will not apply if the offeror has reserved the right to refuse or reduce acceptance if the offer gives the offeror at least one-third of the voting rights, or if the offer is addressed specifically to certain shareholders without it being made simultaneously or in conjunction and with the same content.

The offer period for a VTO is between two and 10 weeks, and four weeks frequently used as the initial offer period.

iv  Standstill
The target company is allowed to take a more or less cooperative approach in a takeover situation. However, there are restrictions on the board of the target company taking action that might frustrate the willingness or otherwise of an offeror to make an offer or complete an offer that has already been made. These restrictions apply after the target has been informed that a mandatory or voluntary offer will be made. During this period, the target company may, as a main rule, not issue new shares or other financial instruments, merge, or sell or purchase material assets or shares in the company. These restrictions do not apply to disposals that are part of the target’s normal business operations or when a shareholders’ meeting authorises the board or the manager to take such action with takeover situations in mind. As a result of this, a considerable number of Norwegian-listed companies have adopted defensive measures aimed at preventing a successful hostile bid.

The Norwegian Competition Act provides that all transactions fulfilling certain thresholds must be notified to the NCA, and that completion is suspended until clearance.

v  Squeeze-out
It is rare that an offeror can expect to acquire 100 per cent of the shares and votes in the target company through a voluntary or mandatory offer process; however, if the offeror is able to acquire more than 90 per cent of the shares and voting rights, it has the right to acquire (squeeze out) the remaining shares even if the minority shareholders refuse.

The Limited Liability Companies Act and the Public Limited Liability Companies Act provide that if a parent company, either solely or jointly with a subsidiary, owns or controls more than 90 per cent of another company’s shares and voting rights, the board of directors of the parent company may, by resolution, decide to squeeze out the remaining minority shareholders by a forced purchase at a redemption price. Minority shareholders have a corresponding right to demand the acquisition of their shares by a shareholder with a stake of more than 90 per cent of the company’s shares.
The resolution shall be notified to the minority shareholders in writing and made public through electronic notification from the Norwegian Register of Business Enterprises (the Register). A deadline may be fixed, which must be at least two months after the date of electronic notification from the Register, within which the individual minority shareholders may make objections to or reject the offered price. The acquirer becomes the owner of (and assumes legal title to) the remaining shares immediately, following a notice to the minority shareholders of the squeeze-out and the price offered, and the depositing of the aggregate consideration in a separate account with an appropriate financial institution.

If any minority shareholders do not accept the redemption price per share offered, they are protected by appraisal rights that allow shareholders who do not consent to seek judicially determined consideration for their shares at the company’s expense. The courts decide the actual value of the shares. In determining the actual value, the starting point for the court will be to establish the underlying value of the company divided equally between all shares. However, if the squeeze-out takes place within three months of the expiry of the public tender offer period for a listed company, then the price is fixed on the basis of the price offered in the tender offer unless special grounds call for another price.

Provided that the conditions for a squeeze-out are met, it is a straightforward process to have the target company delisted from the OSE or Oslo Axess. However, if these conditions are not met, it could be substantially more challenging to delist the target company even when the offeror has managed to acquire more than 80 per cent of the votes.

vi Statutory mergers

Subject to the approval of the majority of two-thirds of the votes and the share capital represented at a general meeting of shareholders, Norwegian limited liability companies (LLCs) may merge, creating a company (the surviving company) that takes over all assets, rights and obligations of one or more assigning companies (the surrendering company or companies). The articles of association of a company may provide for a higher majority threshold, but may not set a lower one. Under a statutory merger, the shareholders of the surrendering company have to be compensated by way of shares in the surviving company, or by a combination of shares and cash, provided that the amount of cash does not exceed 20 per cent of the aggregate compensation. If the surviving company is part of a group, and if one or more of the group companies hold more than 90 per cent of the shares and the votes of the surviving company, compensation to the shareholders of the surrendering company may consist of shares in the parent company or in another member of the surviving company’s group. It is further possible to effect a merger by combining two or more companies into a new company established for the purpose of the merger. After completion of a statutory merger, any surrendering companies are dissolved.

Under Norwegian law, a statutory merger will be considered as a continuation of the companies involved in the merger, implying that the transaction does not represent an assignment of the original companies’ rights and obligations.

Certain formalities need to be observed to complete a merger under Norwegian law. A joint merger plan describing the general terms of the merger has to be prepared and negotiated between the surviving and surrendering companies. The joint merger plan must be signed by the board of directors prior to the general meeting of shareholders resolving to approve the merger plan. The board of directors, after signing the joint merger plan, have to issue a report to the shareholders explaining the reasoning behind the merger, and how, inter alia, this may affect the company’s employees. If a public LLC (ASA) is involved in a legal merger there are
more detailed requirements for the content of the report. In addition, each of the participating entities’ boards shall ensure that a written statement containing a detailed review of the merger consideration payable to the shareholders of the participating companies is issued, including an opinion of the fairness of the consideration. This statement is to be prepared and issued by an independent expert (such as an auditor) when the participating entity is an ASA. When the participating entity is a private limited company (AS), the statement may be issued by the board and confirmed by the company’s auditor. The resolution to merge the companies must be reported to the Register within certain time limits to avoid the resolutions being deemed void. The shares used as consideration to the shareholders in the surrendering company are issued according to the rules applicable to a capital increase.

Since Norway implemented Directive 2005/56/EC, it is further possible to conduct a statutory merger of a Norwegian company cross-border within the European Union and the EEA; however, public tender offers and other offer structures are often used instead of a statutory merger, which cannot be used by foreign companies (outside the European Union or the EEA), allows only 20 per cent of the consideration to be given in cash, requires more formalities and documentation, and normally takes longer to complete than a public offer. Still, a statutory merger may be suitable when an exchange offer mechanism would not procure complete control under one corporate umbrella, and if there is not enough cash available to effect a mandatory offer and squeeze out the minority shareholders.

Statutory mergers are generally not regulated by the STA’s public takeover rules; however, transactions that are similar in form to mergers (share-for-share exchanges) but whose structures do not meet the formal requirements for a merger under Norwegian legislation, may be subject to the STA’s takeover rules if the target company’s shares are listed on the OSE.

vii Employee board representation
In both ASAs and ASs, employees are entitled to be represented on the board of directors, provided that the number of full-time employees in a company exceeds 30. Under these circumstances, employees will be entitled to elect between one and up to one-third of the members of the board from among the employees. The exact number of employee representatives on a board varies according to the number of employees in the company. Employee representatives will have the same voting rights as the other board members. Employee board representation is not mandatory under Norwegian law, but cannot be rejected if requested by employees when the conditions for representation are fulfilled.

A bidder should note that the employees of a Norwegian subsidiary may also demand to be treated as employees at the Norwegian parent or sub-parent level, thus obtaining representation on the board of directors of the Norwegian parent or sub parent.

viii Requirements of residency
The chief executive officer and at least 50 per cent of the members of the board of directors must be residents of Norway, unless the Ministry of Trade, Industry and Fisheries grants an exemption in an individual case. These residence requirements do not apply to citizens of an EEA Member State, provided the board members are residents of an EEA Member State.
Gender requirements
For public LLCs, Norwegian law imposes a requirement that both genders shall be represented on a board of directors. As a main rule, each gender must be represented by at least 40 per cent on the boards of directors of public companies. Consequently, on a board of five directors there cannot be fewer than two members of each gender. Exceptions apply to the directors elected from among employees. The obligation to have both genders represented on the board does not apply to Norwegian private LLCs.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

EU initiatives
Several new EU directives, regulations and clarification statements regarding the capital markets are proposed or have been implemented in recent years. Norway will have to adopt and implement some of these to comply with its obligations under the EEA agreement. These EU initiatives are likely to have a direct or indirect impact on the regulatory framework for public M&A transactions in Norway. As a result of these initiatives, several amendments to the STA are expected to take place during the next 12 to 24 months.

The government appointed an expert committee to evaluate and propose relevant amendments to existing Norwegian legislation resulting from amendments to the Transparency Directive, MiFID I and the Market Abuse Directive. The committee was mandated to prepare three separate reports to the government. All three reports have now been delivered. The first report, inter alia, proposes implementing certain amendments to the STA with regard to disclosure requirements for derivatives with shares as underlying instruments. According to the proposal, the materiality thresholds and disclosure requirements that apply for acquisition of shares in listed companies shall now also apply for derivatives with shares as underlying instruments, irrespective of such equity derivatives being cash-settled or settled by physical delivery of the underlying securities.

The committee further proposes that both borrowing and lending of shares shall become subject to the same notification regime for both the lender and the borrower. Soft, irrevocable undertakings will remain exempt from the disclosure obligations. The existing disclosure obligations under the STA also include an obligation to disclose information in relation to rights to shares, regardless of whether the shares already have been issued or not. This is a stricter disclosure and filing obligation than what follows from the minimum requirements set out in the Transparency Directive, and the committee has proposed that the obligation be abolished. If adopted by Parliament, Norwegian law will no longer have mandatory disclosure obligations for warrants and convertible bonds not linked to any issued (existing) shares.

The second report, published in January 2017, proposed, inter alia, further amendments to the STA to implement MiFID II and MiFIR into Norwegian law. In April 2018, the Ministry of Finance issued a white paper to Parliament based on the committee’s second report. In June 2018, Parliament resolved to implement these proposals into Norwegian law, but the changes do not contain amendments that are directly relevant for the bidder or target in an M&A process.

The third report deals with the implementation of the Market Abuse Regulation and includes proposals under which the STA rules governing market abuse have been expanded. These include, among others, a proposal for new rules concerning market sounding that
occurs in preparations for a potential transaction. It is also proposed that primary insiders will be personally obligated to publish information about their trading activities in listed financial instruments.

The fourth report was published in January 2018 and concerns the implementation of supplementary regulations regarding MiFID II and MiFIR.

Finally, a fifth report was published in June 2018 concerning the implementation of the new Prospectus Regulation and rules regarding national prospectus requirements.

ii New takeover rules expected

In addition to the five reports referred to above, on 23 January 2019, the Committee has also submitted a report concerning the Norwegian rules on voluntary and mandatory offers, with a particular focus on the current limited regulation of the pre-offer phase. This Committee report does not arise out of changes to EU rules, but rather the need to review and update the Norwegian takeover rules on the basis of past experience and market developments.

In its report, the Committee proposes, inter alia, a new requirement that a bidder must carry out certain preparations before it announces that it will launch an offer to acquire a listed company. The Committee also proposes new content requirements for a notification that a voluntary offer will be made, including information on matters of importance for the market’s assessment of the offer and for the formation of the price. It is proposed that it be clarified that the Norwegian Takeover Supervisory Authority (now the OSE) shall publish such notification immediately. Furthermore, a new requirement is proposed that bidders must present a voluntary offer no later than four weeks from the publication of the notice announcing that an offer would be issued. At the same time, it is proposed that the Takeover Supervisory Authority may grant an exemption from this deadline in special cases. The Committee proposes that the minimum length of the offer period in voluntary offers be extended from at least two to at least four weeks.

Is proposed that the existing main rule that the offer price under a mandatory offer must correspond to the highest consideration paid or agreed by the bidder in the last six months before the mandatory offer obligation being triggered be continued. However, the Committee proposes a separate regulation setting out rules for calculating the offer price in cases where there is a need for an exception from the above main rule or where it is not possible or reasonable to use the main rule for calculating the offer price. In this regard, it is also proposed that the offer price should be adjustable if the Takeover Supervisory Authority considers that the stock prices during the period in question are being kept at an artificial level, the stock purchase that is the basis for the offer price was not made on normal commercial terms or the mandatory offer obligation is being triggered in connection with a restructuring of a company in serious financial distress. In that case of adjustments of the offer price where stock prices have been kept at an artificial level, or where the stock purchase that is the basis of the offer price was not made on normal commercial terms, the Committee proposes that the adjusted offer price shall be calculated on the basis of three-month volume-weighted average stock prices.

Further, the Committee proposes introducing a general requirement that information published on a planned or submitted takeover offer must be correct, clear and not misleading. The scope of application is intended to be broad, and comprises the preparation phase, the phase after a bid is launched and the bidding phase.
The Committee also proposes a new right for the accepting stockholders to revoke their acceptances for a period limited to three trading days after a competing offer is made and disclosed, provided this occurs during the offer period for the original (first) offer.

Furthermore, the Committee proposes new rules on amending a tender offer, so that a bidder prior to the expiry of the offer period may amend the terms of such an offer in favour of the stockholders and also extending the offer period, provided the bidder has reserved such rights in the offer document itself and that such amendments are approved by the Takeover Supervisory Authority.

The Committee does not propose to implement rules regulating the type of transaction agreements used in connection with takeovers of listed companies or similar commitments between a bidder and a target company. Nevertheless, it proposes implementing a rule into the new legislation that authorises the government to issue more detailed rules in a separate regulation to govern the use of such agreements in connection with mandatory and voluntary offers.

It is also proposed that the takeover rules are amended to clarify the scope and applicability of such rules on companies domiciled in another country having issued stocks traded on a Norwegian regulated market. Further, the introduction of an obligation for companies domiciled outside the EEA is proposed to ensure that, if such non-EEA company’s stocks are listed on a Norwegian regulated market, the company will have a special obligation to provide information on its website about the rights of its minority stockholders.

According to the proposal, the Takeover Supervisory Authority will be authorised to issue fines of up to 10 million kroner for natural persons and up to 20 million kroner for legal entities for violation of a number of key rules, or up to 2 per cent of the total annual turnover in the last annual accounts for the same. If approved by the Parliament in its proposed form, this will, inter alia, apply to:

- the obligation to provide accurate, clear and non-misleading information in connection with an offer;
- prerequisites for presenting an offer;
- the obligation to provide notification of a mandatory offer or voluntary offer;
- the obligation to make a mandatory or voluntary offer; and
- the requirement for a minimum offer price in mandatory offers.

It is currently unclear when the Parliament can be expected to adopt these amendments into Norwegian legislation. However, we do not expect the proposed changes to be implemented into Norwegian law until 1 January 2020 at the earliest.

iii Expected amendments to the prospectus regime

In June 2017, the EU adopted a new Prospectus Regulation to improve the existing prospectus regime. The Regulation replaces the Prospectus Directive. Both the Prospectus Directive and the existing Prospectus Regulation are implemented in Norwegian law, and the rules are set out in the STA and the STR. The requirement of a prospectus or equivalent

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document will no longer apply to securities offered in connection with a takeover by means of an exchange offer, merger or division, provided a document is made available that contains information describing the transaction and its impact on the issuer. On 19 June 2018, a government-appointed expert committee delivered a new report in which it proposed amending the prospectus rules in the STA and STR by implementing the new Prospectus Regulation into Norwegian law. From such time that the new rules are finally implemented into Norwegian law, the requirement of a prospectus or equivalent document will no longer apply to securities offered in connection with a takeover by means of an exchange offer, merger or division, provided a document is made available that contains information describing the transaction and its impact on the issuer. It is currently unclear when Norway will be able to finally implement the new Prospectus Regulation into Norwegian law.

iv  New National Security Act

In March 2018, the Parliament adopted a bill for a new National Security Act. This new Act grants the government powers to intervene and stop acquisitions of shares in a company holding investments in sectors considered vital from a Norwegian national security perspective. The new Act entered into force with effect from 1 January 2019. This means that Norway has now implemented a national security review of acquisitions that is fairly similar to the type of review conducted by the US Committee of Foreign Investments.

v  Proposed amendments to the Norwegian financial assistance prohibition

At the beginning of 2019, the Ministry of Trade, Industry and Fishery issued a consultation paper revisiting a previous Ministry proposal of February 2016 for the certain further easing of the Norwegian financial assistance prohibition rule (see below). The proposal was issued together with some other proposals to amend the rules of the Norwegian Companies Acts in order to implement EU Directive (EU) 2017/828 into Norwegian law. In the 2019 consultation paper, the Ministry once again has slightly revised its proposal to abolish the requirement that a buyer (borrower) must deposit adequate security towards a target company if the buyer receives financial assistance from the target in the form of security for the buyer's acquisition financing. If adopted in its current proposed form, Norway will finally have a type of whitewash procedure that could work also for leveraged buyout (LBO) transactions. In the past, it has been rather impractical to obtain such assistance from a target company in typical LBO transactions (see Section VI.ii). However, a proposal has not yet been put forward to Parliament, and it is too early to say whether this proposal will be forwarded to Parliament in its current form.

IV  FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Foreign nationals were relatively active in the Norwegian financial markets until a noticeable retreat in 2015, largely as a result of a collapse in oil prices. However, from 2016 and throughout 2018 foreign bidders returned and, so far in 2019, foreign appetite for Norwegian assets continues to be relatively high.

In the first half of 2018, 141 Norwegian M&A transactions were announced with a deal value of more than €5 million, of which 43.9 per cent involved foreign buyers. Overall,
in 2017, the total number of M&A transactions with a deal value of more than €5 million was at a record high of 283, of which 47 per cent involved foreign buyers. Six Seven of the 10 largest inbound M&A deals during 2018 involved foreign buyers, while eight of the 10 largest inbound PE transactions involved foreign funds investing in a Norwegian target company. Eight

See Section V for examples of inbound cross-border M&A deals during 2018.

Foreign investors’ appetite for Norwegian assets in the first four months of 2019 increased compared with the same period in 2018, both in terms of the number of deals, and the relative percentage of the total deal count for this period was also higher. Seven of the 10 largest M&A transactions involved a foreign buyer, one more than in the first four months of 2018, while for the same period in 2017, three of the 10 largest M&A transactions involved foreign buyers. For the same period, 79 Norwegian M&A transactions were announced with a deal value of more than €5 million, of which 49.3 per cent involved foreign buyers. Nine This is an increase in terms of the percentage of the total deal volume compared with 2018, in which 47 per cent involved foreign buyers. Ten In terms of the number of deals, there was an increase of 16.2 per cent in volume compared with 2018. Examples of inbound cross-border transactions so far in 2019 include Partners Group Holding AG’s €1.2 billion acquisition of a stake in CapeOmega AS, Hg Capital’s €750 million acquisition of a stake in Visma AS and Nasdag Inc’s €687 million bid on Oslo Bors VPS Holding ASA, the Norway-based group that offers marketplaces for listing and trade in securities, registration of ownership and settlement of securities in Norway, market data and online solutions.

The foreign ownership rate of shares listed on the OSE at the end of 2018, calculated by market value, was 38.5 per cent, an increase compared with 38.36 per cent in 2017, but still below the record of 40.8 per cent from 2007.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Technology, media and telecommunications

In 2018, the technology, media and telecommunications (TMT) sector was largest in terms of acquisitions in Norway, accounting for 19.8 per cent of the total deal count for the year. This represented a 2.9 per cent increase in deal volume compared with 2017. However, the rise in percentage within this sector was due to a decreasing deal volume in other sectors for 2018, and the actual number of deals within the TMT sector in terms of volume actually remained flat, with a zero per cent increase compared with 2017. The strength of M&A activity during 2018 within this sector continued to be driven by global trends such as digitalisation, AI, the IoT, data analytics, infrastructure light business models and augmented reality. The increase in average deal value within the TMT sector also continued to increase in 2018. The most notable transaction in 2018 was Telia Company AB’s acquisition of GET AS, an Oslo-based provider of subscription programming services, from TDC A/S for €2.2 billion in cash. The transaction was to include TDC Norway. Other significant deals were EQT’s €440 million sale of Tampnet AS, a Norway-based provider of satellite telecommunications services, to an investor group composed of Arbejdsmarkedets Tillaegspension (50 per cent) and 3i

6 Source: Mergermarket.
7 Ibid.
8 See footnote 5.
9 Ibid.
Infrastructure PLC (50 per cent), and Orange’s acquisition of BaseFarm AS, a Norway-based hybrid cloud and big data technology solution provider from ABRY Partners, for around €350 million.

As in previous years, the majority of deals in this sector were rather small, since several target companies originate from venture capital (VC) investments reaching a stage in their development where investors are seeking an exit. Since the post-crisis cooldown, there has been relatively moderate interest in VC investments in the Norwegian market, which to a great extent has resulted in the VC market lagging behind when compared to more mature companies. However, the trend of more people being attracted to innovative tech investments has continued.

The volume of deals within the TMT sector accounted for 22.8 per cent of the total deal volume during the first four months of 2019. However, with the exception of Hg Capital and Canada Pension Plan Investment Board’s €750 million acquisition of Cinven’s stake in Visma AS, the transactions have been relatively small.

Based on current market sentiment, there are likely to be relatively high numbers of TMT deals throughout the remainder of 2019, thanks largely to a domino effect whereby corporates that were inactive in 2015, 2016, 2017 and 2018 will continue to replicate peer deal success and related advantages. However, there are some concerns, including that the pricing of companies within this sector has been on the rise for some time, and some commentators feel that there could be a lack of robustness for development.

**ii  Industrials and manufacturing**

The strong momentum within the industrial and manufacturing sector continued throughout 2018, accounting for 17.3 per cent of the total deal count for the year. This represented a 0.5 per cent decrease in the total deal volume compared with 2017. However, in terms of the actual number of deals, this represented a 16.9 per cent decrease compared with 2017. The strength of M&A activity during 2018 continued to be driven by this sector benefiting from a weakening Norwegian krone. However, most of the transactions were small. One exception was Qumei Investment AS’s €594 million acquisition of Ekornes, announced in May 2018. This was the seventh-largest M&A transaction concluded last year. Another notable transaction was FSN Capital Partners’ acquisition of SafeRoad AS for €244 million, also announced in May 2018.

The momentum within the industrial and manufacturing sector has continued entering 2019, with 17 deals announced in the first four months, representing 21.5 per cent of the total deal count for the period. The most notable of these deals were Tubacex SA’s acquisition of Nobu Group for €51 million in deal value and AVK International A/S’ acquisition of Furnes Jernstøperi AS, a Norway-based company engaged in the manufacturing of industrial equipment and machinery.

**iii  Services**

This was another busy sector in 2018, accounting for approximately 13.8 per cent of the total deal count. This is an increase from the 11.1 per cent of the total deal count for 2017, and the services sector was one of the most active sectors in 2018 with a total of 39 transactions, two more than in 2017. Many corporates in the business services sector continue to experience margin pressure. Technology-led disruptive innovations have the potential to transform the
way business service providers operate, with the potential for becoming more global. With opportunities for global growth, M&A delivery scale, improved geographical footprint and capability, these are considered an attractive way for creating revenue and cost synergies.

The most notable transaction within the services sector in 2018 was announced in July 2018, when ABRY Partners, a US-based PE firm, announced its $411 million bid for Link Mobility Group.

During the first four months of 2019, nine deals were related to the services sector. The most notable was the acquisition by Sumitomo Corporation, the listed Japan-based company engaged in, inter alia, imports and exports, of Q-Part Operations BV from KKR for €398 million. The deal included the target’s parking operations in Sweden, Norway and Finland.

iv Consumer
The consumer and retail sector accounted for 10.2 per cent of the total transaction volume in 2018, a slight decrease compared with 2017 (11.7 per cent). In terms of number of transactions, the sector showed a 25.6 per cent decrease compared with 2017. In May 2018, Canadian Tire Corporation, Limited announced that it had acquired Helly Hansen AS, a Norway-based designer and marketer of high-performance outdoor clothing for a total consideration of €642 million.

Other notable deals were OpenGate Capital LLC’s acquisition of Jøtul AS and Icon Capital AS’s acquisition of minority stake in MaloramaAS, Norway’s largest wholesaler and distributor of paint and coating products.
In Q1 2019, 11 out of a total number of 61 deals were related to the consumer and retail sector, five more than in Q1 2018.

v Energy (including oil and gas)
Throughout most of 2018, oil and gas prices continued to improve. However, at the end of the year prices started to slide back. Despite this, investments within the oil and gas sector continued to slowly improve throughout 2018. Overall, 11.7 per cent of all deals in 2018 were related to energy and oil services and the offshore sector, of which the oil and gas segment accounted for 7.1 per cent. The oil and gas industry continued to reconfigure its business model to sustain and grow in a lower oil price environment. Reduced oil prices until mid-2016 led to many sponsors taking an interest in exploration and production (E&P) assets at favourable prices, which continued into 2017 and 2018, resulting in increased interest in such assets in general. The most noteworthy transaction was announced in August 2018: the €805 million acquisition of Mime Petroleum, a Norwegian oil and gas exploration and production company, by Blackstone Group LP and Blue Water Energy LLP.

Notable transactions within the E&P segment included Neptune Oil and Gas Limited’s €304 million acquisition of VNG Norge AS, a Norwegian oil and gas exploration and production company, Aker PB’s acquisition of a 77.8 per cent stake in King Lear Discovery for €216 million, and Polskie Gornictwo Naftowe i Gazownictwo SA’s acquisition of a 42.38 per cent stake in the Tommeliten Alpha gas and condensate field for €192 million.

Within the electric power supply market, it was announced in June 2018 that Keskusosuuskuunta Oulun Seudun Sahko, Vantaan Energia Oy and Oy Turku Energia-Abo Energi AB had acquired a 10 per cent stake in Hafslund Produksjon AS from Fortum Oyj AB, a listed Finland-based energy group engaged in producing power from nuclear and wind
sources, for €160 million. In September 2017, it was announced that TronderEnergi Nett AS, a Norway-based company engaged in the distribution of electricity, had agreed to acquire Gauldal Nett AS from Fredrikstad EnergiNett AS for an undisclosed consideration.

In Q1 2018, two transactions were related to the oil and gas sector, which is three less than in Q1 2018. Both of these deals were in the E&P segment. However, within the oil services and equipment market segment, potential sellers continue to be reluctant to initiate sales processes, preferring to use bilateral sales processes rather than auctions. We expect that this segment will continue to improve in 2019, depending on changes in oil prices.

vi Private equity
The number of transactions involving PE sponsors either on the buy side or sell side took a dive of 9.7 per cent in 2018. Regarding buyout investments by volume, Sweden saw the highest volume with 39.5 per cent, followed by Denmark with 24.5 per cent, Norway with 18.5 per cent and Finland with 17.5 per cent.

Norway’s PE industry is largely driven by new investments and add-ons, but in 2018 there was a significant decrease in the number of exits and a slight increase in the number of new investments. Of all the transactions during 2018, half were new investments and add-ons, 9 per cent were secondary and 21 per cent were exits. However, of the deals involving PE sponsors, the average reported deal size took a significant dive from €567 million in 2017 to €249 million in 2018. Of the 10 largest disclosed transactions in 2018, all 10 had a deal value exceeding €100 million (there were nine in 2017), and two of the 10 largest announced and completed transactions involved PE.

Among the most notable PE deals in 2018 were Blackstone Group LP and Blue Water Energy LLP acquiring Mime Petroleum AS for €805 million, the sale of Helly Hansen to Canadian Tire Corporation by Teachers’ Private Capital, Limited for €698 million and T EQT Partners AB’s €440 million sale of Tampnet AS to ATP Group. In July 2018, it was also announced that Victory Partners VIII Norway, a company controlled by ABRY Partners, launched a voluntary bid to acquire Link Mobility Group ASA for €411 million. This was among the largest PE deals in the Norwegian market in 2018.

The PE market experienced a dive at the beginning of 2019, with a 26 per cent decrease in announced deals compared with Q1 2018, and also a significant decrease in average deal size. Still, PE funds continue to look actively for opportunities in the Norwegian market.

In April 2019 it was announced that HitecVision had agreed to sell CapeOmega AS to Partners Group Holding AG for €1.2 billion. Hg Capital and the Canada Pension Plan Investment Board acquired Cinven’s stake in Visma AS for €750 million, also announced in April 2019.

For the moment, it may be that PE professionals are prepared for a more challenging investment climate in 2019. Some delays and failures in deal execution as a result of market uncertainty have also started to be seen, but the pressure on PE funds to continue to put their capital to work means that deals will continue to happen. Consequently, we believe any slowdown in deal activity by PE funds is likely to be short-lived. Under all circumstances, we expect a continuing high number of PE and VC-related exits, add-ons and secondary transactions, in particular within the healthcare, industrial, TMT and consumer sectors in the next 12 to 24 months, but possibly with a drift towards more non-secular industries such as healthcare and consumer staples. The number and size of deals involving PE sponsors will depend on market developments and volatility. Some large distressed assets within the oil and gas segment may also tempt some funds into opportunistic investments.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

The high-yield bond market has recovered from a period in the doldrums and is now quite buoyant. Higher and more stable oil and gas prices, particularly during the second half of 2016 and throughout 2017 and for parts of 2018, combined with capital continuing to be inexpensive and plentiful, has contributed to a significant strengthening of the credit markets. Bidders are again considering high-yield bonds as a means of financing new acquisitions.

While some Norwegian banks continue to be selective even at the beginning of 2019, in particular for projects exposed to the oil and gas industry, the presence of alternative lenders and institutional investors in the form of collateralised loan obligations funds (CLOs) flooding the international financing markets with an ever-more borrower-friendly documentation, combined with an improved bond market, have created a very borrower-friendly environment. The trend of unitranche or term loan B-style (TLB) loans spreading globally continues and funds offering these types of loan products are marketing their products particularly towards PE sponsors.

i M&A financing

Traditionally, third-party financing of acquisitions is provided by way of bank loans. In large transactions, the senior loan will be governed either by Norwegian or English law, with one bank acting as agent for the syndicate of lenders. In syndicated transactions, the senior loan agreements used will normally be influenced by the forms used internationally, in particular the standard forms developed by the Loan Market Association. Acquisition financing (in particular for PE transactions) tends to be provided by way of two or sometimes three layers of debt, with subsequent seniority. In recent years, generally we have witnessed a greater variety of combinations of debt layers and lenders involved, especially in larger LBO transactions.

Increasing competition from the high-yield bond market, unitranche funds (see below) and mezzanine providers, which ask for high interest rates, has made mezzanine financing less competitive than other options. It is rarely seen for new deals, although some traditional mezzanine funds are starting to adapt to the new market situation by offering products similar to unitranche loans. There is an increasing use of second lien facilities instead.

Using debt securities such as high-yield (junk) bonds for acquisitions has not been common in Norway, mainly because, compared with financing an acquisition with a credit facility, financing through a high-yield bond debt involves coordinating the closing of a transaction with what is, in fact, public financing. In most cases, the acquisition will be subject to various conditions, typically including various forms of regulatory approval. Funding an acquisition through a traditional credit facility is generally more feasible than a high-yield bond. Historically, larger listed corporations have dominated acquisition financing obtained through the Norwegian bond market. Such corporations have frequently been willing to take a practical approach by issuing bonds and uploading debts on their balance sheet to have dry powder easily available for future acquisitions without necessarily having to take into consideration how to coordinate a drawdown with the conditions precedent under a pending sale and purchase agreement. Such instruments would generally be documented under New York or English law, or Norwegian law for issue in the local market. However, from 2012 to September 2014, acquisition financing raised in the Norwegian debt capital market was increasingly popular. During this period, it also became fairly common among sponsors to attempt to refinance acquisition debt post-completion by using the Norwegian
bond market. Bonds governed by Norwegian law are usually issued pursuant to the standard terms of Nordic Trustee ASA, which acts as the trustee for the majority of bonds issued by Norwegian companies.

Between May 2016 and the first half of 2019, the bond market has been improving significantly. Bidders are again raising financing in the high-yield bond market in connection with Norwegian leveraged acquisitions. We have also observed an increasing number of sponsors refinancing acquisition debt post-completion at favourable coupon rates by using the bond market. We expect that the high-yield bond market's popularity for raising acquisition financing will continue (depending on how the debt capital markets develop).

In the past year, there has been increased activity from non-bank (alternative) lenders and funds that are offering to replace or supplement traditional senior secured bank loans to finance M&A transactions. The products these lenders are offering typically include TLB facilities and unitranche loans.

Vendors may occasionally also be willing to bridge the valuation gap by offering a bidder to finance parts of the purchase price to achieve the price the vendors are asking. If structured as vendor loan notes, these will sometimes (but not always) be subordinated to the other elements of the acquisition financing. Vendor loan notes will then normally be on similar terms (or senior) to the subordinated loan or preferred equity capital provided by the PE sponsor, but are usually priced to give a lower rate of return. The split between debt finance and true and quasi-equity will be determined on a transaction-by-transaction basis, and particularly by reference to the underlying business and its funding requirements.

Other forms of debt financing that may be used in acquisitions, such as securitisations, are relatively rare in Norwegian business combinations.

ii Financial assistance and debt pushdown

A buyer may also want to borrow funds from a target company (or its subsidiaries, following completion of a transaction). While as a general rule there are no major obstacles in this regard, in an asset deal where the business assets are bought by the entity financing the deal, a debt pushdown is substantially more difficult in a share transaction. Public and private LLCs have been prohibited from providing upstream financial assistance in connection with the acquisition of shares in a target company (or its parent company).

Since 1 July 2013, the former prohibition on financial assistance has been eased by the introduction of a type of whitewash procedure. Under this rule, both private (AS) and public (ASA) limited liability target companies can, subject to certain conditions, provide financial assistance to a potential buyer of shares in the target company itself. This must be granted based on normal commercial terms and policies, and the buyer must deposit adequate security for his or her obligation to repay any financial assistance received from a target company.

Financial assistance must also be approved by the target’s general assembly by a special resolution. This requires the same support from the target’s shareholders as would be needed to amend the target’s articles of association (i.e., unless otherwise required by the articles themselves, at least two-thirds of the votes cast and the share capital represented at the general meeting). In addition, the target’s board has to prepare a special report that contains information about:

a the proposal for financial assistance;
b whether financial assistance will be to the target’s corporate benefit;
c conditions that relate to the completion of the transaction;
an assessment of the effect of the assistance on the target's liquidity and solvency; and
the price payable by the buyer for any shares in the target company or any rights to any such shares.

This report has to be attached to the notice of the general meeting sent to shareholders.

The target company's board will also be under an obligation to obtain a credit rating report on the party that is to receive such financial assistance.

The requirement to deposit adequate security for the borrower's obligation to repay any upstream financial assistance provided by a target will, however, mean that it becomes impractical to obtain direct financial assistance from the target company in most LBO transactions due to the senior financing banks’ collateral requirements in connection with such deals. Banks normally request extensive collateral packages, so in practice there will be no adequate security left, or available, from the buying company (or its parent company) for securing any financial assistance from the target group, at least for the purchase of the shares. The extent to which the offered security is adequate may mean that the target has difficulty providing upstream assistance unless the new owners, or the vendors, are able to come up with some additional collateral. Consequently, in practice, the new rules have so far had little impact on how LBO financing is structured under Norwegian law, at least in PE transactions. In most cases, the parties continue to pursue debt pushdowns by refinancing the target company's existing debt, as had previously been the case. It was proposed in 2016 that the requirement that a buyer (borrower) must deposit adequate security towards the target company be abolished. This proposal was not put before the Parliament, and at the beginning of 2019, a revised proposal was been published to abolish the adequate security requirement under Norwegian law. However, it still unclear when and if this revised proposal will be implemented. If it is adopted by Parliament, it will be possible in LBO transactions for a buyer to receive financial assistance from the target company in the form of security for the buyer's acquisition financing. (See also Section III.v.)

### Corporate benefit

The power of an entity to grant security or guarantees is limited by the doctrine of corporate benefit in some situations. Under Norwegian law, a board of directors has a general duty to act in the best interests of the company and all its shareholders. There is currently limited case law to determine the boundaries of the corporate benefit requirements, but it has been assumed that boards enjoy fairly wide discretion to consider the corporate benefit. If a board, following due consideration, concludes that a transaction is in a company's interests, it will be difficult to challenge a well-documented resolution to this effect.

However, under Norwegian law it is uncertain to what extent a group benefit is sufficient when there is no benefit to the individual group company, for example, in connection with granting a guarantee or providing a security. In principle it is assumed that a Norwegian company is able to provide upstream and cross-stream guarantees and security provided that:

- this will not jeopardise its continuing existence;
- its corporate objects are not transgressed by such transactions;
- it can be argued that cross guarantees benefiting the company exist or that the relevant group company receives any type of guarantee fees; and
- guarantees and securities are not in breach of the financial assistance propitiation (see Section VI.ii).
The Public Limited Liability Companies Act and the Private Limited Liability Companies Act now both contain a provision in Section 8-7(3) No. 3 stating that a loan or security to the benefit of another legal entity within the group is not included in the prohibition on loans or security to a company’s shareholders, provided that the loan or security will economically benefit the group. This provision indicates that a group benefit may be sufficient when issuing intragroup guarantees, even if there is no direct benefit to the individual group company that is issuing the guarantees.

The validity of a legal act entered into by a legal entity can be set aside if, as a result, its objects are transgressed and the counterparty was or ought to have been aware of the transgression. Lenders will typically require the submission of corporate resolutions in which the borrower’s board of directors confirms that the transactions contemplated by the finance documents to be entered into by the Norwegian company are beneficial to the interests of the company. On this basis, lenders can argue that they did not know or could not have known that the corporate objects had been transgressed.

iv Need for shareholder approval

Both the Public Limited Liability Companies Act and the Private Limited Liability Companies Act require that agreements between a company and a shareholder, the shareholder’s parent company, a director or the general manager, a shareholder’s related party, or someone who acts according to an agreement or understanding with any of the aforementioned parties, must be approved by the company’s general meeting if the consideration to be paid by the company has an actual value exceeding 10 per cent (AS) or 5 per cent (ASA) of the company’s share capital at the time of the transaction. It has been assumed that the rules in principle also apply to loans and guarantees, provided the interests and fees paid exceed these thresholds. If the rules apply, the board of directors must issue a report to the shareholders, including a statement that there is a reasonable correlation between the value of the consideration to be paid by the company and the value of the consideration received by it. In addition, an independent expert (ASA) or the company’s auditor (AS) must issue a statement confirming that the board’s statement is correct.

Certain exemptions apply, such as agreements entered into following the rules governing the incorporation or share capital increase against a contribution in kind, certain management remuneration arrangements, transfers made according to publicly quoted prices, and what are referred to as ‘agreements entered into as part of the company’s normal business and that contain price and other terms that are customary for such agreements’. An exemption rule now exists for intragroup agreements entered into between a parent company and a subsidiary provided that the parent owns all shares in the relevant subsidiary and the loan or security is to the benefit of the group, or the parties have adopted the new whitewash procedures relating to financial assistance.

As long as a parent company controls all shares in the relevant subsidiary issuing the intragroup loans and guarantees used, it can now be argued that there will no longer be a need for banks to request that loans and guarantees have to be approved by the shareholders. Approval may still be necessary in cases as referred to in Section VI.ii or where the parent does not control all shares in the relevant group companies issuing the loans or securities. Intragroup loans may trigger a need for shareholder approval from the receiving subsidiaries’ shareholders, unless they are entered into as part of the relevant subsidiaries’ ordinary business activity and contain prices and other terms that are normal for such agreements. In legal theory, it has been argued that intragroup loan agreements entered into in connection with M&A
transactions very often must be considered as falling outside the normal business activity of the respective company receiving the financing and, therefore, under all circumstances need to be approved by the company’s shareholders.

Note that in early 2019 the Ministry proposed amended the above statute in both the Public Limited Liability Companies Act and the Private Limited Liability Companies Act so that these rules now shall only apply to agreements between a company and its related parties, and only if the company’s consideration under such agreement has an actual value exceeding 2.5 per cent of the sum on the company’s balance sheet. It is further proposed that the board shall deal with such agreements, and must, no later than two weeks prior to such agreement entering into force, inform all shareholders about the agreement, and each shareholder shall then be entitled to require that the agreement must be dealt with at a shareholders’ meeting.

v Pricing of credit

At the time of writing, the pricing of credit in the Norwegian leveraged finance market seems to be relatively similar to the situation in 2018. To be competitive, Nordic banks are now offering TLB for 375 to 400 basis points over the Norwegian interbank offered rate (NIBOR). There has been a move away from the traditional senior A/B tranches (with even amortisation on the A tranche and bullet repayment on the B tranche) to an all-TLB structure with minimal front-end amortisation. Typically, the margin on the A tranche will be 50 basis points lower than for the B tranche. On some smaller deals where the banks’ acquisition financing department has not been involved, margins have been more favourable.

A tranches throughout 2018 and into 2019 have been less frequent than in previous years. When banks insist on an A/B tranche structure, they can seldom expect to achieve more than a 20/80 split, compared to a 40/60 split, or sometimes 50/50 split, as was the norm in the years immediately following the credit crunch.

Leverage multiples have continued to increase since 2015, all depending on each individual investment case. During 2018, we observed everything from 2.5 to 6.7 times EBITDA (all senior) and combinations of senior, 2nd Lien or high-yield bonds around 7.5 times EBITDA, even if most banks would hold back on accepting an increase in leverage multiples above 6 times EBITDA. For some large Norwegian targets with attractive cash flow, there were indications that some international banks were willing to support more than 7 times leverage (potentially 7.5 times if cash flows or valuation were supportive), while most Nordic banks would, subject to credit committee approval, be willing to accept a debt structure of 7 times EBITDA with senior debt leverage between 5.5 to 6.5 times EBITDA.

Throughout 2016, 2017 and 2018 and the beginning of 2019, most Nordic banks seem to be attempting to resist equity contributions below 35 per cent. There has been a clear increase in acquisition multiples and banks prefer that a borrower finances parts of the increase itself by contributing more equity to the structure. Sponsors may still attempt to circulate draft term sheets to the banks with financing ideas with only a 20 to 30 per cent equity contribution from the sponsor; there were deals of this kind in both 2016, 2017 and 2018.

In general, in our view the arrangement fee in bilateral transactions in May 2019 was between 225 and 275 basis points. In syndicated deals, the arrangement fee now seems to be standard at 250 basis points for medium-sized transactions. If a syndicate consisted of two or three banks, of which one is a foreign bank, this very often increased the arrangement fee by
50 to 75 basis points compared with a bilateral transaction. Agency fees have also increased. The banks blame this, inter alia, on more cumbersome obligations to comply with know your customer guidelines.

For larger deals, unitranche structures combining senior and subordinated debt into one debt instrument at a blended price seem to have replaced traditional mezzanine. Throughout 2018, we observed some international banks willing to propose term B, C, D, E and F-style loan facilities for financing Norwegian assets at very favourable rates.

Up to May 2019, two PE sponsor-backed M&A deals were refinanced by issuing high-yield bonds in the debt capital market, one less than during the same period in 2018. These were achieved through interest rates from 365 to 700 basis points over NIBOR.

vi Financial covenants, mandatory prepayments and excess cash sweep

A full suite of financial covenants more or less used to be the norm in the leveraged debt market, usually comprising leverage, interest cover, cash-flow cover and restrictions on capital expenditure, and such covenants would be tested frequently. Borrowers would seek to amend the interest cover covenants to provide additional headroom.

However, there has been an explosive development in financing provided by high-yield bonds issued in the debt capital market. Bond financing may still retain incurrence-based financial covenants (i.e., compliance with a fixed-charge covenant test or leverage test measured at the time debt is incurred, investments are made or dividends are issued). Nowadays, most Norwegian banks are willing to grant acquisition financing only based on leverage and cash flow cover covenants.

Throughout 2018 and into 2019, in larger deals with an international banking syndicate, it has become the norm to use cove lite-like terms for LBO transactions, but banks will normally seek to resist such terms on small to medium-sized transactions. To meet increased competition on smaller deals, banks continue to ease back on some of their terms and there has been a move towards more relaxed terms (covenant-loose) for senior debt in the leveraged market for mid-market deals. Typically, interest cover and capital expenditure covenants are not seen very frequently in leveraged finance transactions.

Equity cure rights (the right to cure breaches of financial covenants by injecting additional equity) are generally accepted among banks. However, permitted amounts, their use in consecutive financial quarters and the application of equity cure proceeds to repay debt are subject to negotiation. Banks will generally tend to restrict equity cures and will try to ensure that as much as possible of the equity cure amount is being applied to prepayments. By mid 2019, there seemed to be a general consensus among the larger banks that they would be prepared to accept equity cure rights of up to five times the terms of the facilities, even though it was known that, for occasional deals, banks had been willing to move to up to six times. This is one more or less the same as for 2018. We have now also started to see increased pressure on banks to accept EBITDA cures, and there have now been deals in Norway conducted with this type of cure. On large transactions, up to a 5 times EBITDA cure is fairly frequent, while for mid-sized deals, 2 times EBITDA cures should now be possible to achieve.

The scope of agreed carve-outs and de minimis thresholds for mandatory prepayment in cases of disposal proceeds, acquisition proceeds, insurance proceeds and excess cash flow

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Patient admits treatment was not as effective as expected.

In a syndicated loan agreement, one bank will act as an agent on behalf of the other banks in the syndicate according to a clause in the agreement. For this, the borrower will have to pay an annual agency fee.

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continue to be the subject of hard negotiations, and will vary according to the deal. However, since 2013, the sweep percentage has steadily gone down, and the downwards ratchet leverage levels at which a cash sweep ceases to apply have started to increase.

It now seems that banks’ terms and conditions in the leveraged finance sector have been forced to return to those of the pre-crisis era. Obviously, banks will seek to hold back this development as long as possible. How far sponsors are able to drive the banks further in this respect remains to be seen.

VII EMPLOYMENT LAW

Under Norwegian law, employees are afforded protection through legislation, mainly the Workers’ Protection Act (the Act), which implements the Acquired Rights Directive\(^\text{11}\) and collective bargaining agreements. The Act further includes protection against, inter alia, unlawful dismissals and mass layoffs.

Private acquisitions of or public offers for shares in a target company will not generally affect the terms of an individual’s contract of employment with the target company. A transaction will not itself trigger any duties towards the target company’s employees for the new shareholder. However, the target company is duty-bound to inform the employees.

When a business (asset) is acquired, according to the Act, employees as a main rule have the right to have their employment contracts transferred to the purchaser, and the purchaser will therefore assume all rights and obligations of the transferor, provided that the unit being transferred is an independent economic unit that keeps its identity subsequent to the transfer. Certain exceptions apply to pension regimes. An employee may refuse the transfer of his or her employment to the new employer. The former and the new employer shall, as early as possible, provide information concerning the transfer, discuss it with the employees’ elected representatives and then inform each employee. Similar provisions are often provided for in collective bargaining agreements, and the provisions in these agreements may therefore also apply to share transactions.

Employees are protected against termination based on a transfer of business, but terminations resulting from rationalisation measures may take place. The rules for asset transfers also apply in cases where the identity of the employer changes after a merger.

The Act sets out detailed rules that must be observed with respect to, inter alia, workforce reductions, dismissals and redundancy notices, and transferring and relocating employees, in particular in a business combination that takes place as an asset deal. These rules are supplemented by notification and discussion obligations in connection with a business combination set out in collective bargaining agreements (if applicable) with some of the labour unions.

Furthermore, the Norwegian Reorganisation Act of 2008 must be observed prior to plant closures and mass lay-offs. This Act sets out detailed rules and imposes an obligation on the owner of a business if it is considering a workforce reduction that involves more than 90 per cent of the company’s workforce or if it is considering closing the business activity.

In March 2015, the Conservative government surprisingly reintroduced a Bill proposal implying changes to the rules relating to restrictive covenants in employment relationships. The Ministry of Labour under the previous government had introduced the basis for the

proposed amendments in 2010. The Bill proposal was never put forward. However, the proposed changes have now been reintroduced and, in spite of objections from several employer and business organisations, Parliament has resolved to adopt the proposal.

From 1 January 2016, non-recruitment clauses between an employer and other businesses will be invalid except when such undertakings are agreed in connection with takeover situations. Since 1 January 2016, however, in takeover situations, a non-recruitment clause can only be agreed for a maximum of six months from the date on which the parties resolved to terminate negotiations if negotiations fail. Non-recruitment clauses can further be agreed for a maximum six-month period from the date of transfer of a business provided the employer has informed all affected employees in writing.

It is not obvious if the letter of the new law also prohibits a seller and a buyer in a share purchase transaction from agreeing non-recruitment clauses for longer periods, provided the target company itself (as the employer of the relevant employees) is not a direct party to the agreement. It can be argued that a non-recruitment clause in a share purchase agreement does not violate the new legislation as long as the non-recruitment clause only refers to the target company’s employees, and the target company itself is not a party to the agreement. There is a risk that non-recruitment clauses agreed for longer periods in share sale and purchase transactions may still be invalid. The basis for this is that even if the target company is not a direct party to the sale and purchase agreement, the effects of the clauses in share purchase agreements may still turn out to be the same as if a target company had become a party to the agreement. Consequently, it can be argued that non-recruitment clauses agreed for longer durations in share purchase agreements at least violate the spirit of the new legislation, and thus must also be considered prohibited.

VIII TAX LAW

i Acquisition of shares

Norwegian shareholders, as LLCs and certain similar entities (corporate shareholders), are generally exempt from tax on dividends received from, and capital gains upon the realisation of, shares in domestic or foreign companies domiciled within EU and EEA Member States. Losses related to such realisation are not tax-deductible. Consequently, corporate shareholders may sell shares in such companies without being taxed on capital gains derived from the sale. Costs incurred in connection with the sale of shares are not tax-deductible. Certain restrictions exist regarding foreign companies not located in EU or EEA Member States, or located in low-income tax states within EU and EEA Member States, that are not conducting businesses out of such countries (controlled foreign companies (CFC) rules). On 1 January 2012, Norway abolished the former 3 per cent clawback rule on capital gains so that capital gains earned by corporate shareholders has become subject to zero tax. This applies regardless of whether the exempted capital gain is derived from a Norwegian or a qualifying non-Norwegian company. Dividends received by a Norwegian company on business-related shares in group subsidiaries within the EEA, held directly or indirectly with more than 90 per cent inside the EEA, are also exempt from Norwegian corporate tax in the hands of the receiving corporate shareholders. The 3 per cent clawback rule will, however, apply to dividends received by corporate shareholders owning less than 90 per cent of the shares, and for foreign corporate shareholders with a permanent establishment in Norway that receive dividends from Norwegian companies, subject to such foreign corporate shareholders participating in or carrying out business in Norway to which such shareholdings are allocated.
Under these circumstances, 3 per cent of dividends are subject to taxation as ordinary income at a rate of 22 per cent (reduced from 23 per cent with effect from 1 January 2019) (giving an effective tax rate of 0.66 per cent).

Dividends received or capital gains derived from realisations of shares by shareholders who are Norwegian private individuals (personal shareholders) are taxable as ordinary income. With effect from 1 January 2019, the government increased the tax rate on dividends received from or capital gains derived from the realisation of shares held by Norwegian private individuals. According to the new rules, the amount derived from, inter alia, such distributions or capital gains must be multiplied by 1.44 (an increase from 1.33 in 2018), and this grossed-up amount is thereafter to be taxed as ordinary income for private individuals at a rate of 22 per cent. In effect, this increases the effective tax rate on distributions and gains from the 30.59 per cent rate under the former tax regime to 31.68 per cent. Any losses are tax-deductible against a personal shareholder’s ordinary income.

Capital gains from the realisation of shares in Norwegian LLCs by a foreign shareholder are not subject to tax in Norway unless certain special conditions apply. The extent of the tax liability of foreign shareholders in their country of residence will depend on the tax rules applicable in that jurisdiction.

Normally, an acquisition of shares in a Norwegian target company will not affect the target’s tax position, including losses carried forward, and such attributes normally remain with the target unless the tax authorities can demonstrate that the transfer of shares is primarily tax-motivated.

**ii Acquisitions of assets**

Capital gains derived from the disposal of business assets or a business as a whole are subject to 22 per cent tax and losses are deductible. A Norwegian seller can defer taxation by gradually entering the gains as income according to a declining balance method. For most assets, the yearly rate is a minimum of 20 per cent, including goodwill (however, see Section VIII.x).

The acquirer will have to allocate the purchase price among the assets acquired for the purposes of future depreciation allowances. The acquirer will be allowed a stepped-up tax basis of the target’s asset acquired. The part of the purchase price that exceeds the market value of the purchased assets will be regarded as goodwill. However, the tax authorities may dispute the allocation to goodwill instead of other intangible assets with a considerably longer lifetime.

As gains from the disposal of shares in LLCs are generally exempt from tax for corporate shareholders, this will, in many instances, make the sellers favour a share transaction over an asset transaction. This will not, however, be the case in transactions involving a loss for the seller, as a loss will still be admitted for the sale of assets.

**iii Mergers**

Under Norwegian law, an enterprise can be acquired through a tax-free statutory merger in return for the shareholders in the transferor company receiving shares as consideration. Such a transaction will be tax-exempt for both the shareholders and the merging companies. To qualify as a tax-exempt merger, all companies involved need to be domiciled in Norway; however, according to amendments made to the tax regulations in 2011, cross-border mergers and demergers between Norwegian companies and a company domiciled within the European Union or the EEA (subject to certain conditions being fulfilled) can also be carried out as tax-free mergers or demergers under Norwegian law.
To qualify as a tax-free merger, all tax positions will have to be carried over without any changes, both at the company level and at the shareholder level.

A cash element may be applied as consideration in addition to shares in the transferee company, but may not exceed 20 per cent of the total merger consideration. Cash payments will be considered as dividends or as capital gains, both of which will be taxable if the receiver is a personal shareholder. If cash compensation shall be considered as dividends, it must be divided between the shareholders in accordance with their ownership in the transferor company. Dividends or gain will be tax-exempt if the shareholder is a corporate shareholder, except for the tax on 3 per cent of their dividend income derived from shares in the merging companies, which is taxed at a tax rate of 22 per cent if the shareholder owns less than 90 per cent of the shares in the merging companies.

iv Distribution of dividends and interests

No withholding tax is imposed on dividends or liquidation dividends paid by a Norwegian LLC to an EEA-resident corporate shareholder provided that the shareholder is genuinely established and conducts a real business activity in the relevant jurisdiction. Furthermore, an EEA-resident corporate shareholder must be comparable to a Norwegian LLC. In this context, an assessment would need to be performed to determine whether the company is genuinely established pursuant to a business motive and that the establishment is not purely tax-motivated. The assessment will differ according to the nature of the company in question, and it must be assumed that assessments of a trading company and a holding company will not be the same. If the required criteria are not met, the withholding tax rate in the applicable double taxation treaty for the involved jurisdictions will apply. If a foreign holding company is considered an agent or nominee for another real shareholder (not a legal and economic owner of the dividends) or a pure conduit company without any autonomy to decide what to do with its income, the tax authorities may apply the default 25 per cent withholding tax rate (i.e., not accept treaty protection). Foreign buyers of Norwegian assets should thus be cautious when setting up acquisition structures and include tax reviews of any prior holding structures when conducting due diligence.

Interest payments are not subject to withholding tax, even if payments are made outside the EEA; however, the government has proposed a new tax reform, which includes a rule allowing the government to introduce withholding tax on interest and royalty payments (see Section VIII.x). Regarding excessive interest and reclassified loans, see Section VIII.vi.

v Deducting losses on receivables between related companies

A company may finance its subsidiaries either by loans or by equity. If using a relatively high amount of loan financing, the parent company could deduct the losses on receivables (bad debt) in the case of an unsuccessful investment while realising a tax-exempt gain on shares where an investment is successful. As of 6 October 2011, a parent company’s right to deduct losses on receivables on related entities where the creditor has ownership of more than 90 per cent has been restricted. However, the limitation will not apply to losses on customer debt, losses on debts that represent previously taxed income by the creditor, or losses on receivables arising from mergers and demergers.
vi Thin capitalisation and transfer pricing

Under Norwegian law, significant restrictions on the deduction of interest paid to related parties were implemented with effect from 1 January 2014. Additional restrictions were implemented with effect both from 1 January 2016 and from 1 January 2019. The term related parties covers both direct and indirect ownership or control, and the minimum ownership or control requirement is 50 per cent. Where a related party to the borrowing company has issued security for loans raised from an external lender (typically a bank), the interest paid to the external lender shall be considered internal interest that will be subject to limitations for deduction for tax purposes. Nevertheless, a loan from an unrelated party secured by a guarantee from another group company shall not be considered an intragroup loan provided that 50 per cent or more of shares in the group company issuing the security are owned or controlled by the borrowing company. The limitation rule will also not apply to third-party loans in situations where a related party provides a pledge over that party's shares in the borrowing company, or provides a pledge or charge over the related party’s outstanding claims towards the borrowing company. Further, negative pledges provided by a related party in favour of a third-party lender will not be deemed as security within the scope of the interest limitation rule. Notwithstanding the above, the interest limitation rule will still apply if the loan from an unrelated party can be considered as a de facto back-to-back loan from a related party.

According to the interest limitation rules, interest expenses will, in general, still be fully deductible against interest income. However, interest expense excluding interest income (net interest expense) will only be fully deductible if the total amount of interest expenses does not exceed 5 million kroner (a threshold value, not a basic tax-free allowance) during a fiscal year or if the interest expense is paid to a non-related party. Outside these situations, from 1 January 2016 the rules hold that net interest expenses paid to a related party can only be deducted to the extent that external and internal interest expenses combined do not exceed 25 per cent (previously 30 per cent) of the taxable profit after adding back net internal and external interest expenses and tax depreciation. This is a type of taxable approach to a company's EBITDA. If a company has paid interest on intragroup loans exceeding 25 per cent of the calculation basis, any excess amount shall be added back to its taxable income.

For the purpose of calculating the net interest paid, which may be subject to limitations, the term interest includes any payment considered as interest for Norwegian tax purposes, including certain premiums and discounts. The same applies to gains and losses on receivables issued at a higher or lower price than the strike price. However, gains and losses are not regarded as interest income or interest expenses for the person who has acquired the debt in the secondary market. Currency gains or losses are not considered as interest; nor are gains or losses on currency and interest derivatives.

Further, the limitation of interest deductions shall be calculated on a per-legal-entity basis, and any related-party interest payments that are not deductible due to such limitation may be carried forward for a maximum period of 10 years. Interest received shall be classified as taxable income for the creditor company, even if the debtor company is denied deductions due to the proposed limitation. Group contributions and losses carried forward may not be used to reduce income resulting from interest limitation. Interest limitation will thus result in payable tax.

At the end of the 2016, the EFTA Surveillance Authority (ESA) issued a reasoned opinion stating that the Norwegian interest limitation rules of 2015 in their current form violate the freedom of establishment, and thereby Article 31 in the EEA agreement. In a
response dated 31 January 2017, the Ministry of Finance argued that the Norwegian interest limitation rules are compatible with Norway's EEA obligations; however, the Ministry also described certain proposed changes to the rules that should be implemented. The next step is for the ESA to decide whether it will take Norway to the EFTA Court for infringing its EEA obligations.

With effect from 1 January 2019, the Norwegian interest limitation regime has been amended: interest payable on bank facilities and other external debt within consolidated group companies is now subject to the same interest deduction limitation regime as interest paid to related parties. The new amended rule only applies if the annual net interest expenses exceed 25 million kroner in total for all companies domiciled in Norway within the same group. Further, two revised escape rules aimed at ensuring that interest payments on loans from third parties not forming part of any tax evasion scheme still should be tax deductible has been implemented. The previous interest deduction limitation rules will continue to co-exist with the new rules, but the scope of the old rules only applies to interest paid by Norwegian enterprises to a related lender outside of a consolidated group (typically where the related lender is an individual).

For enterprises within the petroleum sector, the Ministry has stated that it may consider introducing separate interest deduction limitation rules.

vii Taxation of carried interests

Under current tax law, there is no explicit rule for taxation where managers of investment funds receive profit interest or carried interest in exchange for their services and receive their share of the income of a fund. The prevailing view until recently has been that, as long as such managers invest capital into funds, the carried interest will be considered a capital gain and taxed at capital gains rates, and if the managers are organised as LLCs, the corporate stockholders’ income in the form of dividends and gains on stocks or ownership interest in other companies would also be exempt from taxation in accordance with the exemption method. However, the tax authorities have initiated several administrative actions challenging the prevailing view by seeking to treat such capital gains as income, subject to ordinary income taxation as salary at a higher tax rate.

In December 2013, Oslo District Court rejected the tax authorities’ primary claim in a dispute between the tax authorities, on one side, and Herkules Capital (a Norwegian PE fund’s advisory company) and, on the other, three key executives employed by the advisory company who had an ownership interest in the advisory company. The Court concluded that there was no basis for considering carried interest as income from labour to be taxed as wage and salary income at a much higher maximum tax rate (now 46.7 per cent) in accordance with the tax authorities’ primary position. The Court also rejected the tax authorities’ argument that distributions from a PE fund to its partners should be subject to additional payroll tax (14.1 per cent). However, the Court concurred with the tax authorities’ alternative claim that such profit is subject to Norwegian taxation as ordinary income from businesses at the then-prevailing tax rate of 28 per cent (now 23 per cent). The taxpayers, being the adviser and the key executives, had not argued that carried interest should be taxed as a capital gain allocated to the general partner, as the general partner (in this particular case) did not have any ownership interest in the fund. The question of whether carried interest should be treated as a capital gain was therefore not considered by the Court.

The tax authorities filed an appeal, and in January 2015, the Court of Appeal reversed the District Court’s ruling and upheld the tax authorities’ original tax assessment (i.e., that
the carried interest should be considered as salary income for the relevant key executives). The Court of Appeal further concluded that the distribution to the key executives of such profits in this particular dispute also was subject to payroll tax (at 14.1 per cent) under Norwegian law, and ordered the key executives to pay a 30 per cent penalty tax on top.

The taxpayer appealed the ruling to the Norwegian Supreme Court, and in November 2015, the Supreme Court finally overturned the Court of Appeal and invalidated the tax authorities’ tax assessment. The Supreme Court concluded that the carried interest should be considered as ordinary income from business taxed at the then-prevailing tax rate of 28 per cent (now 22 per cent), but that such income could not be considered as salary income for the relevant key executives. As such, there could be no question of payroll taxes on such distributions.

viii Group contributions
Norwegian companies cannot file consolidated tax returns or form fiscal unities, but a transfer of taxable income within an affiliated group of Norwegian entities is possible through group contributions to offset taxable profits against tax losses in another Norwegian entity. It is possible to grant more group contributions than taxable income, but the grantor company will not be able to deduct the excess amount. This excess amount, which is not deductible for the grantor, would equally not be taxable for the recipient. The distributable reserves form the limit for total group contributions and dividend distributions. To enable group contributions, the contributing and receiving entities must be corporate entities taxable in Norway, an ultimate parent company must hold more than 90 per cent of the shares and voting rights of the subsidiaries (either directly or indirectly) at the end of the parent’s and the subsidiaries’ fiscal year, and the companies must make full disclosure of the contribution in their tax returns for the same fiscal year. Furthermore, the Norwegian group contribution rules are, under certain conditions, also applicable to Norwegian branches of foreign companies that are resident within the EEA. As from 1 January 2018, Parliament has implemented a rule allowing a grantor company to deduct group contributions to a recipient resident within the EEA, provided the recipient has a tax loss carried forward from previous business activity in Norway, subject to the recipient reducing the tax loss carried forward with an amount equal to any group contributions received.

ix Stamp duty and capital duties
Norway does not levy capital duties. Stamp duty is triggered only if real property is acquired. If the shares in a company owning real property are acquired, no stamp duty is levied.

x The 2016 Norwegian tax reform
During the past four years, the government has proposed and implemented several new rules based on a previous proposal for a broader tax reform (proposed reform) issued in October 2015.

Under the proposed reform, the government originally stated that it intended to adopt a rule allowing it to introduce withholding tax on interest and royalty payments. So far, such rules have not been adopted. However, the government has now stated that it aims to propose a new bill to be adopted by the Parliament in this regard during the course of 2019. In the fiscal budget for 2019, the Ministry of Finance has proposed a new rule, elaborating on a previous proposed reform to reduce the possibility for treaty shopping by implementing a rule stating that all entities established and registered in Norway will have Norwegian tax domicile, unless
Norway

a treaty with other states leads to a different result. Consequently, companies registered in Norway shall in the future never be considered stateless. This rule will also apply to companies previously established and registered in Norway but having later moved their tax domicile out of Norway. Even companies established and registered abroad shall be considered to have Norwegian tax domicile, provided the management of such companies (in reality) is carried out from Norway. These new rules have been implemented with effect from 1 January 2019, or from the first fiscal year starting after 1 January 2019, but no later than 1 January 2020.

In the 2017 fiscal budget, the government also states that it intended to submit a consultation paper for amending the Norwegian CFC rules. The consultation paper was originally expected to be issued during the course of 2017, but it has not yet been issued.

See Section VIII.vi regarding further restrictions on the interest deduction limitation regime.

IX COMPETITION LAW

Under Norwegian law, an acquisition, merger or other concentration involving businesses must be notified to the NCA if the following conditions are met: the undertakings concerned on the target side have a group turnover in Norway exceeding 100 million kroner; the acquirer has a group turnover in Norway exceeding 100 million kroner; and the combined group turnover of the acquirer and the target in Norway is 1 billion kroner or more. The NCA is empowered to issue decrees ordering that business combinations that fall below these thresholds still have to be notified, provided that it has reasonable cause to believe that competition is affected, or if other special reasons call for such investigation. Such a decree has to be issued no later than three months after the date of a transaction agreement or the date when the control was acquired, whichever comes first.

On 1 January 2014, Norway implemented a more comprehensive form of notification (more similar to a Form CO), though more limited in substance than the former complete filing form. However, the Ministry of Trade, Industry and Fisheries has also adopted a simplified procedure for handling certain transactions that do not involve significant competition concerns within the Norwegian market – a short-form notification that is similar to the EU system. In March 2016, Parliament adopted amendments to the simplified merger control procedure, which now covers:

\(a\) joint ventures with no or de minimis actual or foreseen business activities within Norway. A turnover and asset transfer test of less than 100 million kroner is used to determine this;

\(b\) the acquisition of sole control over an undertaking by a party that already has joint control over the same undertaking; and

\(c\) concentrations under which one or more undertakings merge, or one or more undertakings or parties acquire sole or joint control over another undertaking, provided that:

- none of the parties to the concentration is engaged in business activities in the same product and geographic market (no horizontal overlap), or in a product market that is upstream or downstream from a product market in which any other party to the concentration is engaged (no vertical overlap);
- two or more of the parties are active on the same product or geographical market (horizontal overlap) but have a combined market share not exceeding 20 per cent (previously 15 per cent) (horizontal relationships); or
one or more of the parties operates on the same product market that is upstream or downstream of a market in which the other party is active (vertical overlap), but none of the parties individually or in combination has a market share exceeding 30 per cent (previously 25 per cent).

After receipt of a filing under the new rules, the NCA now has up to 25 working days to make its initial assessment of the proposed transaction, allowing, however, for pre-deadline clearance, so that at any time during the procedure, the NCA can state that it will not pursue a case further. The NCA must, prior to expiry of this deadline, notify the parties involved that a decision to intervene may be applicable. If it issues such a notice, it has 70 working days from the date the notice was received to complete its investigation and reach a conclusion. This basic period can be extended under certain circumstances. Since an amendment in 1 July 2016, the statutory timetable for clearance under the Norwegian merger control regime allows 145 working days total case handling time.

There is no deadline for filing a notification, but a standstill obligation will apply until the NCA has cleared a concentration. As under EU merger rules, a public bid or a series of transactions in securities admitted to trading on a regulated market such as the OSE can be partly implemented, notwithstanding the general standstill obligation. For such exemption to be effective, the NCA must be notified about the acquisition immediately (normally the day on which control is acquired).

A simplified notification may, under the new regime, be submitted in Danish, English, Norwegian or Swedish, whereas a standardised notification has to be submitted in Norwegian. Since 1 July 2016, the substantive test (which was previously based on a substantial lessening of a competition test) has now been aligned with the same substantial impediment to efficient competition test as applicable under the EU rules, meaning that Norway must now apply the same consumer welfare standard as the Commission instead of the previous total welfare standard.

From 1 April 2017, the power previously held by the King Council to intervene in merger control cases has been abolished. These powers have been transferred to an independent appeal board, which now handles appeals in merger control cases.

Failure to comply with the notification duty leads to administrative fines. The NCA may issue fines of up to 10 per cent of the undertaking’s worldwide turnover. The highest fine so far amounted to 25 million kroner and was issued to Norgesgruppen in 2014. In principle, breaches can also be subject to criminal sanctions, but this has not yet occurred.

X OUTLOOK

Even though there was a dip in Norwegian M&A activity in 2018 compared to the record year seen in 2017, 2018 was still a very strong year for M&A from a historical perspective. Despite a decline in global M&A during Q1 2019, the first four months of 2019 began with increased M&A activity in Norway compared to last year. The Norwegian oil and gas sector has now adapted to lower oil prices and as a result has regained profitability, which again has resulted in the Norwegian economy recovering from the setback experienced following the drop in oil prices in 2014. Experts expect petroleum investments to rise by 10 per cent to 14 per cent in 2019, which again is expected to help boost Norway’s mainland activity further. A continuingly weak kroner is also expected to continue increasing investments within the Norwegian manufacturing sector in 2019. Currently, the Norwegian economy
seems to be reasonably balanced, with a trend of policy rates being on the rise. The general impression is that there is quite a lot of optimism regarding the Norwegian M&A market, even if recently indications of economic worries and geopolitical uncertainties combining to depress the global M&A figures have been seen.

Still, Norwegian companies continue to be exposed to the same pressures that are currently driving deal activity globally, including lack of opportunities for organic growth in a generally low-growth environment, transformational developments in technology and the need to acquire new technology to stay ahead of competition. Acquiring or collaborating with technology providers to drive innovation in their processes, rather than as an asset in its own right, seems to be a key consideration across all sectors. This applies, for example, in energy, life sciences, telecommunications, transport and financial institutions. This trend also looks set to continue globally in 2019, and corporates seeming to view M&A deals as crucial for strategic growth. The relatively strong economic outlook, presence of continuing strong public markets, large cap deals, CEO confidence and transaction pipeline all seem to indicate that the Norwegian M&A market most likely will be strong in 2019 and 2020 as well.

Nevertheless, there are some uncertainties, such as the possible effects of high housing prices, which could turn out to be unfavourable even if the market for now looks to be stabilising. However, rising interest rates, a high number of unsold houses and a high level of housing starts to population growth may curb the growth in house prices. It is expected that the Norwegian Central Bank may continue to raise interest rates during the next 12 to 24 months. In combination with stricter leveraging regulations, this could trigger a housing market correction. If so, the critical issue is to what extent the market is heading for a soft or hard landing. A recent International Monetary Fund house-price regression exercise suggests that Norway’s house prices were overvalued by 15 per cent at the end of 2016, which makes a soft landing possible. A housing market correction could indirectly contribute to less deal activity in the market, since it is expected to reduce spending by Norwegian households.

Globally, there are also looming uncertainties to consider, including the fact that Chinese corporate debt continues to be at a record high. If this reaches some sort of breaking point it could trigger a new financial crisis and recession, resulting in a weaker global economy. Trade wars, protectionism and escalating geopolitical turmoil may also have a negative effect on global M&A activity, indirectly affecting Norwegian deal volume. In this regard, bidders from Asia-Pacific were more or less non-existent during Q1 2019 in the Norwegian M&A market. According to Mergermarket, the number of outbound M&A deals from China are currently at their lowest level since Q4 2013, indicating that the US–China trade war has started to impact cross-border deal flows.

At the same time, a survey among global companies indicates that a majority of the companies that participated in the survey plan to divest within the next two years, which is expected to have a continued positive effect on M&A deal activity in Norway. Companies are now very often looking to streamline their operating models, which quite often will have an impact on their divestment plans for the next 12 to 24 months. We also believe that many investors continue to view Norway as a good place to invest owing to its highly educated workforce, technology, natural resources and well-established legal framework for M&A transactions. Consequently, the total M&A deal volume in the Norwegian market should remain relatively strong in 2019, with certain sectors showing a clear amount of increased activity.

One sector in which we believe there will be more activity in 2019 than last year is the energy sector, and in particular within the oil and gas segment. Still, things often
shift rapidly in today’s market environment: a slight short-term improvement in oil prices combined with executives’ fears of losing opportunities to competitors may have a substantial effect on the level of optimism in the market and potential investors’ willingness to carry out deals. Many businesses are currently driven by rapid technology changes and the battle for customers. Consequently, businesses are fighting to stand out from their competitors, and cross-sector convergence (i.e., expanding beyond traditional core activities to acquire new capabilities) is one way to be differentiated, typically by adding new technology through acquisitions. This is an important factor currently spurring M&A activity around the world, which is also influencing the Norwegian M&A market. Many Norwegian businesses possess important technology and intellectual property rights that may be useful in sectors and businesses other than those for which they were originally developed. An increase in interest from foreign investors wanting to acquire Norwegian technology through M&A has recently been observed, and we believe that this is likely to continue irrespective of how oil and gas prices develop.
Chapter 34

PANAMA

Andrés N Rubinoff

I OVERVIEW OF M&A ACTIVITY

Panama's economy continues to lead in Latin America, with a growth in gross domestic product (GDP) of 3.7 per cent in 2018. The economy has been supported by the expanded Panama Canal and the appreciating US dollar, with a forecast a real GDP growth above 5.8 per cent for 2019. To that end, Standard & Poor’s recently upgraded Panama’s sovereign credit rating to BBB+, announcing the improved rating together with a stable outlook at least a month before the outcome of presidential elections on 5 May 2019.

M&A activity in Panama was expected to remain robust throughout 2019, as industries such as logistics, energy and mining maintained a vibrant economic growth, while others companies in the retail and financial sectors are ripe for consolidation or acquisition. Large infrastructure projects, such as the US$2.6 billion construction of a third metro line, are also contributing factors in the increase in foreign direct investment in Panama. The third metro line, a monorail system stretching 25km west of Panama City, is currently at the bidding process stage, with four bidders aiming to procure the contract. It will cross the Canal over the Fourth Bridge, which will house the metro line and eight lanes to meet the needs of the rapidly growing cities west of the capital. The Fourth Bridge project has an expected cost of around US$1.5 billion and was granted to Consorcio Panamá Cuarto Puente, a joint venture between China Communications Construction Company LTC and China Harbour Engineering Company LTD.  

The energy sector in Panama will continue to experience government and foreign direct investment. Given Panama’s long-running sustained economic growth, it is unsurprising that energy demand in the country is expected to keep increasing. The difference between the first trimester of 2018 and 2019 reflects a growth of 4.1 per cent. Investment in the clean energy sector has also experienced significant growth and, at the going rate, clean energy production has produced significant achievements, such as the inauguration of the Ikakos Power Plant, a solar energy plant that produces around 40 megawatts yearly. The government is currently working on the bidding process for Transmission Line 4, which will have cost approximately US$450 million, and which will cement the connection between heavy hydroelectric energy
production in the west part of the country and the east part of the country’s increasing demand. This project has attracted foreign investment, but the bidding process has not found a bidder that can comply with the requirements set forth by the government.

The International Monetary Fund (IMF) Western Hemisphere Department recognised Panama’s positive future growth due to:

- the expansion of the Panama Canal;
- the development of several services industries;
- the approval of free trade agreements with the United States, the European Union and Canada; and
- the growth of the mining industry.

The latter has increased thanks to copper mining, which element has only recently started to be tapped. The Cobre Panama copper mine, controlled by First Quantum Minerals, is said to be practically operational: Cobre Panama is the nation’s most important private investment project, with an estimated production of 320,000 tonnes of copper per year. As noted in an IMF Country Report for 2014, the copper mine was expected to bring about ‘US$6½ billion over 2013–17, about US$1½ billion of which have already invested’. The IMF calculates that the mining project will contribute around 1.5 per cent of Panama’s GDP in 2019.

Panama is consistently rated by international indexes as one of the best countries in Latin America for business and investment. The World Bank’s Doing Business 2019 ‘ease of doing business’ index ranked Panama 79th of the 190 surveyed countries. This may be due to its encouragement of foreign investment through legal incentives. In 1998, the government enacted the Investment Stability Law, which guarantees equal treatment to foreign investors under the law as is given to their domestic competition, and guarantees the same commercial and fiscal conditions for 10 years to foreign investors who invest at least US$2 million in Panama. Under Law 41 (2007), Panama has motivated multinational companies to locate their headquarters in Panama through tax incentives. As of May 2019, 147 international companies have been established under the Law, including major multinationals such as Hyundai, Procter & Gamble, AES, Halliburton, Hewlett-Packard, Peugeot/Citroën, Pan-American Life Insurance Company, Caterpillar, LG, 3M, Western Union and Roche, owing to the various taxation, immigration, labour and employment incentives offered specifically to benefit multinationals that establish their regional offices or headquarters in Panama.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The relevant Panamanian laws and regulations governing business combinations include the Corporations Law, the Limited Liability Company Law and the Commercial Code, which is supplemented by the Civil Code. As combinations generally cause taxable events, the Tax Code and its regulations (especially Executive Decree 18 of 1994, which establishes a special regime regarding share-for-share mergers) and Law No. 18 of 2006, which created

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5 impresa.prensa.com/economia/BM-licitaria-linea-transmision_0_4721527869.html.
a special capital gains regime, are also pertinent. In the case of publicly traded companies, the Securities Law\(^9\) and its regulations govern tender offers, proxy statements and rules of disclosure, among other matters.

Business combinations in Panama are usually structured as share or asset purchases, tender offers or mergers, but other techniques can also be used. One example is the capitalisation of shares of two operating companies to a holding company incorporated for that purpose with joint participation in the holding company. In the case of publicly traded companies, combinations usually involve a two-step process that begins with a tender offer (either for shares, cash or a combination of both) followed by an actual merger.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Corporate and takeover law can be divided into two kinds of transactions: mergers and share and asset purchases. In the case of mergers, Panama law allows a company to be absorbed by another regardless of the place of incorporation of either firm (merger by absorption). It also allows two companies to merge, forming a new consolidated body. Once a merger becomes effective, the absorbed company ceases to exist as a legal entity, and the surviving company assumes all the assets, rights, licences, capital, liabilities and obligations of the absorbed company by universal succession. Unless the articles of incorporation state otherwise, a merger agreement must be executed by a majority of the directors of each company, and approved by the holders of a majority of the issued and outstanding shares of each firm. The merger agreement must then be registered with the Registry of Companies in Panama to bring it into effect, unless a later effective date is defined in the merger agreement.

Regarding share and asset purchases, unless the articles of incorporation state otherwise, the acquisition of a company generally requires approval from a majority of the directors of the acquiring company regardless of whether it is structured as a share or an asset purchase. On the other hand, the sale of a company, if it represents all or substantially all of the assets of the seller, generally requires approval from both a majority of the directors and holders of all issued and outstanding shares with the voting rights in the event of selling a company.

### IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Foreign direct investment continues to be a principal driver of M&A activity and has been on the rise in the past couple of years: due to the nation’s strengthened alliance with China, we have seen increased interest in the acquisition of local companies by Chinese conglomerates, which have also heavily invested in major engineering, procurement and construction projects. Political instability in nearby Latin American countries has also been a substantial driver for investment into Panama, as individuals and companies seek to diversify their country risk.

Generally there are no foreign ownership restrictions in Panama. Because of issues of national security and national interest concerns, however, ownership of local companies by foreign governments or nationals is restricted in certain industries, including, inter alia, aviation, radio and television, and retail trade. In the case of the retail services market, foreign participation is generally prohibited, with very few exceptions.

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\(^9\) The Securities Law, Decree Law No. 1 of 1998.
V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

Most of the important sectors in the Panamanian economy have been subject to cross-border acquisitions, but M&A activity is expected to continue to be distributed across several industries, led most likely by the traditional financial services (including insurance) and energy sectors, followed by the food and retail industries (both wholesale and consumer sales). The aftermath of the Panama Papers and the controversy surrounding money laundering allegations involving a prominent retail trade group have led to stricter tax, regulatory and anticorruption compliance legislation in the country. Consequently, consolidation among medium and small banks is still expected to pick up, spurred by reduced access to correspondent banks, which are limiting their services because of local regulatory burdens, and increased compliance standards imposed on foreign banks and the perceived reputational risk stemming from the publication of the Panama Papers. This current issue in the Panamanian financial services sector may have further long-term implications. For example, recently Banco Panamá, a small bank located in Panama, merged with Banco Aliado in a transaction valued at US$210 million.

Given the demand for energy in Panama and the region, the energy sector has been the object of recent important acquisitions and new market entrants, including the acquisition by CELSIA (part of the Colombian conglomerate Grupo Argos) of GDF Suez assets in Panama and Costa Rica for a reported US$830 million, and InterEnergy Holding’s simultaneous acquisition and US$300 million project financing of the construction of Phase II and Phase III of the Penonomé wind power plant, the largest wind farm in Central America. Now operational, the plant produced 401,734MWh in 2018, representing 4 per cent of the country’s total energy demand. Significant acquisitions and joint ventures are expected in the next few years in this sector as Panama continues to find and incentivise new sources of energy for its rising demand, while further regulating its existing non-renewable and renewable resources.

Increased deal activity is expected following the now-complete Canal expansion and the growth of the port industry with regard to the logistics, transportation and distribution and maritime industries, as this sector saw growth of 7.3 per cent last year. In the telecommunications sector, Millicom International Cellular SA acquired 80 per cent of Cable Onda, SA, a leading provider of broadband internet, pay-TV, fixed telephony and B2B telecommunications services in Panama, for a reported US$1,462 million.

In recent years, M&A deals in Panama have had many drivers. Certain deals have been instigated by a need to consolidate in a very competitive environment, others have been undertaken to control costs and exploit synergies, and yet others have been fuelled by the global economy and the need to develop new international markets and expand market share. Some of the largest transactions in Central America have included Panamanian target companies, independent of whether they are an operating company or a holding company registered in Panama with operations in the region. Additionally, we are seeing a move from New York law or New York-run deals to Panama law or Panama-run deals for Latin America-based transactions that do not necessarily have a connection to Panama.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

M&A financing in Panama is usually provided by local and international banks, as there are no limitations on international lending. With the end of the financial crisis, deals have also been increasingly funded through private equity firms or through local and international securities issues.

VII EMPLOYMENT LAW

In a merger scenario, the surviving company assumes the labour relations and liabilities of the absorbed company. Similarly, in share acquisitions, the target company retains responsibility for labour relations and liabilities. Asset acquisitions, however, present a special case. If the sale comprises all or almost all the assets, causing business operations to be transferred, both the buyer of the assets – the new employer – and the seller are, for a period of one year following the acquisition, jointly and severally responsible for all labour liabilities that arise prior to the acquisition of the assets or business. Furthermore, employees retain all their rights and benefits, and no adverse changes can be made to their terms of employment. Thus, in many asset acquisitions, insofar as may be legally feasible, buyers require sellers to terminate all or certain labour relations as a precondition to closing a deal, in order to rehire some employees on more favourable terms. Labour unions and employees must be notified of the employer substitution even though they cannot prevent it from taking place.

VIII TAX LAW

One of the main components of any sell-side deal structuring is taxation. The structure of an acquisition is usually influenced to a large extent by the need to make a transaction tax-effective for the seller, without causing adverse tax consequences to the buyer. As Panama generally follows a territorial system of taxation, only Panama-source income (generally income and capital gains realised in connection with a trade, business or real estate transaction in Panama) is taxable. Thus, mergers or acquisitions of companies organised in Panama that do not carry out any trade or business or own assets within the country are generally not taxable. Mergers or acquisitions are generally structured as either share-for-share transactions or share-for-cash transactions, or a combination of both. Acquisitions can also be fashioned as a straight purchase of shares or a purchase of assets. A brief description of the tax treatment for each follows.

Share-for-share mergers are tax-free transactions, provided that no cash is paid out (except up to 1 per cent of the value of a transaction for adjustments of fractional shares) and certain other accounting parameters are followed. In a share-for-share merger, the shareholders of the merged company keep a tax basis on the shares of the surviving company that they receive equal to their average pre-merger tax basis of the surrendered shares.

Share-for-cash mergers, on the other hand, are not tax-free transactions. Gains realised by sellers in these transactions, which are deemed to be gains from Panama-sourced income, are subject to a 10 per cent capital gains tax. The capital gain is the difference between the selling price allocated to Panamanian sources and the tax basis of the shares owned by the selling shareholder. Furthermore, the law requires buyers to withhold 5 per cent of the total purchase price allocated to Panamanian sources (as an advance of the capital gains tax) and directly pay this amount to the tax authorities within 10 days of the transfer of the shares. If the 10 per cent capital gains tax on the realised capital gain is less than the 5 per cent advance...
withholding, sellers can request a tax credit for the difference. This credit must be used in the same fiscal year as that in which the capital gain is realised. Alternatively, sellers can choose to treat the 5 per cent advance capital gains withholding as the final and definitive capital gains tax payable in connection with the sale of the shares. In practice, most sellers pay the 5 per cent purchase price capital gains withholding, as it is difficult to request and use the tax credit in the same year that the transaction took place.

Share purchases are subject to a 10 per cent capital gains tax on Panama-sourced gains in the same manner that share-for-cash mergers are taxed, including the 5 per cent advance withholding obligation. The Department of Revenue of the Ministry of Economy and Finance has repeatedly taken the position that capital gains tax applies to the sale of the shares not only of Panamanian corporations, but also of any upstream company, regardless of its jurisdiction of incorporation, as long as this company, directly or through one or more subsidiaries, has Panama-sourced income. Consequently, gains derived from the direct or indirect transfer of shares of a legal entity that has obtained Panama-sourced income is subject to tax at a rate of 10 per cent.

Following a tax reform (Decree Law 135 of 2012), if a transaction involves, indirectly, the transfer of shares of a Panamanian company with Panama-sourced income, the seller and buyer can now apply pre-established calculations to determine the capital gains tax due on the percentage of a transaction’s purchase price that is attributable to Panamanian assets. To pay the capital gains tax, the buyer and seller will need to file a joint sworn affidavit setting forth the total capital gains tax paid and the calculations used to arrive at the figure. In addition the buyer, who is responsible for the payment, must obtain a temporary tax identification number in Panama, known as 8-NT, and report and pay the capital gains tax. This temporary registration has no additional tax implications or reporting requirements in Panama for the buyer; however, buyers and sellers must be aware that the local tax authority has recently ramped up the audit and enforcement of capital gains tax, particularly in high-profile transactions. Recently, the National Assembly enacted Law No. 70 dated 31 January 2019, which modifies the criminal code and sanctions as a crime the act of tax evasion in excess of US$300,000.

Asset purchases are generally taxable events in Panama. Gains realised on the sale or disposition of assets located in Panama are generally subject to a 10 per cent capital gains tax. In addition, the transfer of chattel property, such as inventory or equipment, is subject to a value added tax equal to 7 per cent, and the transfer of real estate is subject to a 2 per cent transfer tax. In addition, buyers of an ongoing business concern must be aware that they will become liable for the past taxes of the business, even if they are buying the assets of the business and not shares of the company.

Frequently, M&A transactions involve either a pre-closing dividend to exclude assets from a transaction or a post-closing dividend to distribute gains to shareholders. In this regard, as a general rule, corporations in Panama are subject to a 10 per cent dividend tax (20 per cent if the shares are issued to the bearer) on Panama-sourced income. Thus, income that is not Panama-sourced is generally not subject to dividend tax. However, following the recent tax reform, if the company paying the dividend engages in commercial or business activities in Panama that require the company to obtain a business licence, then in addition to paying the 10 per cent dividend tax on Panama-sourced income, it is also subject to a 5 per cent dividend tax on non-Panama sourced income.
Goodwill is another frequent point of conflict between buyers and sellers. Buyers generally want to be able to claim a tax deduction for the amortisation of any goodwill paid in an acquisition. However, amortisation of goodwill is only deductible in Panama if the seller recognises it as income on its annual tax return.

IX COMPETITION LAW

There is no mandatory merger control approval process in Panama; the process is entirely voluntary. That said, with the new antitrust and competition regime established by the Competition Law, economic concentrations created by the mergers of conglomerates within the Panamanian market have come under increasing, albeit still limited, scrutiny by regulators. The Competition Law prohibits economic concentrations whose effects may unreasonably restrict or harm free competition. An economic concentration is defined as the merger, acquisition of control or any other act pursuant to which corporations, associations, shares, trusts, establishments or any other kind of assets are combined, and which occurs between suppliers or potential suppliers, customers or potential customers, and other competing or potentially competing economic agents. The Law applies to any acts or practices that may unreasonably restrict or harm free competition, and whose effects take place in Panama, regardless of where those acts have been carried out or perfected.

The Competition Law does not prohibit all economic concentrations, but only those whose effects may unreasonably restrict or harm competition. In addition, the Competition Law expressly provides that the following business combinations shall not be deemed prohibited economic concentrations:

- joint ventures formed for a definite period of time to carry out a particular project, which is also contemplated in other jurisdictions;
- economic concentrations among competitors that do not have harmful effects on competition and the market; and
- economic concentrations involving an economic agent that is insolvent, if certain conditions are met, which is, roughly speaking, equivalent to the failing company exemption prevalent in other jurisdictions.

Moreover, economic concentrations with restrictive effects on competition may obtain clearance from the Competition Authority if their restrictive effects are outweighed by their contribution to obtaining further efficiencies, such as:

- improvements in commercialisation and production systems;
- fostering technical and economic progress;
- improvements in the competitiveness of an industry; and
- contributions to consumer interests.

If advance verification for an economic concentration is sought and approved, the economic concentration cannot be subsequently challenged. If no advanced verification is sought and the transaction has been consummated, the Competition Authority may file a lawsuit with a specialised superior court within three years of the transaction’s effective date if it considers the economic concentration to unreasonably restrict or harm free competition, seeking that conditions be imposed on the parties to ensure competitiveness in the marketplace, or seeking a partial or complete divestiture of the concentration (or both).
Panama

X OUTLOOK

Panama’s economy is expected to grow at a moderate and sustainable rate, despite the perceived reputational damage to the financial and legal services industries. On this matter, the government has countered issues by cooperating and aligning with international standards, thus making firm commitments to creating a more transparent environment for foreign investors. For example, the government has committed to adopt data-sharing arrangements consistent with US Foreign Account Tax Compliance Act and the OECD’s Common Reporting Standards, and has implemented several strict anti-money laundering regulations applicable to both the financial and non-financial sectors. Multinational corporations, regional conglomerates and private equity firms continue to seek and take advantage of the country’s unique geographical position, its free market system and investor-friendly climate, which will cause the prevalence of cross-border M&A in Panama to increase. A recently adopted bankruptcy law (similar to Chapter 11 under the US federal bankruptcy laws) is also likely to spark interest in distressed assets and companies. Undoubtedly, Panama will remain in the spotlight for foreign investors, and the body of legislation governing M&A in Panama will continue to evolve as cross-border transactions become more complex.
I OVERVIEW OF M&A ACTIVITY

The Portuguese economy continued to show some positive signs in the past year, in particular with GDP growing 2.1 per cent in 2018\(^2\) (GDP started to grow in 2014, at a rate of 0.9 per cent, and continued to grow in 2015, 2016 and 2017, at a rate of 1.5, 1.4 and 2.7 per cent, respectively, in contrast with the 1.4 per cent decrease in 2013 and the 3.3 per cent decrease in 2012). The first quarter of 2019 registered GDP volume growth of 0.5 per cent compared with the first quarter of 2018.\(^3\)

In addition, 2018 was the third year after the conclusion of the financial assistance programme with the European Commission, the International Monetary Fund and the European Central Bank, which was initiated in 2014 further to Portugal's bailout in 2011 and the execution of a memorandum of understanding with those entities in May 2011, and this has also contributed to restoring confidence in the Portuguese economy.

All these signs of growth have been reflected positively in Portuguese M&A activity during the past year, both in terms of number and volume of deals: there were more than 350 M&A deals, and the 158 transactions with disclosed value totalled approximately €22.583 billion (76.12 per cent higher than the value registered in 2017).\(^4\) The following events have been key factors for this dynamic in the Portuguese M&A market during the past couple of years:

a Several privatisations, foreseen under the Portuguese financial assistance programme, were carried out, such as:

- the sale of EGF (a company engaged in the treatment and management of wastewater and solid urban waste, which was sold to SUMA, a joint venture between Mota-Engil and ACS, companies active in the Portuguese and Spanish construction sector respectively);

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1 Francisco Brito e Abreu is a partner and Joana Torres Ereio is a senior associate at Uría Menéndez – Proença de Carvalho.
• the privatisation of CP Carga (a railway freight transport operator) through the sale of 95 per cent of the company’s share capital to MSC Rail (a subsidiary of the Swiss MSC Mediterranean Shipping Company); and
• the sale of TAP (the leading Portuguese airline company, 66 per cent of which was acquired by a consortium headed by David Neeleman (owner of, inter alia, the Brazilian airline Azul) and Humberto Pedrosa (owner of the Portuguese transportation group Barraqueiro), which was partially reverted upon the new government taking office in November 2015).

b Portuguese banks and other entities in the financial and insurance sectors have focused on selling non-core assets and businesses.

c In August 2014, Espírito Santo Group, a conglomerate that comprised, inter alia, one of the biggest banks in Portugal, Banco Espírito Santo (BES), collapsed, forcing a profound reorganisation in the group, including the transfer of part of BES’ businesses to a new bank (Novo Banco), and leading to the divestment of several businesses and to the sale of Novo Banco itself.

d The collapse of the Espírito Santo Group resulted in significant losses in several relevant Portuguese companies, and in particular had an impact on Portugal Telecom, the biggest Portuguese telecommunications player, affecting its merger with Brazilian Oi (a deal that was aimed at creating one of the 20 biggest telecom companies in the world with more than 100 million clients) and leading to the acquisition of its Portuguese business by Altice, which was completed in June 2015.

e International investment and private equity funds have been particularly active in the Portuguese market, and even though their interest in Portugal has been originated by the crisis, the truth is that they maintain a very relevant role in the dynamic of the Portuguese economy, presenting bids in most of the relevant deals in the tourism, real estate, insurance and banking sectors.

f Chinese and Angolan investors have also played a significant role in M&A activity, acquiring companies in several business sectors.

g 2014 was a turning point for the real estate sector, with relevant deals in all segments and with real estate being the most active sector in the Portuguese M&A market, and this trend has been reinforced year on year.

h Tourism has been key for the revitalisation of the Portuguese economy and has also been growing every year, reaching 13.7 per cent of the GDP in 2017.5

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Portuguese legal framework governing M&A comprises, in particular, the following laws:

a the Civil Code, enacted by Decree-Law No. 47344, of 25 November, as amended, which contains the general rules governing sales, purchases and contracts;

b the Commercial Companies Code, enacted by Decree-Law No. 262/86, of 2 September, as amended (PCCC), which includes the general framework governing Portuguese companies (the most common are sociedades anónimas, which may be listed or non-listed

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companies, and *sociedades por quotas*, both of which are limited liability companies) and also the legal regime governing share capital increases and decreases, mergers and demergers, transfers of shares in *sociedades por quotas* and financial assistance;

*the* Securities Code, enacted by Decree-Law No. 486/99, of 13 November, as amended, which is applicable to listed companies⁶ but also contains the general regime regarding some matters, such as the transfer of shares in *sociedades anónimas*;

*the* Competition Code, enacted by Law No. 19/2012, of 8 May;

*the* Labour Code, enacted by Law No. 7/2009, of 12 February, as amended; and

*the* private equity legal regime, enacted by Law No. 18/2015, of 4 March.

In addition, regulated sectors such as banking, financing and insurance are governed by specific laws and regulations, some of which are issued by the respective regulatory entities.⁷ Moreover, privatisations are specifically governed by laws enacted by the government containing the applicable regime for each privatisation.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

#### i Financial sector: structural reforms

A memorandum of understanding established as the main goals for the financial sector, inter alia:

* the preservation of its stability;
* an increase of liquidity and a balanced deleverage of the banking sector;
* the reinforcement of banking regulation and supervision;
* the restructuring of Caixa Geral de Depósitos, the state-owned bank; and
* the reinforcement of the legal framework governing the restructuring and winding up of credit entities and of the deposit guarantee fund, as well as the legal framework applicable to the insolvency of natural and legal persons.

In line with these goals, profound changes have been implemented in the legal framework governing the financial sector, and most of said goals, even if to a variable extent, have been accomplished.

Decree-Law No. 298/92, of 31 December, which governs credit institutions and financial entities, has been the object of an in-depth reform in the past few years, and enacted by several laws and decree-laws, in particular:

* Law No. 23-A/2015, of 26 March, which transposes Directives 2014/49/EU, of 16 April 2014, and 2014/59/EU, of 15 May 2014. Inter alia, the Law:
  * increased the powers of the Bank of Portugal regarding recovery measures;
  * amended the rules applicable to deposit guarantee schemes;

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⁶ Listed companies are overseen by the Portuguese Securities Market Commission (CMVM).

⁷ In particular, Decree-Law No. 298/92, of 31 December, as amended, governs credit institutions and financial entities, which are supervised by the Bank of Portugal, and Decree-Law No. 94-B/98, of 17 April, as amended, governs the activity of insurance companies, which are supervised by the Portuguese Insurance and Pension Funds Authority.
increased the number of possible resolution measures that may be determined by the Bank of Portugal, allowing, in particular, the segregation of assets to an asset management vehicle;

allowed the Bank of Portugal to determine internal recapitalisation measures (bail in);

established specific rules regarding financial support between companies pertaining to the same group; and

imposed an evaluation of the assets and liabilities of the entities subject to resolution measures before the same are implemented.

b Decree-Law No. 20/2016, of 20 April, which sets forth that shareholders’ general meetings of credit institutions whose articles of association establish voting caps must take place every five years to resolve on the maintenance or revocation of said voting caps (otherwise, said voting caps will be considered forfeited).

c Law No. 16/2017, of 3 May, which requires banks to disclose the identification of the shareholders with qualified shareholdings within the banks, as well as the beneficial owner of those same shareholdings.

ii Corporate laws

In 2017, there were two relevant amendments to the PCCC.

Bearer securities

Aiming at preventing corruption, money laundering and tax fraud, and increasing transparency in the capital markets, Law No. 15/2017, of 3 May prohibits the issue of bearer securities, and created a transitional six-month period (until 4 November 2017) to convert existing bearer securities into registered securities. This Law came into force on 4 May 2017.

As a consequence, all securities issued by Portuguese entities, including shares, must be registered securities, meaning that issuers must be able to identify their holders at any time.

Pursuant to this Law, bearer securities that were not converted into registered securities within the aforementioned six-month period cannot be validly transferred, and their holders’ right to participate in the distribution of results is suspended until such conversion is completed.

Conversion of shareholder loans into share capital

Pursuant to Decree-Law No. 79/2017, of 30 June, shareholders of limited liability companies by quotas that gather the necessary votes to approve the amendment of a company’s articles of association may approve a share capital increase by conversion of shareholders’ loans granted by them to the company by means of a simple communication to the company’s directors.

After receiving said communication, the directors must inform the remaining shareholders, who have 10 days to oppose the share capital increase, which only becomes effective if none of the latter opposes the conversion.
iii Private equity

The private equity legal regime has also been the object of reform in the past few years, with the regime enacted by Law No. 18/2015, of 4 March (which partially transposes the Directive on Alternative Investment Funds Managers,8 and Directive No. 2013/14/EU, of 21 May 2013) replacing the regime enacted in 2007, and which also regulates, for the first time, investment in social entrepreneurships and in specialised alternative investments.

One of the main modifications is the creation of two different regimes applicable to private equity companies depending on the value of the portfolios under their management: a stricter regulatory regime is applicable to entities that manage private equity funds whose portfolio value is higher than €100 million when such portfolio includes assets acquired with the use of leverage, or €500 million when such portfolio does not include such assets, and in relation to which there are no reimbursement rights that may be exercised within a period of five years as of the date of the initial investment. Private equity companies that do not fall under these thresholds may also be governed by this stricter regime, provided that they opt in.

The stricter regime applicable to private equity companies entails, in particular:

a an authorisation from the Portuguese Securities Market Commission (CMVM) prior to their incorporation (as opposed to a prior registration with the CMVM as applicable for other private equity companies);

b that all reasonable measures shall be taken and adequate procedures shall be implemented to identify, prevent, manage and monitor conflicts of interest that may be harmful to the interests of the private equity funds under their management and their investors; and

c the obligation to functionally and hierarchically separate the functions of risk management from the operating units, including the portfolio management.

Private equity companies falling under the lighter regime set forth in this Law, but that manage portfolios whose net value exceeds €250 million, must incorporate an additional amount of equity that shall be equal to 0.02 per cent of the amount by which the portfolio’s net value exceeds €250 million.

The management regulations of private equity funds may establish the division of funds into several independent sub funds represented by one or more categories of investment units.

In line with this regime, the CMVM has also issued a new regulation governing these matters: Regulation No. 3/2015.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS9

i M&A transactions headed by strategic foreign investors

Activity in the Portuguese M&A market in the past has been to a large extent due to the role of foreign investors – especially Chinese, US, Spanish, German and Angolan investors – who have played a key role in the revitalisation of the Portuguese economy.

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9 All amounts indicated for the transactions indicated below result from publicly available sources.
This phenomenon is related not only to the pressure of Portuguese companies and the state to divest, which has created excellent opportunities for investors, but also to the fact that Portugal is regarded as a strategic hub between Europe and countries such as Angola, Brazil, Mozambique and other former Portuguese colonies.

Chinese investment has played a particularly relevant role in this, beginning with the acquisition, in 2011, by China Three Gorges Corporation from the state of a 21.35 per cent shareholding in EDP, the biggest electricity producer, distributor and trader in Portugal, for €2.7 billion, followed by the acquisition in 2012, by State Grid Corporation of China, of a 25 per cent shareholding in REN, the largest Portuguese energy grid company, for approximately €387 million. At the beginning of 2014, Fosun International acquired from the state 80 per cent of Caixa Seguros, the largest Portuguese insurance group, including the companies Fidelidade and Multicare, for €1 billion, and in October 2014 Fidelidade acquired 96 per cent of Espírito Santo Saúde, one of the biggest health groups in Portugal, after this company's successful initial public offering at the beginning of 2014 for more than €455 million.

The following are some of the most relevant recent deals featuring Chinese investors:

- in August 2016, Hainan Airlines acquired 23.7 per cent of Azul, the Brazilian airline company that is part of the consortium that won the privatisation of TAP, for €450 million. By July 2016, Hainan Airlines had already paid €30 million for bonds convertible in TAP’s share capital. In March 2019, Hainan Airlines sold its interest in TAP to Azul and Global Aviation Ventures, both controlled by David Neeleman; 
- in November 2016, Fosun acquired 16.7 per cent in Millennium BCP in a share capital increase reserved to it and increased that stake to 24 per cent in a new share capital increase that took place in February 2017 for a global investment of €549 million; 
- in June 2017, a subsidiary of China Three Gorges Group (ACE Portugal Sàrl) acquired 49 per cent of EDPR PT – Parques Eólicos, a 422MW wind farm, for €248 million; 
- in November 2017, China Tianying acquired the insurance companies Groupama Seguros de Vida and Groupama Seguros for an undisclosed amount. 
- in June 2017, EDP sold 49 per cent of EDPR PT – Parques Eólicos to a subsidiary of China Three Gorges Group for €242 million.

- in May 2018, China Three Gorges launched a takeover offer over EDP and EDP Renováveis, subject, in particular, to the withdrawal of the voting cap in EDP’s articles of association by EDP’s shareholders’ general meeting. Since the withdrawal was not approved, in May 2019 the CMVM put an end to the takeover offer based on non-compliance with the conditions established by China Three Gorges.

- in November 2018, the Macao businessman Kevin Ho, through KNJ Investment, acquired a 30 per cent stake in Global Media Group for €15 million; 
- in July 2018, Bison Capital Financial Holdings completed the acquisition of Banif Banco Investimento from Oitante.

European investors have been more active in recent years. Examples include the acquisition of SAPEC Agro Business (engaged in crop production products and crop nutrition, with sales in over 70 countries) by Bridgepoint, completed in January 2017, for €456 million; the takeover launched by Caixabank on Banco BPI, which was successfully completed and entailed an investment of €645 million; and the acquisition of Ascendi by Ardian for €600 million. In July 2018, Blackstone sold Fórum Almada to Merlin Properties for €406.7 million. In line
with this trend, of the 160 inbound acquisitions completed in the past year, 136 were carried out by European investors, with Spain and the United Kingdom sitting in first and second place, respectively.10

Angolan investors have been very active in the Portuguese market. Key players include Isabel dos Santos, daughter of the Angola’s former president and Africa’s richest woman, who already owns shareholdings in, inter alia, GALP (the largest Portuguese oil and gas company), NOS (one of the leading companies in the telecommunications sector, resulting from a merger between Optimus and ZON) and EuroBic (an Angolan private bank based in Portugal). In June 2015, she acquired 65 per cent of Efacec Power Solutions (the core company of Efacec Group, the largest Portuguese electric group) from Mello Family and Têxtil Manuel Gonçalves for approximately €200 million.

American funds have also been very active in the Portuguese market, and have participated in most of the bids for relevant transactions in the past few years. In particular, in January 2016, North Bridge acquired a minority stake in OutSystems, a Portuguese company engaged in the production and development of software, which holds subsidiaries in Brazil, Dubai, the Netherlands and the United States, for €50 million. In March 2016, the Carlyle Group acquired 50 per cent of Logoplaste (an industrial group engaged in the manufacturing of rigid plastic packaging) for €570 million. In June 2018, OutSystems raised US$360 million from KKR and Goldman Sachs in exchange for a minority stake. In the second quarter of 2018, Morgan Stanley Infrastructure Partners and Horizon Equity Partners acquired a 75 per cent stake in Towers of Portugal from Altice for €495 million. In December 2018, the Carlyle Group and Explorer Investments acquired Penha Longa Hotel and Golf Resort for €100 million and in February 2019, Oaktree acquired a stake in Belas Clube de Campo, with a global estimated investment of €500 million.

ii M&A transactions headed by national investors in key destinations

In 2018, 60 per cent of the outbound registered deals completed in the past year were carried out in European companies, with Spain clearly leading the rankings (with approximately 40 per cent of the deals), then followed by two non-European countries: Brazil and the United States (with 12 per cent and 8 per cent, respectively, of the outbound deals).11

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In addition to the transactions listed in the preceding section, the following are some of the other most important M&A deals that have taken place in the past few years.

i M&A transactions related to financial and insurance institutions

In the context of the requirements both at a local and at an EU level regarding ring-fencing and the separation of banks’ deposit-taking functions from more risky businesses, several

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banking and insurance groups have been selling non-core businesses. The increasingly strict regulatory requirements in both the banking and insurance sectors have also led to strategic divestments by several players. The following are examples of deals in these sectors:

a. In April 2016, Bankinter (a Spanish bank) acquired the retail and insurance business of Barclays Portugal for approximately €160 million;
b. In December 2016, Real Vida Seguros (pertaining to the Portuguese Patris group) acquired both a controlling stake in Banif Pensões from Oitante and 100 per cent of Finibanco Vida from Montepio Geral;
c. In February 2017, the Chinese conglomerate Fosun completed the acquisition of a 24 per cent stake in Millennium BCP for a global investment of €549 million (see above);
d. Again in February 2017, Caixabank successfully completed its takeover of Banco BPI, raising its stake from 45 to 84.5 per cent, for €645 million;
e. In August 2017, Novo Banco entered into an agreement to sell 90 per cent of its Cape Verdean subsidiary (Banco Internacional de Cabo Verde) to IIBG Holdings BSC, a transaction that was approved by the Cape Verdean antitrust authorities in May 2018;
f. In October 2017, Lone Star completed the acquisition of 75 per cent of Novo Banco, a bank that resulted from the transfer of part of Banco Espírito Santo’s businesses after its collapse in August 2014, for a global investment of €1 billion. Portugal’s bank resolution fund retained the remaining 25 per cent of Novo Banco;
g. In March 2018, Novo Banco sold the business of its Venezuelan subsidiary to Bancamiga, Banco Universal for an undisclosed amount;
h. In May 2018, Santander Totta (a Spanish bank) acquired Banco Popular Portugal for €1; and
i. In June 2019, Deutsche Bank completed the sale of the retail, private and commercial client business of its Portuguese branch to the Spanish bank Abanca.

ii. **Energy sector**

The energy sector has also been particularly active in the past few years.

As far as renewable energy is concerned, the past couple of years have seen some of the biggest wind asset portfolios being sold, including the sale of Iberwind to Chinese group Cheung Kong for €1 billion, the sale of Finerge to First State for €900 million and the sale of a stake in EDF Energies Nouvelles’ wind business in Portugal to Lancashire County Pension Fund, all in 2015. In June 2018, New Finerge, the company that acquired the Finerge wind farm business in 2015, acquired five companies engaged in the wind sector. In May 2019, Finerge announced the acquisition of two wind asset portfolios from Martifer and SPEE, and in June 2019 announced that it will be one of the bidders in the solar energy auctions to be launched by the government as from July 2019. In March 2019, Total Eren acquired from Novaenergia Fund the company Novenergia Holding Company, which owns, in particular, Generg, one of the biggest renewable energy players in Portugal that also has activities in six other European countries.

Several deals also took place in the gas sector. In October 2016, Marubeni and Toho Gas acquired from Gálp Gás a 22.5 per cent stake in its natural gas distribution business for €138 million. In March 2017, Artá completed the acquisition of Gascans from Portuguese private equity Explorer for €70 million. In February 2019, Gascans was then sold by Artá to UBS Asset Management for €100 million. In October 2017, REN completed the acquisition of EDP Gás from EDP for €532 million.
In 2018, Aquila Capital acquired the entire share capital of EDP Small Hydro, SA, a company engaged in the operation of hydro power plants, for €164 million.

The sale of Partex Oil and Gas by Fundação Gulbenkian to Thai company PTTEP for €622 million was announced in June 2019 and is expected to be completed by year-end.

### iii Real estate and construction sectors

The real estate sector contributes very significantly to the activity levels in Portuguese M&A, and 2018 confirmed this trend: real estate was the most active sector by number of deals, with some of the highest levels of activity ever seen.

Since 2017, the sale of shopping centres has been particularly prevalent. For instance:

- **a** in 2017, Fórum Coimbra and Fórum Viseu were sold by Locaviseu to Greenbay and Resilient for a global amount of €220 million;
- **b** in January 2018, Dolce Vita Tejo (the second-biggest shopping centre in Portugal) was sold by Baupost and Eurofund to AXA Investment Managers for €230 million;
- **c** also in January 2018, Sintra Retail Park, Fórum Sintra and Fórum Montijo, valued at €400 million, were sold by Blackstone to Auchan;
- **d** in July 2018, Blackstone sold Fórum Almada to Merlin Properties for €406.7 million; and
- **e** in April 2019, Leiria Shopping was sold by Sonae Sierra Fund to DWS Grundbesitz for €128 million.

The hospitality and residential sectors have also thrived, with deals such as the acquisition in December 2018 of the Penha Longa Hotel and Golf Resort by a joint venture formed by the Carlyle Group and Explorer Investments for €100 million, and the acquisition by Oaktree of a stake in Belas Clube de Campo, with a global investment estimated of €500 million.

Moreover, several logistic platforms were sold, such as:

- **a** in May 2017, EIPA II in Azambuja, totalling 54,640 square metres, was acquired by Deutsche Asset Management from ECS Capital;
- **b** in November 2017, Logicor (one of the largest European logistic platforms) was sold by Blackstone to China Investment Corporation for a global amount of €12.250 billion; and
- **c** in January 2018, four of DIA's logistic platforms in Spain and Portugal were acquired by Blackstone for €90 million.

Related to the dynamism seen in the real estate sector, the construction sector has also been quite active, with the sale of several construction companies such as Grupo Elevo (sold in September 2017 by Vallis Construction Sector for €90 million), Opway (sold in December 2017 by the company’s management team for an undisclosed amount) and Ramos Catarino (sold in May 2018 by the Catarino family for an undisclosed amount), all of which were acquired by Nacala Holdings.

In addition, Teixeira Duarte, one of the biggest Portuguese construction companies, put in place a divestment plan, in the context of which it sold Lagoas Park. SA in June 2018, the company that owns a business park near Lisbon, to the private equity fund Kildare for €375 million, and in August 2018, its 7.5 per cent stake in Lusoponte to Vinci and Mota-Engil for €23.3 million.

In January 2019, InterCement Brasil completed the sale of the Portuguese and Cape Verdean business of Cimpor to the Turkish group Oyak for €700 million.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

As a result of the financial crisis, and of the considerable decline of leveraged loan transactions and longer-term financings by bank syndicates, Portuguese companies have resorted to alternative sources of financing to support both their M&A investments and their current businesses. In particular, the issuance of corporate bonds (including high-yield bonds), as well as factoring and financial leases, have become more and more common.

Bank restructurings in Portugal have also opened a window of opportunity for an influx of alternative financing to traditional banking, notably through hedge funds, private equity and capital venture operations.

In particular, private equity funds, both local players and some of the major international private equity funds, have been quite active in Portugal, seeking to turn the recession into an advantage for specific investment transactions.

Additionally, a shift from Portuguese-style (short-form) documentation to Loan Market Association-based documentation governed by Portuguese law is a new trend noted in the banking sector, triggered by the risk aversion of Portuguese banks.

Currently, and in line with the revitalisation of the Portuguese market, banks are more willing to finance companies, both local and foreign investors (even though most foreign players obtain financing abroad). This contrasts with the situation seen until recently, where companies felt the need to go to foreign markets to obtain financing. In addition, financing through the issuance of bonds is becoming more and more common.

VII EMPLOYMENT LAW

No significant developments had an impact on M&A activity in the past 12 months.

However, it should be noted that the Portuguese market and legal community are still adjusting to the substantial amendments, approved by Law No. 14/2018, of 19 March, on the Portuguese Labour Code, which considerably changed the employment-related rules governing transfers of undertakings or parts of undertakings. In this regard, a special mention should be made about the now-express acknowledgement of employees’ right to oppose the transfer of their employment agreements upon a transfer of an undertaking or establishment.

In fact, the recent changes to the regime now expressly make it possible for employees who oppose a transfer to stay with their existing employer whenever such a transfer causes them serious damage. However, the amendments do not give a complete definition of what is to be considered serious damage but merely provide some abstract examples, such as where there is an evident lack of solvency or a precarious financial situation of the transferee, or even when, in the employees’ view, the transferee’s human resources policies do not warrant their trust. Considering the lack of conceptual rigour of these new rules, it will be up to the labour courts to determine how easy or difficult bringing an allegation of serious damage will be.

In the past year, the ultimate consequences of an employee’s objection to a transfer have also been called into question, given the unclear wording of the new provisions. In fact, if an employee objects to a transfer and stays with the transferor, the latter could refuse to keep the employee and force him or her to bring a lawsuit to prove the alleged serious damage. If successful, the employee’s right to stay with the transferor would be recognised, but it is unclear what would happen if the employee is unsuccessful. Would the employee be deemed to have transferred to the acquirer of the business? Will the illegal enforcement of the opposition right be qualified as a resignation without the right to compensation? The answer to these questions is unclear, and it will be up to the courts to provide additional guidance in this regard.
The opposition right is particularly ill-designed in respect of situations where a transferor ceases to exist (notably, in the case of a merger). The most sensitive solution would be to consider that the right of opposition could only determine that an employee would be entitled to terminate a employment agreement and claim the payment of an indemnity from the transferor (equivalent to the severance compensation paid in the event of redundancy), but until the courts issue rulings with this understanding, the answer will remain unclear.

It is also worth mentioning that the new changes also set forth that an employee who did not oppose the transfer of his or her employment agreement may later on terminate the contract with the acquirer of the business and demand payment of a compensation, if he or she sustains he or she has suffered serious damage as a result of the transfer. However, the deadline for enforcing this right is controversial: for instance, is there a statute of limitations or a deadline to operate the termination? Some scholars maintain that the right to terminate the agreement and claim the payment of severance compensation from the acquirer of the business would only be possible in relation to the transfer of an undertaking as a whole and not a (partial) transfer of a business. Again, this is also debatable and, given how recent these changes are, it is not yet possible to anticipate where the courts will stand in this matter.

These rules concerning a transfer of an undertaking entered into force on 20 March 2018 and apply to all such transfers occurring as of that date.

It should be stressed that these labour rules do not apply to share purchase deals. In fact, this regime merely concerns the transfer by any means (spin-off, merger, assignment, etc.) of an undertaking, an establishment, or part of an undertaking or an establishment constituting an autonomous unit.

VIII TAX LAW

No significant developments had an impact on M&A activity in the past 12 months. It should be noted, however, that the conditions for the qualification of the relevant shareholding under the participation exemption regime were changed as of January 2016 as follows: the minimum percentage of participation was increased from 5 to 10 per cent, but in turn, the minimum holding period required was decreased from 24 to 12 months prior to the distribution of dividends or the disposal of the relevant participation.

IX COMPETITION LAW

Even though no relevant modifications to the merger control legal framework were registered in the past year (the Portuguese merger control framework was further aligned with the EU merger control framework with the entry into force of the new Competition Act in 2012, which has remained materially unaltered since), the simplified filing form and pre-notification contacts have been increasingly used, enabling a swifter assessment and earlier decisions regarding uncomplicated matters.

To increase transparency, at the end of each year, the Portuguese Competition Authority (PCA) publishes its strategic priorities regarding competition policy for the following year on its website. According to a statement issued by the PCA, its main priorities for 2019 include the following:

a increasing the fight against cartels;

b reinforcing its ex officio capabilities to conduct investigations;
increasing knowledge on the use of algorithms or AI by companies that could lead to anticompetitive practices; and

do obtain greater celerity in merger control investigations.\textsuperscript{12}

In line with this set of priorities, the PCA continues to actively pursue its goal of protecting and promoting competition in the Portuguese economy.

With regard to merger control, the PCA is expected to continue to promote the use of the simplified filing form, as well as pre-notification contacts, to deliver swifter decisions and enhance transparency in the market. Moreover, it seems that the PCA’s merger control decisions are increasingly subject to judicial review. In 2015, the Portuguese Competition, Regulation and Supervision Court rejected, on one hand, the appeal by Media, Zon Optimus and Portugal Telecom related to the PCA’s decision to initiate an in-depth investigation of this concentration and, on the other, another claim by these undertakings alleging that the concentration had been tacitly approved.\textsuperscript{13}

Again in 2015, the Portuguese Competition, Regulation and Supervision Court confirmed the PCA’s decision in Arena Atlântida/Pavilhão Atlântico.\textsuperscript{14}

More recently, the PCA’s clearance decision of the SUMA/EGF concentration (a merger between two relevant companies operating at different levels of the Portuguese waste management market), which followed an in-depth investigation, was fully endorsed by the Portuguese Competition, Regulation and Supervision Court, as all the appeals introduced by several of the Portuguese municipalities and main competitors against the PCA’s approval were entirely dismissed by the Court.

\section*{X OUTLOOK}

M&A activity is expected to continue at a good pace in upcoming months.

The following point to the maintenance of the current levels of activity in the sector in Portugal:

a the continuing improvement of the Portuguese economy;

b the ring-fencing process and the restructuring of local players;

c increasing access to financing; and

d the sustained interest of foreign investors, including major international investment funds, in Portugal.

In addition, important deals are ongoing or in the pipeline, such as the sale of Altice’s Portuguese fibre business and the sale of Tranquilidade by Apollo.
Chapter 36

QATAR

Michiel Visser, Charbel Abou Charaf and Mohammed Basama

I OVERVIEW OF M&A ACTIVITY

During the past year, there has continued to be sustained M&A activity in the domestic market involving Qatari investors and institutions, while a significant number of outbound investments have focused primarily on Europe and the United States.

In the local market, Barwa Bank and International Bank of Qatar merged in what is the largest domestic M&A transaction in Qatar in 2019 thus far. Mergers of other Qatari banks and financial institutions are, however, still being considered.

That said, outbound activity remains the cornerstone of M&A in the region, as highlighted by the recent US$200 million investment by the Qatar Investment Authority (QIA), the sovereign wealth fund of the state of Qatar, in Airtel Africa, and the €506.8 million sale by Qatari Diar of its entire stake in French publicly listed company Veolia Environnement, representing approximately 26.1 million shares and 4.6 per cent of the share capital.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

i General overview of the legal system

In accordance with the 2004 Constitution, Shariah law is the primary source of Qatari legislation. In addition, legislation is based on the Civil Code and the Commercial Law. The Civil Code gives natural and legal persons the freedom to agree on all matters, without limitation, provided that their agreement does not conflict with the law, public policy or morality. The Commercial Law regulates commercial activities, business agencies, commercial concerns, trade names and commercial contracts in general. The Commercial Law also regulates banking transactions, bills of exchange, promissory notes and cheques, and provides a first set of substantive provisions regarding bankruptcy under Qatari law.

ii Other legal frameworks

While they see very little M&A activity, the Qatar Financial Centre (QFC), established by Law No. 7 of 2005, the Qatar Science and Technology Park (QSTP), established by Law

1 Michiel Visser is a partner, Charbel Abou Charaf is a local partner and Mohammed Basama is an associate at White & Case LLP.
2 Law No. 22 of 2004.
3 Law No. 27 of 2006.
No. 36 of 2005, and the Qatar Free Zones Authority (QFZA), established by Law No. 34 of 2005 as amended by Decree Law No. (21) of 2017, provide additional legal frameworks for companies in Qatar, with considerable advantages.

The QFC
Companies licensed by the QFC are subject to a separate set of rules and regulations that enable them to enjoy various commercial benefits related to M&A. However, given that most QFC firms are subsidiaries or branches of parent companies, there is rarely any M&A activity at the level of QFC entities. This trend could change, given recent developments at the QFC, with a noticeable increase in newly incorporated holding companies and special purpose vehicles that could be involved in M&A.

The QSTP
Similarly, the QSTP is a free zone, affiliated with Qatar Foundation, designed to promote and support research and development, technology and the investment activities that serve the objectives of the QSTP. It has rarely seen any M&A activity, given that its members are largely international companies.

The QFZA
The QFZA acts as a regulator for free zones in Qatar and aims to attract foreign direct investment in the free zones as well as encouraging domestic investors to expand internationally. Companies can be established in the free zone areas pursuant to the Free Zones Authority Companies Regulations 2018 and are thereafter regulated by the QFZA. The QFZA’s legal framework is relatively new and is still in the process of being fully established.

iii Corporate law
General overview
M&A activity is primarily governed by the new Companies Law. It is also regulated by the Qatar Financial Markets Authority’s Law No. 8 of 2012, as amended, and by the Law Regulating the Investment of Non-Qatari Capital in Economic Activity (New Foreign Investment Law).

Under the Companies Law, a company can have multiple forms. The two most widespread types of companies in Qatar are the limited liability company (LLC) and the joint-stock company (JSC) in the form of a private JSC.

iv Private acquisitions
Mergers
Under Qatari law, a merger occurs when one company is merged into another company, or one or more companies are merged into a new company. The merger contract will contain terms providing for, inter alia, an evaluation of the liabilities of the merged company and the number of shares allocated to the capital of the merging entity. The merger shall only be
valid if previously approved by the competent corporate bodies of the companies involved, in accordance with the respective articles of association (articles). Mergers in Qatar are rare, and the merger provisions of the Companies Law are consequently infrequently invoked.

**Demergers**

The Companies Law provides that a company can split into two or more companies, whereby each company will be deemed an independent legal entity and can take on any of the legal forms mentioned in subsection ii.

A demerger must be approved by a decision issued by the extraordinary general assembly (EGA) of the company, with the favourable vote of shareholders representing at least 75 per cent of the share capital. The resolution for demerger should outline the names of the shareholders and their shareholdings, the rights and obligations in respect of all the companies resulting from the demerger, as well as the manner by which assets and liabilities are to be distributed among them.

In the event that the shares of the company to be demerged are traded on Qatar’s main stock exchange, the Qatar Exchange, the shares of the companies resulting from the demerger shall be tradable upon issuance of the demerger decision.

Finally, it is important to note that the Companies Law allows shareholders that voted against the demerger to exit from the company. However, no further details are provided for in the Companies Law regarding the exit process.

**Acquisitions**

An acquisition will only be deemed valid if the following requirements are met:

a. the acquiring company and the target company must each issue a resolution by their respective EGA approving the acquisition and setting out the waiver of the right of first refusal of existing shareholders: these resolutions are to be certified by the Ministry of Commerce and Industry;

b. the acquiring company must issue a resolution to increase its capital and thereafter allocate that increase to the shareholders according to their shareholdings in the company, in accordance with its articles;

c. completion of the procedures to transfer ownership of the shares of the target, which will not be opposable until the shares are duly registered in accordance with the provisions in the Companies Law;

d. if the acquisition is a buyout, the acquiring company must pay the value of the shares and deposit the shares in a special account to distribute them to the shareholders that were registered at the time the EGA approved the sale of shares;

e. if the acquisition was made through a share or bond conversion, the acquiring company must submit those shares or bonds to the target for the target to distribute them to the shareholders that were registered at the time the EGA approved the acquisition;

f. the target must amend its constitutional documents, including the articles, and elect a new board of directors accordingly; and

g. the acquiring company must take all necessary measures to preserve the rights of the minority shareholders, including offering to purchase the stock or voting rights of the minority shareholders for a value not less than the value of the stocks or shares covered by the acquisition, or the value determined by an expert in accordance with the provisions of the Companies Law.
Public M&A

Overview of the Securities Market Regulation

The Qatar Financial Markets Authority (QFMA) is governed by Law No. 8 of 2012, which establishes the rights of the QFMA to regulate takeovers and mergers of public companies. The relevant rules and regulations issued by the QFMA are the Mergers and Acquisitions Rules of 2014, discussed in further detail in Section III. Although it was initially not mandatory for listed companies to comply with the Corporate Governance Code (CG Code), the version issued by the QFMA in 2016 operated a comply or clarify principle. However, the most recent version of the CG Code makes it of compulsory application to listed companies.

The QFMA rules and regulations provide specific listing, disclosure and notification requirements for listed companies.

M&A in certain regulated industries

While M&A activity is generally conducted in accordance with the above-mentioned steps, certain regulated industries provide for particular processes.

The financial sector

The Qatar Central Bank (QCB) is governed by the QCB Law, which details the mechanism for the merger of financial institutions, subject to the thresholds and procedures set out in the Companies Law and the restrictions set out in the New Foreign Investment Law.

Under the QCB Law, two or more financial institutions can merge in one of two ways: two or more companies can merge into a new company or the target can merge into the acquirer. In both cases, the following steps must be taken:

a. approval of the QCB for the merger is required;
b. a preliminary agreement, or plan of merger (called an initial agreement under the QCB Law), must be signed by the parties;
c. prior to signing such an agreement, a full due diligence review must be undertaken; and
d. an application for the merger containing certain documents and information must be submitted to the QCB, following which the Governor of the QCB has 60 days to issue a decision approving or rejecting the merger. That decision is appealable.

In addition, the QCB Law imposes the creation of committees at the level of the companies intending to merge, on which the QCB must be represented. The exchange of information between the merging companies is also strictly regulated: any exchange requires prior approval by the Governor of the QCB, and the content of the exchange and the identity of its recipients are restricted.

A merger can be imposed by the QCB on any financial institution facing problems that have a fundamental effect on its financial condition.

The QCB Law does not shed much light on the legal framework governing acquisitions of financial institutions, but addresses the issue in a single provision requiring the approval of the QCB on any acquisition, pursuant to the terms and conditions set by the QCB, and applying the benefits and privileges granted under the merger provisions to any such acquisition. In practice, it seems that the QCB is applying the acquisition provisions of the Companies Law as set out in subsection iv.

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**The telecommunications sector**

Legislation in the telecommunications sector consists of various laws and regulations. The main governing act is the Telecommunications Law (Telecom Law).\(^7\) As the regulator of this sector, the Supreme Council for Information and Technology (formerly known as ictQATAR and currently known as the Communications Regulatory Authority (CRA)) plays a key role.

The Executive By-Law for the Telecommunications Law (Executive By-Law)\(^8\) and various CRA notices and instructions, including the 2011 instruction regarding the calculation and payment of the licence fee and industry fee, and the 2012 Radio Spectrum Policy, have helped shape the sector.

The Telecom Law grants discretionary power to the CRA regarding changes of control. Under Article 13, the Executive By-Law also requires approval by the CRA if an individual licence is assigned to another person, where the term assignment includes a transfer of the licence or a change of control of a licensee.

Finally, the target company must deliver to the CRA written notification of an intended transaction no later than 60 days prior to the intended completion date of the transaction.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Until recently, the regulations on securities contained little more than basic provisions on tender offers for shares traded on the Qatar Stock Exchange. Consequently, the offer structure and content were primarily based on the contractual arrangements of the parties, which were often subject to considerable amendments resulting from the rather ‘heavy’ (but necessary) interaction with the QFMA to obtain guidance throughout each stage of the process. On 9 March 2014, the QFMA published the Merger & Acquisition Rules (M&A Rules), thereby providing a more comprehensive, albeit complex, legal framework for public takeovers.

i **The M&A Rules**

**Scope**

The M&A Rules have a wide scope of application, since they generally apply to all acquisitions or mergers where one of the parties is a listed company in Qatar (direct acquisitions) or a subsidiary of a listed company (indirect acquisitions).

**Exceptions**

With the exception of a few provisions, including certain disclosure obligations, the M&A Rules do not apply to: acquisitions or mergers performed outside the state of Qatar; and indirect acquisitions, provided that the subsidiary of the listed company has conducted business activities in the past three years, or where there was no conflict of interest between the listed company (or its subsidiary) and the counterparty to the acquisition or merger.

It is unclear from the M&A Rules whether the above conditions are mutually exclusive, or whether the ‘or’ should rather be read as ‘and’, thus rendering both conditions as requirements for the purposes of the exemption. A literal approach to interpretation would

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\(^7\) Decree-Law No. 34 of 2006.

\(^8\) ictQATAR Decision No. 1 of 2009.
militate against considering the conditions cumulative. Furthermore, there is no guidance in the M&A Rules as to what exactly would constitute a conflict of interest relevant in this context.

Notwithstanding this exemption, listed companies are required to comply with certain (rather substantial) disclosure obligations, both prior to an acquisition or merger, with respect to indirect acquisitions, and immediately upon approval being granted by the regulators of the offeree company with respect to acquisitions or mergers implemented outside the state, and at completion of the transaction in both cases.

**Pre-completion obligations**

In particular, with regard to pre-completion obligations, listed companies are required to disclose certain information to the QFMA and the market, including:

- **a** details of the offeror, the offeree company (i.e., the target), the major shareholders (i.e., shareholders owning 5 per cent or more of the share capital of a company), and the directors and senior executives;
- **b** with respect to indirect acquisitions only, details of the subsidiary, its business and the degree of dependency on the listed company;
- **c** details of the minimum and maximum number of shares that can be acquired under the offer;
- **d** the offer price;
- **e** the purpose of the acquisition or merger;
- **f** the envisaged timetable;
- **g** an indication of the consequences that the offer may have on the financial position of the listed company and its shareholders;
- **h** the advantages and disadvantages possibly arising from the acquisition or merger; and
- **i** the disclosure of any conflicts of interest among the offeror, the offeree, their independent advisers and ‘any person having a relationship with the acquisition or merger’ (collectively, concerned persons), the members of their respective board of directors or major shareholders.

**Completion obligations**

Immediately upon completion of an acquisition or a merger, listed companies are required to provide the QFMA and the market with a statement setting out the outcome of the transaction, including an indication of the actual percentage and value of the shares that have been acquired (to rectify any differences or discrepancies with the information disclosed in the previous communication mentioned above), and the effects of any difference on the content of any such previous disclosure. In addition, listed companies have to submit to the QFMA the execution copy of the merger or acquisition agreement.

Finally, the M&A Rules provide that if the procedures for the implementation of the acquisition or merger are not completed (it is not clear whether partial completion would be carved out), presumably within the timeline indicated within the timetable outlined below, a listed company is required to notify both the QFMA and the market of the reasons for this, and provide information as to whether it is expected that the situation will be temporary or final. Again, the M&A Rules appear incomplete, as they do not offer guidance on the triggering event of this disclosure obligation, nor specify the period within which this obligation must be complied with.
**Intention to launch an offer, application, timetable and offer document**

The M&A Rules require listed companies to immediately disclose to the QFMA and the market the intention to submit an offer, as well as any initial understandings with relevant parties concerning the offer. We believe that such a disclosure could not be made efficiently (without otherwise adversely affecting the outcome of the offer) prior to having reached a fair degree of certainty in respect of the actual intention to launch an offer.

Following that disclosure, the offeror is required to submit to the QFMA the following main documents: an application for the acquisition or merger, an offer document and a timetable for the implementation of the acquisition or merger (collectively, documentation).

**Timetable**

The M&A Rules require the offeror to submit to the QFMA a proposed timetable for the acquisition or merger within two weeks of the date of notification regarding the intention to launch an offer. The timetable must include, inter alia:

- the final offer document;
- an opinion issued by the board of directors of the offeree company; and
- proposals with respect to relevant dates, including:
  - the first permitted closing date of the offer;
  - the date on which the offeree company may announce its profits or dividends forecast, asset evaluation or proposal for dividend payments;
  - the date for the public announcement of the offer;
  - the final date for meeting all conditions; and
  - the final date by which to pay the relevant consideration to the shareholders of the offeree.

The M&A Rules do not provide guidance or further details in respect of the above-mentioned dates, and their actual meaning in this context is therefore unclear. The QFMA must be notified immediately if it becomes apparent that the offeror or the offeree is unable to comply with the timetable.

**Applicable time periods**

The offeror is required to provide the QFMA with the documentation at least 30 days prior to the date of the meeting of the EGA held to approve the offer. The offeror is also required to provide the shareholders with the offer document within three days of the QFMA’s approval of that document and at least 15 days before the date of the EGA meeting.

Unless the QFMA extends this period, the offeror must implement the offer within one month of the date on which the offer has been approved by the EGA, or of the date of approval of the offer document by the QFMA if the EGA has not been held.

**Additional disclosures**

During the offer period, listed companies are required to disclose (presumably to the QFMA and the market) any dealings of major shareholders concerning the securities that are the object of the offer. These include details of any person who, individually or jointly with minor children, a spouse or with others owns or becomes the owner of 5 per cent or more of the shares in the offeror or the offeree.
Post-completion obligations

A listed company is required to submit an acknowledgment to the QFMA confirming that completion of the acquisition or merger has occurred.

Mandatory offer

Every person who owns or intends to own, whether individually or with other persons, more than 75 per cent of the shares of the offeree company (relevant stake) is required to notify the QFMA thereof and submit a mandatory offer to buy all the remaining securities (mandatory offer). The mandatory offer must be launched within 30 days of the date on which the holding of the relevant stake is achieved. It is therefore unclear how (if at all) the obligations in relation to the mandatory offer apply to the mere intention or willingness to acquire a relevant stake.

Exemption from mandatory offer

The QFMA may grant a temporary exemption from the obligation to launch a mandatory offer provided that the relevant person owns a stake not exceeding 78 per cent of the share capital, and the 3 per cent in excess of the 75 per cent threshold set out above is disposed of within three months of the date on which the excess percentage was acquired by that person.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

While the two most widespread types of companies in Qatar are the LLC and the JSC, most foreign investors choose to do business in Qatar through an LLC form because of its lighter framework.

Through the establishment of the QFC, Qatar has promoted the country as a regional hub for international finance with the aim of attracting, inter alia, banking, financial services, insurance and corporate head office function businesses. As mentioned earlier, companies licensed by the QFC enjoy an array of commercial benefits, such as 100 per cent foreign ownership and a corporation tax rate of 10 per cent on all locally sourced profits. As a result, the QFC has seen a large number of international and regional banks, financial institutions and insurance companies open under the umbrella of the QFC Regulatory Authority.

Similarly, the QSTP and QFZA allow 100 per cent foreign ownership and for companies to sponsor foreign employees, resulting in the attraction of major international companies.

Foreign involvement in M&A transactions is largely governed by the New Foreign Investment Law. Under the Old Foreign Investment Law, the general rule was that foreign investors could invest a maximum of 49 per cent of the share capital of a Qatari company in all sectors of the national economy so long as the remaining 51 per cent of the share capital is owned by at least one Qatari partner.

The New Foreign Investment Law, which repealed the Old Foreign Investment Law, allows foreign investors to own up to 100 per cent of the share capital of a Qatari company, except in the case of banks, insurance companies and commercial agencies, and companies in any other sector that would be covered by a decision of the Council of Ministers. If a foreign investor wishes to hold more than 49 percent of the share capital of a company, an application must be made to the relevant department at the Ministry of Commerce and Industry.

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Pursuant to the New Foreign Investment Law, foreign companies can perform certain contracts in Qatar if a number of requirements are met, including the contract in question being performed through the foreign company’s Qatar branch, and the contract being with a ministry, governmental agency, public body, institution or company in which Qatar is a shareholder.

Benefits offered to foreign investors include the freedom to repatriate profits as the foreign investors deem fit, tax exemptions and exemptions in relation to customs duties regarding the importation of necessary equipment and materials.

With regard to foreign involvement in publicly listed companies, as a general rule, foreign investors can own up to 49 per cent of the shares listed on the Qatar Exchange upon approval by the Ministry of Commerce and Industry of the specific foreign ownership threshold set in the articles of that company. Moreover, a foreign investor can own more than 49 per cent of the shares of a publically listed company upon approval of the Council of Ministers.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The key trend in M&A activity has been to focus on the myriad opportunities for Qatari investors in the global market. Qatar’s most prominent investors, such as QIA, Ooredoo, Qatar Petroleum, Qatari Diar and Katara Hospitality, have been acquiring assets in both stable economies and emerging markets; note, however, that since the Brexit referendum, there have not been any major investments in the United Kingdom by any of the aforementioned major Qatari investors. This could mean that there are opportunities for Qatari institutions to benefit from investments in the UK market, whether in the real estate, finance, industry, hospitality, energy or sports sectors. In parallel, Qatari investors continue to invest in emerging markets, with a particular focus on real estate.

VI EMPLOYMENT LAW

The Labour Law\(^\text{10}\) provides the main framework for employment law and applies to Qatari employers and workers. However, it does not apply to the following individuals:

- employees and workers of corporations and companies established by Qatar Petroleum;
- employees and workers for government and public bodies, including the ministries;
- officers and members of the armed forces, the police and the maritime forces;
- temporary workers; and
- individuals working in domestic employment (including, without limitation, drivers, cooks and gardeners).

The main government body responsible for individuals working in Qatar is the Ministry of Labour.

With regard to business transactions, the main applicable provision of the Labour Law provides that employees of a target company, and their employment-related rights, obligations and benefits under the relevant employment relationships, transfer to the acquiring company. In turn, and given that the approval of the Ministry of Labour is required to transfer the

\(^{10}\) Law No. 14 of 2004.
sponsorship of individual employees, the acquiring company and the target company must coordinate with the Ministry of Labour to transfer the employees to the acquiring company. Where approval is given, employment relations between the employee and the acquiring company (or the new company) continue without interruption, and the transferor and the transferee are jointly and severally liable for an employee's pay or other claims deriving from the employment relationship that have fallen due before the transfer. Finally, under the Labour Law, a transfer of business does not, in itself, constitute a legal ground to terminate any employment relationship.

i  **Trade unions**

Although the Labour Law permits a single employees' committee to be formed by more than 100 Qatari employees employed by the same entity, trade unions are practically non-existent. The Labour Law requires minimum employee entitlements by which employers must abide, but can amend these if in favour of the employee.

ii  **Qatarisation**

Because of Qatarisation, whereby priority in employment is given to Qatari nationals, non-Qatari employees must demonstrate a need for their skills and the unavailability of a Qatari national to carry out the work, and acquire approval from the Ministry of Labour prior to commencement of the work.

iii  **Pension arrangements and social security**

Pension arrangements and social security are also regulated by the Labour Law: certain insurance and social security contributions for Qatari national employees are required. Moreover, pension schemes are allowed for foreign employees and may be elected by Qatari employees if they are more beneficial than the minimum benefits provided for by law.

iv  **Sponsorship**

Individuals require a valid residency permit and work permit, which may be applied for by an individual or an entity. In either case, the applicant is known as the worker's sponsor. Employees who hold a valid work permit must only perform work for their sponsors. Secondment of an employee to a third party requires approval from the Ministry of Labour and is often restricted in duration.

v  **Immigration law**

On 13 December 2016, the New Immigration Law\(^\text{11}\) regulating the entry, exit and residency of expatriates in Qatar entered into force, replacing the previous Immigration Law.\(^\text{12}\) The New Immigration Law provides notable changes, including the right for an expatriate working in Qatar to move between employers without the need for a non-objection letter from his or her existing employer (subject to the satisfaction of certain conditions), and appeals to a special committee, the Foreign Nationals Exit Grievances Council, in the event that the conduct of a current employer hinders or impedes the exit of an expatriate from the country.

\(^{11}\) Law No. 21 of 2015.

\(^{12}\) Law No. 4 of 2009.
The New Immigration Law has been amended by Law No. 21 of 2017. The amendments include expatriates’ right to exit the country for holiday and emergency reasons, and to leave Qatar permanently prior to the expiry of a employment contract, in each case subject to giving prior notice to the employer.

VII TAX LAW

Several taxes are worth mentioning in relation to the Qatari system: corporate income tax, withholding tax, capital gains and dividend tax, personal income tax, sales tax and double taxation.

The income tax system is subject to the Income Tax Law,\textsuperscript{13} under which a legal entity is considered a tax resident for tax purposes if the company is incorporated under Qatari law, is mainly located in Qatar or has its headquarters in Qatar.

A general flat tax rate of 10 per cent applies to profits arising out of taxable activity in Qatar, but a rate of at least 35 per cent applies to oil and gas operations.

Currently, withholding tax at a rate of 5 per cent is levied on all payments made to non-residents, including in relation to royalties and any other payments for services carried out wholly or partly in Qatar.

There is no capital gains tax or dividend tax on Qatari companies.

Similarly, personal income tax, sales tax and VAT are not imposed on operations in Qatar, although the Qatari authorities are examining the possibility of introducing VAT.

Qatar is a party to treaties for the avoidance of double taxation with several countries, which provide an important incentive for foreign investors operating in Qatar.

Entities licensed under the QFC are subject to a flat rate of 10 per cent on local-source profit but are not subject to withholding taxes. Wholly owned government entities incorporated in the QFC are exempt from taxes.

In the same way, entities licensed by the QSTP are fully exempt from Qatari corporate income tax, while entities licensed by the QFZA can benefit from renewable 20-year corporate tax holidays.

Finally, with regard to the financial sector, a preferential tax treatment may be granted by the QCB to a merging company or a new company resulting from a merger.

VIII COMPETITION LAW

Under the current legislative framework, there are no antitrust or merger control laws applicable to M&A transactions in Qatar. However, an antitrust culture is starting to emerge with the establishment of a De-monopolisation and Competition Protection Committee at the Ministry of Commerce and Industry, which has recently issued notices to large Qatari companies in relation to exclusivity and pricing matters.

\textsuperscript{13} Law No. 21 of 2009.
IX  DATA PROTECTION LAW

The Data Protection Law, which entered into force in May 2017, aims to establish a certain degree of protection for the processing of personal data by granting individuals the right to withdraw consent to that processing, the right to access and review information previously provided to the data controller, and to request deletions, modifications, or both, to any of the information. Moreover, data controllers will be required to put in place appropriate systems and procedures for the processing of personal data to avoid any leaks or unauthorised disclosure of information. Particular information (e.g., relating to race, religious beliefs, health and criminal records) will only be processed with the prior approval of the relevant administrative unit at the Ministry of Transport and Communications. Finally, the Data Protection Law imposes high financial penalties for non-compliance, ranging between 1 million and 5 million Qatari riyals.

X  OUTLOOK

Despite the fall in oil and gas prices in recent years, a heavy flow of investments into the infrastructure sector and the preparations for the FIFA World Cup in 2022 have continued apace. Moreover, there has been a significant boost in the media, retail and food industries. Other sectors that are expected to continue to grow steadily include construction, real estate, hospitality, fashion and technology.
Chapter 37

ROMANIA

Horea Popescu and Claudia Nagy

I OVERVIEW OF M&A ACTIVITY

According to the World Bank's Doing Business Report 2019, Romania is ranked 52nd worldwide on the aggregate ease of doing business index, seven positions lower than the previous year. However, Romania ranks first in the European and Central Asia areas with regards to the ease of doing business across borders, and is well above the average rankings of the region in areas such as getting credit, paying taxes and enforcing contracts.2

From an economic perspective, Romania was again one of the fastest-growing economies. According to estimates published by the Romanian National Institute of Statistics, the economy rose by 4.1 per cent year on year as compared to 2017 (compared with 7 per cent year on year the previous year).3 As compared to 2017, there was a slight decrease in M&A activity after a particularly active 2017 characterised by a significant number of high-value deals. However, M&A activity seen in 2018 represents the evolution of a year of economic growth. Investment activity was broadly spread across the telecoms and IT, real estate and construction, manufacturing and education and healthcare services sectors.

In 2018, there were approximately 130 transactions totalling approximately €1.9 billion only including transactions with a listed value, while the value of all transactions, including unlisted ones, is approximated at between €3.8 and €4.3 billion. Of the 130 transactions in 2018, 26 deals were in the telecoms and IT sector, 24 in the real estate and construction sector, 23 in manufacturing, 11 in education and healthcare services, nine in wholesale and retail, eight in the services sector, six in the finance and insurance sector, five in the agriculture and farming sector, and 18 in other sectors.4

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The general framework for M&A activity in Romania is mainly governed by the Civil Code and Company Law, as republished and further amended and supplemented (Company Law).5 The Civil Code provides the general legal framework governing legal entities as well as the general principles applicable to mergers and demergers. The Company Law provides the applicable rules for the sale and purchase of shareholdings in Romanian companies, as well as those applicable for share capital increases, mergers and spin-offs.

1 Horea Popescu is a partner and Claudia Nagy is a senior associate at CMS Romania.
2 http://www.doingbusiness.org/content/dam/doingBusiness/country/rt/romania/ROM.pdf.
4 Emerging Europe M&A Report 2018/189, CMS in cooperation with EMIS.
5 Company Law No. 31/1990.
On a more practical note, registrations with the Trade Registry (which is the method for publicising operations of companies) follow the rules established by Trade Registry Law, as republished and further amended and supplemented, in addition to ancillary regulations. Depending on the business activity of the target company, the following sector regulations may also be applicable:

a for public companies, the Capital Markets Law and various secondary enactments likely apply, as will Regulation 1/2006 on Issuers and Securities Operations, as further amended and supplemented, in particular by Law No. 24/2017. Public companies come under the supervision of the Financial Supervisory Authority (FSA);

b for insurance companies, the general framework is set forth in Law No. 237/2015 on the authorisation and functioning of insurance and reinsurance activities, and the supervision of the FSA also applies; and

c for banks, the main legislative framework is set forth by Government Emergency Ordinance No. 99/2006 on credit institutions and Regulation No. 5/2013 of the National Bank of Romania (NBR), and the supervision of the NBR also applies. Investors doing business in Europe may find Romanian regulations somewhat familiar, as they are the product of the implementation of EU directives into Romanian law.

Law No. 137/2002 is the main piece of legislation governing company privatisations, which continue to be of interest to many major companies that are still state-owned.

Competition law is also relevant in the M&A field, as economic concentrations between companies must be controlled and competition must remain fair at all times. The Competition Law, as republished and further amended and supplemented, is related to regulations and EU competition law, and contains provisions on notifications to the Competition Council and the European Commission, and the related requirements and thresholds.

In addition to the above, other legal provisions applicable to the particularities of each transaction may become relevant. These include, for example, environmental law, employment law and insolvency law.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Insurance, capital markets and pensions

Following the entry into force of Law No. 24/2017 regarding issuers of financial instruments and market operations, the FSA issued Regulation No. 5/2018 regarding issuers of financial instruments and market operations in order to align the legal framework in the capital markets sector.

In 2018, another significant legislative novelty entered into force, namely Law No. 126/2018 on markets in financial instruments, implementing MiFID II in Romania.  

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6 Trade Registry Law No. 26/1990.
7 Law No. 297/2004 on capital markets.
8 Competition Law No. 21/1996.
Law No. 126/2018 applies to investment firms, market operators, data reporting service providers, central depositaries, central counterparties and investment firms from other Member States operating in Romania, directly or through a branch, and to companies from third countries providing investment services or carrying out other investment activities in Romania through a branch. According to Law No. 126/2018, the competent supervisory authority is the FSA; however, the NBR has special supervisory powers related to the investment services carried out by Romanian credit institutions as well as by the Romanian branches of credit institutions authorised in other Member States.

ii  Energy

At the end of 2018, Government Emergency Ordinance 114/2018 (GEO 114) introduced several tax and regulatory measures for various major industries, including the energy sector. In this respect, the main amendments for the energy sector are as follows:

a  the applicability of the tax on the exploitation of natural resources is to be extended until 31 December 2021;

b  capping natural gas prices: from 1 May 2019 to 28 February 2022, producers, including their subsidiaries and affiliates belonging to the same economic interest group, carrying out both extraction activities and sales activities of natural gas extracted from the territory of Romania, have the obligation to sell at a price of 68 lei per MWh the natural gas resulting from current domestic production activities to the suppliers of natural gas for household customers, and natural gas for heat producers used for the production of heat in cogeneration plants and thermal plants serving public consumption;

c  a 2 per cent tax on turnover to be charged to licence holders in the sector of electricity and thermal energy produced in cogeneration and in the natural gas sector (with the exception of coal-based power generation capacities and electric and thermal energy cogeneration plants); and

d  household customers will benefit from regulated electricity prices between 1 March 2019 and 28 February 2022; household customers were also granted the right to return to regulated electricity prices.

Notwithstanding the above, it is important to note that there is significant opposition from the business environment with respect to GEO 114. There are currently ongoing discussions between the business environment and public authorities to discuss the provisions of GEO 114, which can be further amended through the law that has to approve GEO 114.

In addition, the law for promoting eco-friendly transportation entered into force in January 2018. Under this law, 30 per cent of public transportation purchased by local authorities must be green technology vehicles, such as electric, hybrid, hybrid plug-in, hydrogen (FCV), compressed natural gas propulsion engines, liquefied natural gas propulsion engines and biogas engines. In addition, starting from 2020, private transportation companies (including taxi companies) must purchase electric vehicles in proportion of at least 30 per cent of their fleet.
iii  Tax and tariffs

As further detailed in Section VIII, there have been numerous amendments to the tax legislation, the most important of which are as follows:

a  Government Emergency Ordinance No. 114/2018 on the introduction of measures in the field of public investments and fiscal measures, the amendment and completion of some normative acts and the extension of certain deadlines, introduced significant measures affecting several sectors, as follows:

- tax exemptions with respect to personal income tax for employees in the construction sector;
- health insurance contributions for dividend income; and
- the application of the VAT reverse charge mechanism has been prolonged for several sectors;

b  through Government Emergency Ordinance No. 89/2018 regarding certain fiscal-budgetary measures and amending and completing certain normative acts, a 5 per cent VAT reduction was implemented with respect to several categories of transport services; and

c  Government Emergency Ordinance No. 25/2018 for the repeal of certain legal provisions in the field of publicly funded investments introduces the following amendments:

- borrowing costs that are higher than the deductible threshold of €1 million are deductible for the period in which they were incurred up to 30 per cent of the calculation base;
- ending the public listing of individual bad debtors;
- a VAT adjustment for bad debts can be performed starting from the moment when the bankruptcy procedure is opened, based on a judge's decision.

IV  FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

According to the NBR balance of payments and external debt information for December 2018, foreign direct investment in Romania amounted to approximately €4.9 billion in 2018, as compared €4.8 in 2017.11

The industrial, telecoms and IT and real estate and construction sectors attract the largest share of foreign direct investment. Other attractive sectors, including consumer goods, agribusiness, retail and energy, have also attracted investors. In terms of geographical regions, the areas that attract the most foreign capital are (in order of importance) Bucharest, the centre and the south.12

Romania has numerous advantages for foreign investors: in addition to a large domestic market, the country has a strong industrial tradition coupled with low labour costs and taxes (among the lowest in the European Union).

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12  InvestingRomania.com reports based on the following sources of information: AGERPRES news, analysis and estimates of financial analysts, current and periodic reports submitted to the Bucharest Stock Exchange, and news coming from listed companies.
In this respect, it is clear that Romania actively seeks foreign direct investment, and has taken steps to strengthen tax administration, enhance transparency and create legal means to resolve contract disputes expeditiously. However, the pace of privatisation and restructuring of state-owned enterprises has slowed, yielding mixed results in this respect.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

According to merger market reports, in 2018 there were several transactions in Romania valued at over €100 million. The most attractive sectors for investors in 2018 were energy, manufacturing, IT, banking and financial services, and pharmaceuticals and healthcare.

i Manufacturing

ArcelorMittal, the world’s largest steel producer, sold steel plants in several European countries, including in Romania, to Liberty House for an undisclosed amount. ArcelorMittal Galati is the largest iron-processing plant in Romania. In recent years, ArcelorMittal Galați has recorded average production of approximately 2 million tonnes of steel per year and employs about 7,000 people. The Liberty House Group is headquartered in London and is engaged in metal recycling, steel and aluminium processing, and is part of GFG Alliance, a global group of companies in the energy, mining, metallurgy, engineering, logistics and financial services. GFC Alliance is present in about 30 countries, with an annual turnover of over €13 billion.

Damen Shipyards Group NV completed its acquisition of the Mangalia shipyard. In 2017, a Netherlands-based company engaged in shipbuilding and related maintenance and repair activities, agreed to acquire a 51 per cent stake in Daewoo-Mangalia Heavy Industries SA, a Romania-based shipbuilder and repair services company, from Daewoo Shipbuilding & Marine Engineering Co, Ltd, a listed South Korea-based shipbuilding and offshore company, for a total consideration of €22 million. The Mangalia shipyard, located on the Black Sea, has three drydocks and was a joint venture between Daewoo Shipbuilding & Marine Engineering (DSME) and the Romanian government in 1997. In 2018, the Romanian government informed DSME to exercise its preemption rights over the target sale, and Damen Shipyards Group entered into negotiations with the government regarding the Mangalia shipyard.

Unilever completed the acquisition of Betty Ice, the Competition Council approving the transaction on the basis of voluntary commitments by the Anglo–Dutch giant. Betty Ice was founded in 1994, and is the most important local ice cream producer in Romania with a total turnover of €30 million. The company owns a factory in Suceava and has over 180 ice cream kiosks open during the summer. Unilever is one of the world’s leading consumer goods companies, selling around 400 brands in over 190 countries.

ii Real estate

The largest transaction registered in 2018 was Dedeman’s acquisition of The Bridge office project from Forte Partners for an amount of more than €150 million. Dedeman is a resident group of companies that had a turnover of approximately €1.37 billion in 2017, and is one of the largest Romanian employers with more than 10,000 employees, and the largest retail network, including 48 DIY stores, two logistics centres and a private car park. The group was also active in previous years acquiring, among other things, a 50 per cent stake in Cemacon, a Romanian brick manufacturer, and over 23 per cent of Alro Slatina, the only producer of primary aluminium and alloys in Romania.
Lion’s Head Investments, a joint venture between Old Mutual (South African) and AG Capital (Bulgarian), acquired the Oregon Park office project developed by Portland Trust and Ares Management LP. The transaction had a value of approximately €135 million. Lion’s Head is a long-term real estate investor focused on value-added properties in Southeastern Europe already present in Sofia. The Oregon Park project has an area of 35,000m² that is leased entirely to multinational companies. AG Capital is a regional investment fund made up of investment and real estate development, consulting and asset management companies. Old Mutual Property is one of the most important South African investors with more than 40 years of experience, being part of the Old Mutual Group.

iii  Banking and finance

Romanian investment fund SIF Oltenia has signed a deal for the sale of its 6.29 per cent stake in Banca Comerciala Romana (BCR) to Austria’s Erste Group for €141.7 million. BCR, a member of the Erste Group, is the most important financial group in Romania, considering the operations of the universal bank (retail, corporate and investment banking, treasury and capital markets), as well as companies in the leasing market, private pensions and housing banks. BCR is the No. 1 bank in Romania by asset value (over €15 billion), the No. 1 bank by number of clients and the No. 1 bank on the saving and lending segments.

Leumi Bank has completed negotiations for the sale of its operation in Romania to Argo Financials Fund Limited, an investment fund of Argo Group Limited for an amount of €110 million. Argo Group Limited specialises in investing in emerging markets through the funds it manages. Currently, Argo Group Limited manages several funds investing in instruments with fixed income, non-performing loans and real estate.

iv  Pharmaceuticals

Advent International, one of the largest and most experienced global private equity investors, completed its acquisition of Zentiva, including Zentiva Romania SA, Sanofi’s European generics business for €1.9 billion. Advent is one of the largest and most experienced global private equity investors active in the healthcare sector. This transaction is part of Sanofi’s plans to simplify and reshape the company by removing non-core businesses.

The Phoenix group has acquired the Romanian pharmaceutical wholesaler Farmexim SA and the Help Net Farma SA nationwide pharmacy chain. Farmexim is one of the largest pharmaceutical wholesalers in the country, with 800 employees and 10 national distribution centres, while the pharmacy chain Help Net operates approximately 220 pharmacies and has 1,600 employees. German group Phoenix is one of the world’s largest pharmaceutical companies with annual business of over €20 billion, and is present in 26 countries. In total, Phoenix operates over 2,000 pharmacies in 26 states across Europe.

v  Telecoms and IT

The largest transaction of 2018 was the sale of Liberty Global’s European assets to Vodafone. Liberty Global, the world’s largest international cable business, sold its European assets to Vodafone for an amount of €18.4 billion. The transaction included the sale of Liberty’s Unity media business in Germany, as well as its UPC brand businesses across the Czech Republic, Hungary and Romania. The deal is part of Vodafone’s push to become the leading next generation network owner in Europe. Vodafone Romania is Romania’s second-largest mobile provider, while UPC Romania is the second-largest next generation network operator in Romania.
Cognizant Technology Solutions acquired Softvision, a privately held digital engineering and consulting company focused on the agile development of innovative software solutions and platforms, for an estimated amount of €478.2 million. Cognizant Technology Solutions is an IT solutions provider and one of Fortune 500’s fastest-growing companies.

UiPath, a leading enterprise robotic process automation (RPA) software company, has raised more than €131 million in Series B funding following a year of record growth. The company eclipses €942 million in terms of valuation, and validates RPA as a strategic imperative for digital transformation and the path towards artificial intelligence. This latest round was led by previous backer Accel, along with participation from new investors CapitalG (one of Google’s investment vehicles) and Kleiner Perkins Caulfield & Byers, as well as previous investors Earlybird, Credo Ventures and Seedcamp.

vi Agribusiness
Al Dahra Holding took over Agricost Braila, the largest agricultural producer in Romania, in a deal estimated at over €225 million. Al Dahra is part of Al Ain Holding, controlled by Sheikh Hamdan Bin Zayed Al Nahyan, former Deputy Prime Minister of the United Arab Emirates. The group operates in more than 20 countries, owns and operates an area of more than 200,000 hectares, eight forage presses and production, four rice milling units and two flour grinders. The investment fund intends to purchase additional agricultural land in Romania, and will invest in modernising the existing portfolio of agricultural machinery and technologies.

vii Transportation & Logistics
Private equity fund Mid Europa Partners acquired Urgent Cargus, Romania’s second-largest courier operator, from Abris Capital Partners for €120 million. Urgent Cargus operates a fleet of over 2,600 vehicles, with about 2,900 employees and collaborators and a national network of 72 centres and warehouses. In 2017, Urgent Cargus reported turnover of €80 million and net profits of €0.44 million. Mid Europa Partners is among the largest private investors in Central and Eastern Europe, with approximately €5.1 billion of managed assets.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS
In 2018, the theoretical indebtedness capacity in transactions was estimated at €1.5 billion, 75 per cent of it being financed by equity sources. However, the banks are proving increasingly willing to finance transactions. As such, more mixed financing is expected to be seen in the future through credits and private financing.

Pursuant to NBR data, in 2018, credit standards continued the trend of marginal tightening recorded in the previous period. For 2019, banks expect credit standards to tighten further for all categories of companies, both for long-term and short-term loans. While there has been a moderate increase in credit requests from large companies, small and medium-sized enterprises’ requests for short-term loans have increased significantly, while the number of requests for long-term loans has increased only marginally.

In addition to the above, EU membership enables potential investors to seek financial support through EU structural and cohesion funds. Such financing mostly comes in the form of development grants. A variety of investment incentives are available to applicants active in different economic sectors, in particular to small and medium-sized enterprises, an area with significant potential in Romania. The most relevant programmes for investors are:
Romania

a the Sectoral Operational Programme ‘Increase of Economic Competitiveness’ (POS CCE);
b the Regional Operational Programme (POR);
c the Sectoral Operational Programme ‘Human Resources Development’ (POS DRU); and
d the National Programme for Rural Development (PNDR).

VII EMPLOYMENT LAW

From an M&A perspective, the rules governing the transfer of employees in an asset deal, set out by the Law on Safeguarding Employees’ Rights in the Event of Transfers of Undertakings, Businesses or Parts of Undertakings or Businesses (TUPE Law),13 which transposes EU Directive 2001/23/EC, should be considered.

Under the TUPE Law, in order to protect employees, every time a transfer of an undertaking (or a part thereof) occurs, all of the transferred undertaking’s employees are transferred automatically by operation of law (no consent is required from the transferor, the transferee or the employees), and no cherry-picking is allowed. The purchaser must observe all rights and obligations resulting from existing employment contracts at the time of the transfer, and has the obligation to honour all rights until the relevant contracts expire or are terminated. However, the purchaser has the opportunity to renegotiate the collective agreement with the employees’ representatives one year after the transfer date.

In general, share deals do not impact employment relations at the target level (or at the subsidiary level), as the identity of the employer remains the same. Romanian legislation does, however, set out general employee-related information and consultation requirements in the context of M&A transactions, but they only apply if a proposed share deal significantly impacts working conditions. Even if the law provides that a consultation should be carried out regarding decisions that could significantly affect employees, there is no express obligation to accept employees’ proposals or to sign any related agreements. However, failure to comply with the information and consultation requirements may be sanctioned with fines.

In addition, in the case of a voluntary takeover of a public company, the target’s board must inform its employees of the terms of the takeover and the board’s position on the attempted takeover, as set out in FSA Regulation No.5/2018. The target’s employees may issue a written opinion on the matter to be provided to the bidder, the shareholders and the market.

As regards recent developments from an employment law perspective, these have been limited, and the more material ones are tax-related (as further detailed in Section VIII). In addition, the following legislation was enacted:
a Law No. 176/2018 implementing more restrictive regulations for employers who organise internships;
b GEO No. 26/2019 establishing new provisions on various labour areas, such as setting up a special register for day-to-day workers, additional annual leave for employees following in vitro fertilisation procedures;
c Government Decision No. 584/2018 regulating additional employee protection from risks related to the presence of chemical agents;

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13 Law No. 67/2006 on Safeguarding Employees’ Rights in the Event of Transfers of Undertakings, Businesses or Parts of Undertakings or Businesses.
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\[ d \quad \text{GEO No. 60/2018 implementing additional facilities for employers who hire unemployed people, or conclude apprenticeship contracts or traineeship contracts;}
\]

\[ e \quad \text{Law No. 165/2018, creating a unitary framework for the following types of tickets: gift vouchers, meal vouchers, crèche tickets, cultural vouchers and holiday vouchers that can be issued both on paper and on electronic support. The amounts corresponding to these tickets provided by an employer are deductible for the purposes of income tax; and}
\]

\[ f \quad \text{Government Decision No. 937/2018 providing the new minimum wage in Romania (i.e., approximately €443 per month).}
\]

**VIII TAX LAW**

On 29 December 2018, Government Emergency Ordinance No. 114/2018 on the introduction of measures in the field of public investments and fiscal measures, the amendment and completion of some normative acts and the extension of certain deadlines, which adopted significant measures affecting several sectors, was published in the Official Gazette and has entered into force, and introduce the following key tax amendments:

\[ a \quad \text{tax exemptions for employees in the construction sector: from 1 January 2019 to 31 December 2028, individuals working for employers that carry out construction activities, or in the fields of manufacturing construction materials, are exempt from personal income tax as follows:}
\]

\[ \quad \text{• the exemption will apply if at least 80 per cent of the employer’s turnover is derived from the above-mentioned activities. The turnover will be determined from the beginning of the year, including the month when the exemption is applied;}
\]

\[ \quad \text{• to be able to apply for this exemption, individuals must have gross income of between approximately €638 and €6,380 received on the basis of an employment agreement; and}
\]

\[ \quad \text{• this law also impacts the labour insurance contribution due by employers, which has been reduced to approximately 0.34 per cent;}
\]

\[ b \quad \text{a health insurance contribution for dividend income. Any income from dividends taken into consideration for the calculation of a health insurance contribution is the income distributed and received as of 2018. Dividends distributed before 2018 but received in 2018 are excluded; and}
\]

\[ c \quad \text{a VAT reverse charge mechanism. The application of the VAT reverse charge mechanism has been extended until 30 June 2022 for the following: supplies of cereals and industrial crops, transfers of allowances to emit greenhouse gases, supplies of electricity, green certificates, mobile telephones, integrated circuit devices, game consoles, tablet PCs and laptops.}
\]

Government Emergency Ordinance No. 89/2018 regarding certain fiscal-budgetary measures and amending and completing some normative acts sets forth a 5 per cent VAT that started on 13 January 2019 applicable to the following transport services:

\[ a \quad \text{train or historic steam vehicles on narrow lines used for tourism or leisure;}
\]

\[ b \quad \text{cable installations (cable cars, chairs or ski lifts) used for tourism or leisure;}
\]

\[ c \quad \text{vehicles having animal traction used for tourism or leisure; and}
\]

\[ d \quad \text{boats used for tourism or leisure.}
\]
Pursuant to Government Emergency Ordinance No. 25/2018 for the repeal of certain legal provisions in the field of publicly funded investments, starting 1 January 2019 (or the first day of the fiscal year), borrowing costs that are higher than the deductible threshold of €1 million are deductible for the period in which they were incurred up to 30 per cent of the calculation base. Furthermore, the Emergency Ordinance put an end to tax collection agency ANAF’s obligation to publish online a list of taxpayers with outstanding tax liabilities exceeding approximately €21,246 in the case of individuals carrying on independent activities, and approximately €3,187 in the case of other individuals; and allows a VAT adjustment for bad debts to be performed starting from the moment when a bankruptcy procedure is opened, based on a judge’s decision (and not only after a definitive decision is issued by a judge for closing the bankruptcy procedure of a debtor). If a bankruptcy procedure has begun and is not yet finalised, the VAT adjustment can also be applied beginning 1 January 2019.

IX  COMPETITION LAW

There was limited development of competition legislation in Romania during the past year. In this respect, the Romanian Competition Council published new guidelines regarding the individualisation of sanctions for contraventions set forth in Article 55 of the Competition Law, which brings further clarity to the terms and conditions under which companies are sanctioned by the authority for breaches of competition law. Furthermore, it clarifies the turnover to be considered for sanctioning purposes in the case of a non-resident, referring to the group turnover generated within the territory of Romania.

X  OUTLOOK

After four favourable years, specialists estimate that the Romanian M&A market will continue its positive trend, despite a degree of slowdown in the market. The record transactions of previous years have opened the gate for similar deals, and Romania appears to be on the radar of big investors. Technology start-ups are also expected to grow and attract investors keen on tapping into the potential of entrepreneurs. In addition, local entrepreneurs, taking advantage of the constant economic growth and improved financial situations, seem to be waiting for the right moment or offer to make their exit, thus attracting foreign companies and investment funds in the market.

The telecoms and IT sector has proven to be the star of the M&A market, and is predicted to further generate a greater number of high-value transactions. In this regard, the cybersecurity groups Bitdefender and UiPath are the most eminent examples, and have also generated some of the biggest transaction yet seen in Romania.

The combination of strong and constant economic growth, the desire and need to modernise a variety of public services and the political will to work with the private sector will lead to increasing investments in Romanian infrastructure. With 16 large public–private partnerships approved for the next two to four years in 2018 alone, this positive trend is due to continue and generate further transactions on the market.

Looking forward, we also expect increased interest in domestic M&A transactions of local companies that will want to consolidate the segments in which they operate or enter new sectors. Romania has seen a number of local companies that have successfully become national champions capable of international expansion and strong economic growth, which makes Romanian investment more possible in the region.
Overall, 2019 also seems bright for the Romanian M&A market, which has good macroeconomic prospects where companies, whether local or foreign, have more funds available for investment, generating high hopes for increased dynamism.
I Overview of M&A Activity

Views as to the state of the current Russian M&A market vary. On the one hand, generally business activity is not very high due to a number of reasons (international sanctions, the average quality of the investment climate, lack of a high number of well-developed industries). On the other, every week information about this and notable deals appears in the mass media or becomes known through other sources. Thus, in 2018 and early 2019, the following transactions caught a substantial amount of the business community’s attention:

a. the acquisition by VTB Bank of a 29 per cent share in major food and drinks retailer Magnit from its founder Sergey Galitskiy for approximately US$2.2 billion. Subsequently, 11.82 per cent of Magnit’s shares were disposed of by VTB to Alexander Vinokurov’s Marathon Group for approximately US$1 billion;

b. the acquisition by consumer electronics retailer M.Video of the Russian business of its German competitor Media Markt. That deal was part of a larger transaction involving an acquisition by Media Markt of a 15 per cent share in M.Video for US$470 million comprising US$300 million in cash, and of Media Markt’s Russian business valued at US$170 million. This is important, since from that perspective the deal looks not like a foreign party leaving the Russian market, but rather vice versa, as it investing into Russian economy;

c. the merger of Uber’s business in Russia, Armenia, Azerbaijan, Belarus, Georgia and Kazakhstan with its Russian analogue; Yandex Taxi;

d. the acquisition by the largest Russian insurance company SOGAZ of VTB’s insurance business. The united company’s net assets are estimated at about US$10 billion to US$11 billion;

e. the acquisition by Alexey Mordashov’s Severgroup of 41.9 per cent of the shares in Lenta, one of the largest Russian food and drinks retailers, from EBRD and TPG private equity fund for approximately US$730 million. As of the date of writing, a tender offer to minority shareholders is open. The deal is notable due to the attempt of certain minority shareholders to reverse the sale. Their main argument was that Lenta’s board of directors did not properly assess other possible sale options, as there was a competing proposal from Magnit whose terms, it is reported, were better; and

1 Alexander Vaneev is a partner, Denis Durashkin is a senior associate and Anton Patkin is an associate at BGP Litigation.
2 Hereinafter any statements, data, facts, forecasts, estimates, etc., are made as of May 2019.
Russia

f another resonant matter is the merger between two alcohol retailers, Krasnoye & Beloye and Bristol, and food retailer Dixy. The united company is expected to become third-largest food and drinks retailer in Russia.

Thus, the retail sector (whether food and drinks, taxi services or other retail activities) remains very active, and more deals may be expected during the second and fourth quarters of 2019 and early 2020.

At the same time, oil and gas industry is traditionally hot in Russia, albeit the oil price declining in recent years. Some recent deals worth emphasising are as follows:

a the acquisition of three 10 per cent shares in Novatek’s Arctic LNG-2 by, respectively, Total and Chinese CNODC (CNPC’s subsidiary) and CNOOC. Each 10 per cent share is valued at about US$2.5 billion. It is notable that, in order to meet the tight deadlines involved, Novatek and Total managed to arrange with the antimonopoly and foreign investment authorities in Russia a way to avoid the immediate prior regulatory clearing of the deal. This was achieved by way of pledging the respective 10 per cent share to Sberbank. Thus, Total having to obtain specified governmental consents has been postponed until the end of that pledge; and

b the dissolution of the joint venture (JV) between Glencore and Qatar Investment Authority (QIA), formed to obtain a 19.5 per cent share in Rosneft for €10.2 billion in early 2017. As a result, QIA will hold a 18.93 per cent share and Glencore will hold a 0.57 per cent share in Rosneft.

Further, there were some more large deals in the hi-tech, digital and TMT areas:

a the formation of the JV between Mail.Ru, Megafon, Alibaba and Russian Direct Investment Fund (RDIF) aimed at the further promotion of e-commerce in Russia;

b the formation of the JV between Megafon, Gazprombank, Rostec and Alisher Usmanov’s USM aimed at the development of the IT and digital economy;

c the acquisition by Sberbank of a 46.5 per cent share in one of the leading internet holdings, Rambler, for approximately US$150 million, which may be viewed as a conversion into equity of Sberbank’s loan to Rambler’s principal shareholder, Alexander Mamut; and

d the acquisition by VTB (which may be seen as one of the most active players of Russian M&A market) of the following TV assets:

- a 75 per cent share in STS Media from Ivan Tavrin. The acquisition was made through VTB’s JV with Yuri Kovalchuk’s and Alexey Mordashov’s National Media Group (NMG); and
- a 20 per cent share in First Channel from Roman Abramovich. This asset is also owned by VTB together with NMG (but each holds its share directly, not through their JV).

In addition, the possible acquisition by Sberbank of not less than 30 per cent of the shares of Yandex (considered the Russian Google) was announced in October 2018. From stock exchange quotations, it appears that this piece of news was perceived negatively by the market. Further information on the potential deal is not available.

It must be added that the digital sector is one of the few sectors in Russia today that is demonstrating sustained growth. However, a substantial part of such deals are early stage (pre-seed) investments. Transaction values in most cases are between US$1 million and

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US$10 million. It should be noted that a substantial part of the relevant information and data are not available to the public. However, it venture capital (VC) is one of the most attractive spheres for M&A lawyers in Russia in 2019.

The same, unfortunately, cannot be said about the Russian private equity (PE) sector. Most of the information on PE deals is also not available to the public; therefore, again, there may be various facts and indicators known only to the market participants. However, we possess information such that it may be estimated that there has been low to medium PE activity in Russia as of May 2019.

Finally, it is important to note that some of the deals are being made in quite distressed surroundings, as, for example, the following:

- the invalidation by the High Court (UK) of the application of UC Rusal for the US$770 million sale of a 2.1 per cent share in Norilsk Nickel by Roman Abramovich to Vladimir Potanin. The Court held that such sale violates the shareholders’ agreement made between the said parties in relation to Norilsk Nickel;
- the acquisition by Transneft of a 25 per cent share in Novorossiysk Commercial Sea Port for US$750 million from Summa Group. The deal was negotiated alongside the arrest of and criminal investigation against Summa’s principal ultimate beneficial owners (UBOs), brothers Ziyavudin and Magomed Magomedov; and
- the recent arrest of Michael Calvey, founder and managing partner of Baring Vostok Capital Partners PE fund, as well as of some of his colleagues and business partners, is also linked to alleged violations and breaches within the framework of corporate transactions.

II  GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The principal laws regulating M&A in Russia are:

- the Civil Code;
- the Federal Law ‘On Joint Stock Companies’;
- the Federal Law ‘On Limited Liability Companies’;
- the Federal Law ‘On State Registration of Legal Entities and Private Entrepreneurs’;
- the Federal Law ‘On Securities Market’; and
- the Federal Law ‘On Competition Protection’.

Foreign investments and their governmental approval are governed by the Federal Law ‘On Foreign Investments’ and the Federal Law ‘On Foreign Investments into Industries Important for State Defence and Security’.


There is plenty of subordinate legislation and explanations by the courts of ways to interpret the law. Among them are the following:

- the Federal Antimonopoly Service’s ‘Explanations of the Order and Methodology of the Analysis of the Joint Venture Agreements’ dated 8 August 2013;
- a Ministry of Labour and Social Protection letter dated 19 October 2017 concerning the validity of non-compete clauses within the framework of labour relations;
c the Supreme Court’s Plenary Session’s Resolutions:3
• on basic rules of civil law dated 23 June 2015;
• on contractual liability dated 24 March 2016;
• on contractual performance dated 22 November 2016;
• on challenging major and interested party transactions dated 26 June 2018;
• on entering into contracts and their interpretation dated 25 December 2018; and

d the High Commercial Court (which was subsequently merged into the Supreme Court) Plenary Session Resolution on directors’ liability dated 30 July 2013.

Certain aspects of holding general shareholders’ meetings, information disclosure, notarial certification of transactions (where necessary), performance of share transfers by registrars and depositaries are governed by the below sub-laws:

a Central Bank of Russia (Bank of Russia) recommendations on preparing and holding general shareholders’ meetings dated 19 December 2017;

b Bank of Russia mandatory rules on general shareholders’ meetings dated 16 November 2018;

c Bank of Russia information disclosure standards for issuers dated 30 December 2014;

d Bank of Russia rules on maintaining a securities register dated 11 September 2014;

e Depository Business Committee’s basic standards dated 16 November 2017; and

f Ministry of Justice rules on notarial records management dated 16 April 2014.

In addition, and especially for listed companies4 (companies publicly traded on the stock exchange5), the Bank of Russia Code of Corporate Governance dated 10 April 2014 is non-compulsory but highly persuasive.

Generally, Russian company law is a quite a highly regulated sphere, especially when it comes to listed companies. Therefore the above laws as well as other applicable rules (e.g., company charters, by-laws) should be carefully scrutinised each time it comes to performing a share transfer, calling and holding shareholders’ and board meetings, and disclosing information. Less attractive is the fact that Russian contract law is still not so dynamic and liberal as, for example, English law, although it has made great progress in the past four to five years.6 That may make deal structuring and principal agreement drafting cumbersome in some cases. Other archaic limitations may also preclude implementing some traditional M&A mechanisms. For example, it was discovered recently that it is practically impossible

3 Resolutions’ names are not quoted due to their massiveness – rather, a description of their content is provided.
4 It must also be noted that recent legal amendments allow companies targeted by international economic sanctions to ignore certain information disclosure rules. Those amendments’ effect on the securities market and investment climate is viewed by certain experts as controversial.
5 Formally, a company’s shares do not necessarily need to be listed at the stock exchange in order for the company to be public. It may have such status provided it complies with legal rules on information disclosure, and even absent such listing. However, about the date hereof the Bank of Russia suggested amending the legislation so that only listed companies could have public status. Hereinafter, therefore, references to listed and non-listed companies shall be read as references to public and non-public ones.
6 Many reviews of the extensive reform of Russian contract law in 2015 are available in the public domain. Briefly, the principal English law instruments were implemented then, such as representations and warranties, indemnities and option agreements. Since four years have passed since that reform, we do not view those amendments as recent developments.
Russia

to give effect to a buy-back call option in relation to the shares in a limited liability company (LLC)\(^7\) when the seller signs a share purchase agreement simultaneously or after signing the said option in order to be able to return the sold share on certain occasions. That limitation is due to notaries’ inability, in accordance with the applicable notarial legal rules, to certify an option whereunder the purchaser agrees to sell a share back where that share does not belong to him or her at the date of such option; the notary may only certify a disposal of assets belonging to the party on the day of relevant deal.

In addition, as previously mentioned, regulatory clearings should always be subject to thorough scrutiny, and each deal must, among other aspects, be assessed with a view as to whether it is necessary to obtain a respective regulatory approval or consent. Absent such approval a deal is either void, or voidable, or the new shareholder may not vote on his or her shares. Sometimes regulatory consents act as deal-breakers: thus, as was widely covered in the media, the contemplated acquisition by global oil industry services giant Schlumberger of a 51 per cent share in its Russian competitor Eurasia Drilling Company (EDC) for approximately US$1.9 billion\(^8\) was cancelled earlier this year after about four years of the buyer’s unsuccessful negotiations with the Russian authorities on its approval.\(^9\) Sometimes such regulatory issues may arise even where less expected. As such, it may be surprising for less experienced lawyers that acquisitions of even a 0.1 per cent share in an insurance company requires cooperation with the Bank of Russia in the form of a written notification.

English law\(^10\) is frequently utilised by parties to Russia-related deals. However, foreign law may hardly be relied on at least in the following two cases:

\(a\) in the case of making a shareholders’ agreement in relation to Russian company due to the generally accepted way of interpreting the relevant article of the relevant civil code; and

\(b\) in the case of a sale purchase or other deal with an LLC’s shares, albeit no direct prohibition is set forth, no notary may in fact certify such deal, with the deal being void absent such certification.

Notwithstanding the above aspects, Russian law generally allows the structuring of M&A, JV, PE and VC deals in accordance with the best UK and US practices, even though many specific issues must be taken into account.

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\(^7\) Russian law provides for many types of commercial legal entities, however vehicles of vast majority of deals are listed and non-listed joint-stock companies (JSCs) and LLCs, which are similar in many aspects to non-listed JSCs; however, their shares may not be listed (and are not securities as opposed to stocks), and most disposals with such shares (sale-purchase, pledging, etc.) shall be notarised.

\(^8\) The deal’s parameters, including the size of share to be acquired and the purchase price, were subject to several reviews in the course of negotiations.

\(^9\) Among other conditions discussed with the regulators then by Schlumberger was the appointment of Russian directors to EDC, the transfer of certain technologies into Russia, and the mitigation of international sanctions-related risks related to its possible forced sale of its share in EDC due to sanction limitations.

\(^10\) And less often, other foreign law (e.g., Cypriot, Swiss or German law).
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Among the most interesting developments affecting corporate deals seen in the period running from 2017 to 2019 are as follows:

a new rules on major and interested party transactions. The mandatory approval of interested party transactions by a company’s board of directors or meeting of shareholders has been superseded by an approval at the request of a director or shareholder. Major transactions now do not need approval if a company regularly enters into such transactions. Of particular note in the framework of the interpretation of that rule is the currently pending OVK Corporation case. Among other things, it is contested by the parties that after certain transactions were approved as being major, the company’s CEO filed a claim asking to hold them as being non-major to avoid the necessity for the company to buy back its shares from the shareholders who voted against the transaction;

b new rules on foreign investment approval. The head of the government was vested with the authority to put any acquisition by a foreign party of a share in a Russian company under the necessity of a review by the Governmental Commission on Foreign Investments. Certain concepts relating to ways to treat offshore (non-disclosing) companies by the Commission were also clarified (see Section IX);

c a new class of preferred shares was introduced: preferred shares with the attached priority right of receiving dividends. That class of shares was unofficially called ‘super-preferred shares’. Relevant anti-dilution provisions were also adopted;

d new rules establishing non-listed JSCs: no state registration of share issuances and no preparation of a prospectus (offering memorandum) is needed now in certain cases; and

e the above-mentioned amendments allow certain listed companies targeted by international sanctions to omit information disclosure partly or in full subject to the provision of that information to the Bank of Russia.

As mentioned in footnote 13, some of those novelties were adopted as part of a significant reform of the securities law: approximately half of the new rules are to take effect from 2020, while the other part is already in force. Although a detailed overview of that topic is rather the business of capital markets lawyers, many of the new rules have direct relevance to M&A deals. Some of them are described above.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

As previously discussed, foreign involvement in M&A transactions in Russia is subject to regulatory review in a number of cases, including, without limitation, cases when the target company (the company whose shares are being acquired) is of strategic importance for state security and defence, or when it is a bank or insurance company.

11 After an initial decision and several applications for review, the case is to be heard before the Supreme Court later this year.
12 Or non-listed companies whose debt securities are listed.
13 The latter three amendments are part of a recent significant set of amendments to the Federal Law on the Securities Market.
Undoubtedly, US and EU sanctions implemented in 2014 and gradually developed to date, including the famous US Countering America's Adversaries Through Sanctions Act, are a key factor in the reduction of the amount of inbound Russian foreign investment. Among other things, in June 2019 Morgan Stanley announced the substantial reduction of its Russian business. A number of international law firms have also left Russia in recent years. All the other famous global investment houses and international law firms have substantially reduced their Russian presence.

A change of orientation from the West to the East as declared by Russian authorities in 2014 and 2015 is not obvious, despite certain case-by-case episodes of inbound deals by Chinese and other eastern companies (see Section I). Among others, however, the Russia-Chinese Investment Fund was formed by Russian (RDIF) and Chinese (CIC) sovereign funds.

These factors also negatively affect Russian outbound M&A activity, including those activities not directly targeted by the sanctions. Thus, Alisher Usmanov has sold his share in Arsenal Football Club, while Roman Abramovich is exploring options to sell Chelsea Football Club. In early 2019 it was announced that US Committee on Foreign Investment had ordered one of Mikhail Fridman's companies to dispose of its share in a US cybersecurity company.

There are also positive episodes. Thus, while this chapter was being prepared, Mikhail Fridman (with his allies German Khan and Alexey Kuzmichev) has obtained a 33 per cent share in Wintershall DEA, the largest oil and gas producer in Europe formed after the merger of BASF's Wintershall and LetterOne's DEA. LetterOne is Fridman's, Khan's and Kuzmichev's investment house with a notable presence throughout the world, including by holding shares in the UK healthy food retailer Holland & Barrett. It must be noted that several years ago, LetterOne also faced demands by UK authorities to sell some of its assets in the UK.

Although this deal rather sits in the capital markets sphere, and not the M&A sphere, it is worth highlighting the significantly successful IPO on NASDAQ of HeadHunter, a Russian web resource for employers and candidates listing job and hiring opportunities.

Returning to inbound M&A in Russia, another negative factor is the passing of the period of primary accumulation of wealth and capital that took place in Russia in the 1990s up to 2000. The economy has now entered a more mature phase: in addition to the effect of the imposed sanctions, no strong growth was seen in the first two decades of the new era of the market economy in Russia. Accordingly, there are no further super-incomes, which used to be the main factor attracting many foreign investors. Along with certain legal and regulatory risks (again, other than sanctions), Russia has become a less attractive investment destination than it was before 2008 and before 2014. Thus, among other things, EBRD froze its Russian investment programme in 2014 and later disposed of its share in Promsvyazbank and some other Russian banks. A similar entity, IFC, has done the same; among other things, it has sold its share in Asian-Pacific Bank. Both of the mentioned Russian banks have subsequently been bailed out by the Bank of Russia due to insufficient assets and inadequate liquidity.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

See Section I.
VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

M&A deals are made by purchasers with their own funds or by way of raising debt finance. Loans may be provided by single banks or by syndicates. The Federal Law on Syndicated Loans, which entered into force in 2018, made it possible to structure syndicates and lend respective loans under Russian law. However, to the best of our knowledge there are few legal teams in Russia who have managed to practically apply the Law in the less-than-one-and-a-half years since its adoption. Therefore, more details of its mechanics are yet to be seen.

As regards private equity aspects, see Section I.

VII EMPLOYMENT LAW

The principal issues of employment and labour law in the context of M&A deals are:

a. due diligence of employment-related aspects such as contracts with key employees, internal policies, compliance with other mandatory rules (relating, among other things, to trade unions, collective agreements). In VC transactions in particular (although they may also be applicable in other types of corporate deals), invention clauses in labour contracts, whereunder the rights to key intellectual assets created by employees shall belong to the target company, are common;

b. enforcement of non-competition and non-solicitation provisions, whereunder, respectively, key employees waive their right to apply to be hired by the target company’s competitors, while the seller waives its right to hire such key employees of the target company. Russian law views such arrangements as ineffective, as they limit the freedom of labour and employment guaranteed and secured by the Constitution; and

c. labour law aspects of the termination of the employment of CEOs and other senior executives. Among other things, a Supreme Court Plenary Session Resolution dated 2 June 2015 must be considered.

VIII TAX LAW

In the past few years, the Russian economy has been experiencing de-offshorisation changes, which, of course also has certain impacts on cross-border M&A transactions. Foreign investors willing to enter the Russian market should understand several aspects that are monitored closely by the Russian tax authorities.

When considering a sale or purchase of a Russian-based business, foreign investors should analyse whether the assets of a Russian entity consist of Russian real estate. The rule of Subparagraph 5, Paragraph 1, Article 309 of the Tax Code states that if more than 50 per cent of the assets of a Russian entity (or a foreign subsidiary) are real estate, then a 20 per cent withholding tax should be paid in Russia. The rule is not modern, but compliance with it is currently strictly supervised by the Russian Tax Authorities, and non-compliance will be regarded as tax avoidance or as an unjustified tax benefit.

Foreign investors should also consider their exit strategies beforehand. Starting from the end of 2018, Paragraph 1, Article 250 of the Tax Code was amended in a way that income in the form of liquidation proceeds is regarded as dividends, which means that the rules for the taxation of dividends (including withholding taxes in accordance with double taxation treaties (DTTs)) should apply when a foreign parent company receives liquidation proceeds from its Russian subsidiary. On the other hand, the same bill introduced new Subparagraph 11.1. Paragraph 1, Article 251 and Paragraph 2.3, Article 309 of the Code relate to the
taxation of contributions to a company’s assets in monetary form and its gratuitous return. Now, the income of a parent company received in monetary form as a gratuitous return of a contribution to the assets of a subsidiary is not subject to corporate income tax or withholding tax.

Another very important issue is the development of the concept of the beneficial owner of passive income (dividends, interest, royalties) paid by a Russian company to a foreign company. The rule on beneficial ownership was introduced into Article 7 of the Tax Code and came into force in 2015. Since then, there has been plenty of negative court practice stating that Russian companies cannot use benefits and lower tax rates under DTTs when making payments to foreign parent companies or counterparties unless the foreign recipient of the passive income is a beneficial owner of such income.14

In addition, the look-through approach (Paragraph 4, Article 7) was modified in late 2018. Now, when distributing profits from Russia to a foreign jurisdiction, it is possible not to prove the existence of the beneficial ownership of such income of the first recipient, but to claim a look-through approach and use the advantages of the DTT between Russia and the country of residence of the final (real) recipient of the income, notwithstanding who the intermediary recipients are.

When working on Russian market, Russian controlled foreign company (CFC) rules applicable since 2015 should also be considered. Namely, if a Russian entity belonging to a foreign investor holds shares in the capital of another foreign entity, such Russian entity should submit to the tax authorities the following documents: a notification on participation in a foreign entity if the Russian entity holds more than 10 per cent of the share capital of a foreign company; or a notification on the CFC if the Russian entity holds more than 25 per cent of the share capital of a foreign company (or, if the Russian entity holds more than 10 per cent, while all Russian residents in total hold more than 50 per cent of the share capital of the foreign company in question).

As a general rule, if the Russian company is regarded as a controlling person, it should include the undistributed profits of a foreign subsidiary in its taxable base under corporate income tax.

Finally, in 2018 international companies were introduced to the Russian legal system. To benefit from this new regime, prescribed by Federal Law ‘On international companies’, foreign companies should be redomiciled to the special administrative regions of the Kaliningrad region and Primorskiy territory of Russia.15 In brief, the status of international holding companies provides for the tax-free receipt of dividends or income from a sale of shares from Russian-based or foreign companies if an international holding company holds 15 per cent or more in a subsidiary.

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IX COMPETITION LAW

At the end of 2018, the government adopted the rules for providing information to the regulator in the case of making foreign investments in Russian economic entities. An important point thereof is the fact that foreign investors shall now provide not only information about their controlling persons, but also information about their UBOs. So, control over the foreign investors is increased. It must also be noted that foreign inbound M&A deals in Russia are becoming target of particular attention by the regulators.

In particular, one draft law provides for civil liability when a foreign investor does not clear a transaction regarding a strategic entity with the regulator. In this case, if the consequences of the invalidity of the transaction cannot be applied, the regulator will be able to go to court with a demand to deprive the investor of his or her right to vote and with a claim of forced sale of the investor’s shares in such strategic entity at an auction.

As far as financial organisations are concerned, the Federal Antimonopoly Service of Russia (FAS) recently clarified that merger control in relation to foreign banks is carried out in accordance with the rules of the product market. Thus, the rules relating to financial organisations do not apply, because foreign banks are not financial organisations in the sense of the Federal Law ‘On Competition Protection’.

In addition, the enactment of the Fifth Antimonopoly Package, a set of substantial amendments to the Federal Law ‘On Competition Protection’, is expected soon. Most likely, the following concepts in the field of M&A transactions will appear in the legislation and will have to be assessed by FAS within the framework of merger control:

a the value of a transaction. If the value of a transaction exceeds 7 billion roubles, it is subject to approval regardless of the amount of assets in the perimeter of the deal;
b face-to-face consideration: the parties to the transaction will be able to hold negotiations with FAS in person in the process of merger control. The procedure is now more bureaucratic, and is conducted rather through the exchange of the applicant’s filing and the regulator’s resolutions;
c the regulator’s memorandum or opinion on the substantial aspect of a deal: before making a decision, FAS will issue an opinion on a transaction. This allows the parties to provide additional information or to suggest new transactional terms;
d commitments, undertakings and covenants: the parties may at their initiative suggest to the regulator certain terms and conditions of the negotiated deal;
e trustees: parties and regulators will have an option to appoint an independent person (as a rule, an expert in a particular field) responsible for monitoring the terms of a transaction and its performance, as well as parties’ compliance with the relevant FAS ruling on the deal. Detailed instructions on, inter alia, requirements as to the candidature of such trustee, and the procedure of his or her appointment, are to be adopted by FAS; and
f new conditions: the time limit for the approval of cross-border transactions may be extended for several years.

One of the largest deals approved by FAS in the past year was the merger between Bayer and Monsanto, global chemical industry leaders. The deal was subject to review by the Russian regulator because the merger affects, among others, the Russian market. The relevant FAS ruling included an obligation on Bayer to transfer some of its intellectual property to its Russian competitors (on the base of licences), as well as to ensure their non-discriminatory
access to information in the field of precision agriculture. Control over compliance with the ruling was entrusted to the Center for Technological Transfer at the Higher School of Economics, a specialised and independent organisation.

X  OUTLOOK

It is expected that the hottest sphere in the next few years will be VC transactions. It also appears that the mid-market segment will be more active than the high-end division. Sanction risks will be one of the points requiring the most careful attention.
I OVERVIEW OF M&A ACTIVITY

In 2018, Singapore continued apace with a robust volume of 688 M&A deals valued at about US$99 billion, buoyed by outbound sovereign wealth fund deals.\(^2\) Outbound deals accounted for a greater share of deal value at approximately 82 per cent, up from 72 per cent in 2017.\(^3\) Domestic and inbound deals accounted for 10 and 8 per cent of total deal value, respectively.\(^4\) In total, 458 cross-border deals were consummated at an approximate value of US$89 billion.\(^5\) Private equity (PE) and venture capital (VC) investments numbered a collective 154 deals registering approximately US$6.6 billion.\(^6\) Overall, the Singapore economy grew a healthy 3.2 per cent in 2018, falling within the higher of the initial forecasts of between 1.5 and 3.5 per cent.\(^7\)

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Statute and common law

Under Singapore’s common law system, sources of law include legislation, subsidiary legislation and judge-made case law. Legislation and subsidiary legislation are passed by Parliament and interpreted by the courts. The principles of contract law govern the validity and interpretation of agreements.

Key Singapore legislation relevant to M&A transactions include the Companies Act and the Securities and Futures Act (SFA), and their respective subsidiary legislation. The Companies Act is the principal legislation governing Singapore-incorporated companies, be they private or public. The Companies Act contains, among other things, provisions that regulate the criteria and processes by which share transfers, schemes of arrangement, amalgamations and compulsory acquisitions are effected.\(^8\) The SFA regulates, among other things, offers of securities, notifications when a substantial interest is acquired and market conduct rules, including those relating to insider trading and market manipulation.\(^9\)

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1 Sandra Seah, Marcus Chow and Seow Hui Goh are partners at Bird & Bird ATMD LLP.
3 Ibid.
4 Ibid.
5 Ibid.
6 Ibid.
7 Ministry of Trade and Industry.
8 Section 126, Section 210, Section 215A and Section 215 of the Companies Act, respectively.
9 Section 240, Section 135, Section 218 and Section 198 of the Securities and Futures Act, respectively.
Aside from the above statutes, which are of general applicability, companies in certain sectors are additionally subject to sector-specific legislation. For instance, insurance companies, banks and publishing companies are regulated by the Insurance Act, the Banking Act and the Newspaper and Printing Presses Act, respectively.

### ii The Singapore Code on Takeovers and Mergers

The Singapore Code on Takeovers and Mergers (Code) is issued by the Monetary Authority of Singapore, pursuant to the SFA. The Code governs the conduct, timing, approach and documentation in relation to takeovers and mergers of corporations with a primary listing of their equity securities, business trusts with a primary listing of their units in Singapore and real estate investment trusts. Unlisted public companies and unlisted registered business trusts with more than 50 shareholders or unitholders, as the case may be, and net tangible assets of S$5 million or more, must also observe the letter and spirit of the Code, wherever possible and appropriate.

The Code is administered and enforced by the Securities Industry Council (SIC) which, pursuant to the SFA, has the power to investigate any dealing in securities that is connected with a takeover or merger transaction. While the Code itself does not have the force of law, a breach could result in sanctions imposed by the SIC. Such sanctions include a private reprimand, public censure or, in a flagrant case, further action as the SIC deems fit, including actions designed to deprive the offender temporarily or permanently of its ability to enjoy the facilities of the securities market.

### iii The SGX-ST Listing Rules

SGX-listed entities are further subject to compliance with the SGX-ST Listing Rules (Listing Rules) contained in the SGX-ST Listing Manual (Listing Manual). The Listing Manual comprises the Mainboard Rules, which apply to companies listed on the Mainboard of the SGX-ST; and the Catalist Rules, which apply to companies listed on the Catalist Board of the SGX-ST. In the context of M&A transactions, the Listing Rules applicable to Mainboard and Catalist listed companies are broadly similar. Listed companies are required to disclose or obtain shareholders’ approval (or both) for transactions such as acquisitions and realisations that meet certain thresholds relating to, among other things, net asset value, net profits, aggregate consideration and number of consideration shares issued. Where as a consequence of an acquisition the public shareholdings of the listed company fall below 10 per cent, the company may be subject to delisting.

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10 The Singapore Code on Takeovers and Mergers: Introductory Paragraph.
11 Ibid.
12 Ibid.
13 Ibid.
14 Ibid.
15 Ibid.
16 SGX-ST Mainboard Listing Rules: Rule 1006.
17 SGX-ST Mainboard Listing Rules: Rule 724.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Securities and Futures Act
Wide-ranging amendments to the SFA took effect from October 2018, including a stronger enforcement regime against market misconduct. Among the amendments relating to misconduct was a clarification that disclosures that are false or misleading in a material particular, and likely to have an effect on the market price of securities, securities-based derivatives contracts or collective investment scheme units, are prohibited regardless of whether the effect on price is significant or otherwise.\(^{18}\)

To buttress prosecution of insider trading crimes, a further amendment was made to the SFA to provide for the term ‘persons who commonly invest’ to mean ‘a Section of the public that is accustomed, or would be likely, to deal in any securities of that kind’. This wider definition permits a more flexible test in assessing the effect of price sensitivity on common investors.

In view of these amendments, parties working on the acquisition of a listed company should be careful to maintain confidentiality and to ensure that no false or misleading statements are released or made.

ii The Companies Act
In August 2018, amendments to the Companies Act came into effect seeking to reduce the regulatory burden on companies and improve the ease of doing business in Singapore.

Pursuant to the amendments, the timelines for holding annual general meetings (AGMs) and filing annual returns are now aligned with a company’s financial year-end. Prior to the amendments coming into force, a company had to hold its AGM within 15 months of its last AGM, and its annual return would have to be filed within 30 days after such AGM. From 31 August 2018, the timeline for holding an AGM is within six months from the financial year-end of a private company and within four months from the financial year-end of a listed company.\(^{19}\) Annual returns must be filed within seven months and five months of the financial year-end for private and listed companies, respectively.\(^{20}\)

With effect from 31 August 2018, private companies are exempted from holding AGMs if they send their financial statements to members within five months of the financial year-end.\(^{21}\) However, private companies must still hold an AGM if any shareholder so requests not later than 14 days before the expiry of six months after the financial year-end.\(^{22}\) A further safeguard requires private companies to hold a general meeting to lay out their financial statements if any shareholder or auditor so requests not later than 14 days after the financial statements are sent out.\(^{23}\) Private companies retain the option to dispense with the holding of AGMs, and the threshold of shareholder approval required to approve such dispensation remains unchanged.\(^{24}\)

\(^{18}\) Section 199 of the Securities and Futures Act.
\(^{19}\) Section 175 of the Companies Act.
\(^{20}\) Section 197 of the Companies Act.
\(^{21}\) Section 175A(1) of the Companies Act.
\(^{22}\) Section 175A(4) of the Companies Act.
\(^{23}\) Section 203(4A) of the Companies Act.
\(^{24}\) Section 175(1) of the Companies Act.
Such changes to Singapore’s corporate regulatory regime are expected to reduce compliance costs for private companies exempted from holding AGMs, and to reduce the administrative burden on both private and listed companies with simplified timelines for holding AGMs. These amendments are expected to enhance the attractiveness of the Singapore corporate entity and may encourage relevant corporate actions (including acquisitions).

iii The Listing Manual

In June 2018, SGX-ST approved changes to its Listing Rules to allow for the primary listing of dual class share companies on the Mainboard. Dual class share companies have two classes of voting shares: shares in one class carry one vote per share, while shares in another class carry multiple votes per share. The multiple voting shares now permitted to be listed on the Mainboard are capped at 10 votes per share.25 Corporate governance safeguards are in place to restrict the additional voting rights attached to multiple voting shares from being exercised on key matters. Such matters include the appointment and removal of independent directors and auditors, a variation of rights attached to any class of shares, a reverse takeover and a winding up or delisting.26

The opening of Singapore’s bourse to dual class share companies means that new economy tech-based companies, which often have share classes with different voting rights, will gain access to fund raising via initial public offerings (IPOs) in Singapore. The advent of dual class listings may see IPOs becoming a more popular exit strategy for venture capitalists, over M&A exits, in Singapore.

The revised Code provides that where an offer is made for a dual class share company, a comparable offer must be made for each class of shares, save for when an offer is only made for non-voting shares.27 This approach provides a safeguard for ordinary voting shareholders by ensuring that any premium paid to multiple voting shareholders is also paid to ordinary voting shareholders.

iv The Takeover Code

Exemption of connected fund managers and principal traders

Under the Code, certain categories of persons are presumed to be acting in concert. Such categories include parent companies, subsidiaries, fellow subsidiaries, associated companies, and fund managers and principal traders connected to a financial or other professional adviser on a deal.28 Acquisitions exceeding certain thresholds will trigger an obligation on the part of acquirers to make a mandatory general offer, for all the target’s shares, under the Code.29 For the purpose of calculating whether such thresholds are met, the shareholdings of the acquirer’s concert parties are taken into account.30

Since 1 May 2018, connected fund managers and principal traders can apply for exemptions from the restrictions, prohibitions and obligations arising out of their status as concert parties, on an annual renewable basis or per transaction basis, under a new exempt

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25 SGX-ST Mainboard Listing Rules: Rule 210(10).
26 SGX-ST Mainboard Listing Rules: Rule 730B.
27 The Singapore Code on Takeovers and Mergers: Rule 18.
28 The Singapore Code on Takeovers and Mergers: Definitions.
29 The Singapore Code on Takeovers and Mergers: Rule 14.
30 Ibid.
status regime. Under the Code, fund managers and principal traders from the same financial group as the financial or other professional adviser of a takeover offer are presumed to be concert parties of such adviser and its client. As a result, the dealings of connected fund managers and principal traders in the securities of the offeree company are restricted and subject to certain prohibitions and obligations under the Code.

A fund manager or principal trader exempted under the exempt status regime will not be regarded as acting in concert with the relevant offeror or offeree and will not be subject to the connected person restrictions under the Code. The exempt status applies only where the sole reason for the presumed connection with the offeror or offeree is that the fund manager or principal trader is in the same group as the financial or other professional adviser that is advising the offeror or offeree company.

Revisions to the Code to clarify its application to dual class share companies

On 24 January 2019, on the advice of the SIC and incorporating feedback from a public consultation exercise, the Monetary Authority of Singapore revised the Code to clarify its application to SGX-listed dual class share companies. Unlike single class share companies, the voting rights in dual class share companies are not proportionate to shareholding.

The Code amendments provide relief for shareholders who trigger a mandatory general offer. Under the revised Code, where the obligation to make a mandatory offer is triggered due to a conversion of multiple voting shares to ordinary voting shares or a reduction in the number of voting rights per multiple voting share, the requirement to make a mandatory offer under the Code will be waived if certain conditions are met. Such conditions include that the shareholder is independent of the conversion or reduction event, and has not acquired any additional voting rights in the company from the date he or she becomes aware that the conversion or reduction is imminent. In the event that such shareholder is not independent of the conversion or reduction event, the mandatory offer requirement will still be waived if he or she obtains the approval of independent shareholders to waive their right to a mandatory offer within a specified time, or reduces his or her voting rights to below the mandatory offer thresholds.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Transactions with a foreign element accounted for the lion’s share of Singapore’s M&A investments in 2018, at 90 per cent of total deal value. The profile of cross-border deals continued to be dominated by outbound investments made by sovereign wealth funds GIC Pte Ltd (GIC) and Temasek Holdings Pte Ltd (Temasek). In particular, GIC’s outbound investments constituted most of the year’s highest-valued deals with its consortium investment in Thomson Reuters Corp (F&R Business), valued at US$17 billion. In total, outbound
deals accounted for 69 per cent of all cross-border M&A transactions in Singapore. Despite the financial crisis, banking, financial services and insurance (BFSI) was the top sector for outbound investments.  

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES  
The BFSI sector had a strong showing in 2018, propelled by two large outbound deals: the US$17 billion investment in Thomson Reuters Corp (F&R Business) by GIC (together with its consortium partners), and the US$14 billion investment in Ant Financial Services Co Ltd by a GIC-led consortium that included Temasek. BFSI overtook real estate as the top sector for 2018, representing 32.9 per cent of total deal value. The real estate sector fell to second place ahead of the materials sector, each capturing 20.6 and 13.4 per cent of total deal value, respectively. Together, the top three sectors accounted for approximately 70 per cent of total M&A deal values in Singapore for 2018.  

Other notable M&A transactions for 2018 included GIC’s US$12.5 billion consortium acquisition of Akzo Nobel NV’s Specialty Chemicals business, and its US$5.4 billion consortium investment in hotel real estate company, AccorInvest. Notable PE and VC transactions included the US$2.45 billion investment in Grab Holdings by Toyota Motor Corp and other consortium investors. The technology sector continued to be a significant driver of M&A activity. Aside from the Grab/Toyota deal, other transactions in the technology start-up space included the US$272 million inbound investment in Bigo Technology Pte Ltd by Chinese video-streaming app maker YY Inc and other consortium investors.  

Singapore continued to be a key contributor to M&A and PE and VC deal activity in the region for 2018, with more than 10 deals valued at more than US$1 billion apiece.  

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS  
In 2018, M&A transactions continued to be financed by the usual sources of internal financing, bank and financial institution loans and PE. In particular, local and major international banks and financial institutions were the most common source of financing for M&A deals in Singapore. At a combined 154 investments accounting for US$6.6 billion in 2018, PE and VC funding in Singapore remained fairly active. The top-valued M&A deals in 2018 involved investments by sovereign wealth funds GIC and Temasek, together with their various consortium partners.  

For offers governed by the Code, additional requirements may apply. Where the offer is for cash or cash alternatives, the offer document as well as the announcement of a firm
intention to make an offer should include confirmation from a financial adviser that the offeror has enough cash resources to satisfy full acceptance of the offer.49 Where external financing is to be availed of, the terms of such financing must satisfy the requirements of the financial adviser.

VII EMPLOYMENT LAW

With effect from 1 April 2019, all employees (regardless of rank and salary) fall under the protection of the Employment Act (1 April Amendment), Singapore’s main labour legislation.50 This means that in the case of a business sale, all employees employed in the seller’s business will be automatically transferred to the buyer by operation of law.51 Under the automatic transfer provisions, all transferring employees are entitled to preserve their existing terms and conditions of employment and have the length of their service counted towards their period of employment with the buyer.52 Prior to the transfer, the seller is required to inform and consult with affected employees on the transfer process.53 If the affected employees are members of a trade union, the union must also be involved in the information and consultation process.54 Any dispute or disagreement arising from a transfer of employment may have the effect of blocking or delaying the business sale. The Ministry of Manpower will be the arbiter of these disputes and will in many circumstances act as the conciliator.

Prior to the 1 April amendment, the automatic transfer provisions only applied to a certain employee population (the rank and file, and managers and executives earning less than S$4,500 per month). The buyer had freedom to agree on new terms of employment for other employees, and had more selection control over the number and type of employees it wanted to hire from the seller. Under the current laws, buyers have less leeway in terms of employee transfers.

VIII TAX LAW

In general, the legal obligation to pay stamp duty in an acquisition falls on the buyer in a transaction.55 However, as a practical matter, parties are free to negotiate, as a contractual term, who should bear the costs of paying stamp duty. Stamp duty relief may be available for qualifying share acquisitions in connection with M&A transactions.56 Stamp duty relief may also be available for the transfer of a company’s business undertaking or shares in connection with its reconstruction or amalgamation.57

49 Rule 3.5, Takeover Code.
50 Section 2 of the Employment Act.
51 Section 18A(1) of the Employment Act.
52 Section 18A(4) of the Employment Act.
53 Section 18A(5) of the Employment Act.
54 Ibid.
55 Third Schedule, Stamp Duties Act.
56 M&A Scheme, Inland Revenue Authority of Singapore.
57 Stamp Duties (Relief from Stamp Duty upon Reconstruction or Amalgamation of Companies) Rules.

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At present, transfers of immovable properties and shares are usually effected by way of physical documentation such as sale and purchase agreements and share transfer instruments. If such instruments of transfer were executed in Singapore, or if they were received in Singapore and relate to property situated in Singapore, they are chargeable with stamp duty under the Stamp Duties Act. The proliferation of digital technology offers increasing opportunities for transactions to be effected electronically instead of with physical documentation.

In October 2018, the Ministry of Finance brought into effect amendments to the Stamp Duties Act that aim to ensure that Singapore’s stamp duty regime keeps pace with digitalisation. The key amendment provides for stamp duty to be levied on electronic records that effect a transfer of interest in immovable properties and shares.

i The M&A scheme

The M&A scheme (scheme) was introduced by the government in 2010 to encourage companies to undertake M&A as a growth and internationalisation strategy. To qualify for the scheme, certain transaction-related thresholds must be met. The scheme is currently valid up until 31 March 2020 and comprises the following benefits:

a a tax allowance of 25 per cent of the acquisition value, subject to a maximum deduction of S$10 million for each year of assessment;

b stamp duty relief for qualifying share acquisitions, subject to a relief cap of S$80,000 per financial year; and

c double tax deduction on transaction costs incurred in respect of qualifying share acquisitions, subject to a cap of S$100,000 on acquisition costs.

IX COMPETITION LAW

i Consumer protection and competition

The Competition Commission of Singapore is the agency tasked with administering and enforcing the Competition Act, and was renamed the Competition and Consumer Commission of Singapore (CCCS) after taking on an additional function of administering the Consumer Protection (Fair Trading) Act (CPFTA) with effect from April 2018.

After this change, the mediation of complaints against errant retailers through the Consumers Association of Singapore will continue to be the first port of call to assist consumers. Errant retailers who persist in unfair trade practices will then be referred to the CCCS for investigation. The CCCS has already obtained a court order in mutual agreement with one such errant undertaking, the SG Vehicles group of companies, and their director, which takes effect from 18 April 2019, requiring SG Vehicles to cease various unfair trade practices including ceasing misleading or deceptive practices and ceasing the making of any false claims as to any guaranteed delivery date of any vehicles, and also to install a prominent sign outside their shops stating the full text of the court order.

To enhance the synergies between competition and consumer protection, the CCCS’ powers under the CPFTA work hand in glove with its powers under the Competition Act. Specifically, the CCCS’ powers under the CPFTA can build on the existing market studies

58 Section 4, Stamp Duties Act.
59 Section 60A, Stamp Duties Act.
that the CCCS had already been conducting to test the effectiveness of markets in specific sectors in Singapore. Market studies are already being undertaken to study the impact of developments in data protection and the online travel booking sector.

ii Amendments to Competition Act

Following a public consultation on the proposed changes to the Competition Act, changes were made to the Act with effect from May 2018, including:

a codification of the CCCS’ process for providing confidential advice on anticipated mergers: the CCCS already has a process under its Guidelines on Merger Procedures 2012 for businesses to seek confidential and non-binding advice on anticipated mergers. This is now given statutory effect under the new Section 55A of the Competition Act. The advice will be given strictly on the veracity of the information provided by the merging entities: the CCCS will not request information from third parties or conduct any public consultation to make a comprehensive assessment. As such, the advice issued under Section 55A of the Competition Act will not be binding on the CCCS;

b businesses under investigation may offer legally binding commitments: Sections 60A and 60B of the Competition Act now allow the CCCS to accept binding and enforceable commitments for cases involving anticompetitive agreements and the abuse of a dominant position. Investigations will cease if the CCCS accepts the offered commitments. Previously, such commitments were only available in relation to mergers or acquisitions that substantially lessen market competition; and

c the CCCS is empowered to conduct general interviews during inspections and searches: CCCS officers are now empowered to ask general questions in relation to the same investigation without first serving a written notice when conducting inspections or searches of premises. Previously, occupants of the premises were only required to provide an explanation of the documents produced or seized on the premises or information uncovered during inspections. It is critical that corporations now have a dawn raid response procedure in place to ensure that they fulfil their legal obligations while safeguarding their own legal rights.

iii M&A

In the past 12 months, there have been 11 notifications and one investigation on the public register, with two withdrawn or abandoned and one undergoing Phase II review.

Mergers that result in, or may be expected to result in, a substantial lessening of competition in Singapore are prohibited under Section 54 of the Competition Act (Section 54 prohibition). Merger notification is voluntary under the Competition Act, but parties to a M&A transaction should conduct self-assessments against the guidelines published by the CCCS to determine if there may be a substantial lessening of competition and a merger notification is necessary.

The CCCS has set out the following indicative thresholds that when crossed will likely require further review to determine if there is a substantial lessening of competition: the post-merger market share of the top three undertakings is at least 70 per cent, and the market share of the merged undertaking is at least 20 per cent; or the merged undertaking has a market share of at least 40 per cent. The assessment of whether there is a substantial lessening of competition is qualitative and factual and may be undertaken even if the indicative thresholds are not met. The CCCS will consider various factors in this assessment, including barriers to entry, market transparency and countervailing buyer power.
Failure to adhere to merger control procedures may result in financial penalties of up to 10 per cent of the merger parties’ turnover (for up to three years) in addition to other remedies such as the dissolution of the merger or subsequent divestments.

On 24 September 2018, the CCCS issued an infringement decision imposing financial penalties in excess of S$13 million and directions on Uber Technologies, Inc (Uber) and Grab Inc (Grab) entities to lessen the impact of the sale of Uber’s Southeast Asian business to Grab for a 27.5 per cent stake in Grab. The directions included the removal of Grab’s exclusivity arrangements with drivers and taxi fleets, maintenance of Grab’s pre-merger pricing algorithm and commission rates, and the sale of Uber’s rental fleet to potential competitors if an offer is made based on fair market value.

The infringement decision revealed that the parties had failed to notify the CCCS of the merger despite letters having been sent by the CCCS. Further, the CCCS noted that the parties did not merely provide for antitrust penalties but had ‘precisely’ apportioned such antitrust penalties suggesting they had given consideration to the likelihood that the transaction would breach antitrust rules and result in financial penalties. Accordingly, the CCCS found that they had ‘intentionally, or negligently, infringed the Section 54 prohibition’.

Corporations should be alert to competition law concerns that may arise in their commercial dealings or even in industry gatherings, bearing in mind that that the CCCS is empowered to and does conduct investigations into un-notified mergers and that offenders will suffer both financial and reputational losses.

X  OUTLOOK

Officially, Singapore’s economic outlook is positive with forecasts by the Ministry of Trade and Industry in February projecting growth of between 1.5 to 3.5 per cent. However, the recent escalation of the United States’ trade war with China has caused market volatility and cast uncertainty on the global economic outlook. Singapore’s small and open economy is reliant on trade and susceptible to the vicissitudes of the global economic climate. Cautious buyers may want to adopt more protective provisions and contractual outs in the event of any adverse change in the external environment. Conversely, cautious sellers may want to structure more punitive mechanisms, including reverse break fees, for any deal discontinuation.

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61  Ministry of Trade and Industry.
I OVERVIEW OF M&A ACTIVITY

In recent years, we have seen an increase in complexity and sophistication in the Spanish M&A market caused by the emergence of new players, as well as new and more complex financing formulas and deal structures. 2018 was another excellent year for the Spanish economy and for Spanish M&A, thus confirming the positive expectations anticipated in the last edition of The Mergers & Acquisitions Review.

In 2018 and the first quarter of 2019, Spain consolidated and strengthened the recovery it began in mid-2013. The imbalances accumulated over the years have been substantially reduced, creating a more favourable environment and increasing Spanish companies’ (as well as Spain’s) access to capital markets. As a consequence, GDP grew by 2.6 per cent in 2018. High liquidity in the debt and capital markets, increased investment capacity of private equity and funds (especially international funds), the success of fundraising, low interest rates and the strategic push of big corporations compensated for macroeconomic uncertainties. Despite certain unfavourable political conditions, economic growth also remained strong in the first half of 2019 (with forecasts in the region of 2.4 per cent), backed by improved labour market prospects, less stringent financial conditions and renewed confidence, and also aided by favourable external developments. These factors are expected to lay the foundations for a stable economy in coming years.

The very positive development of Spain’s economy has been counterbalanced by certain political instability (epitomised by the motion of no confidence that led to a change of government in June 2018, and by the still-existing challenges fostered by some pro-independence regional parties in Catalonia) and by uncertainties about the future of the public pension system. Other uncertainties affecting M&A activity include concerns about the global economy – particularly the economic situations of the emerging economies, and in particular the situation of South American countries, which are the traditional target of Spanish direct foreign investments – uncertainties related to Brexit’s final outcome and its impact on the European project, and tense trade relations of Europe and China with the United States.

Despite these apprehensions, M&A activity in Spain has been very solid. M&A targeting Iberia in 2018 increased considerably in terms of volume from the preceding year (an approximate increase of €18 billion from 2017), reaching record levels. In 2018, Spain was one of the leading countries in the eurozone and the fifth in the world in rankings based on volume of M&A transactions. The number of deals in 2018 was also higher than in 2017.
Spain's outlook for 2019 and 2020 remains strong, and we expect this to result in a significant increase in deal announcements throughout the second half of 2019.

The main drivers of M&A activity continue to be the following:

a. Spanish targets have become attractive due to the strengthening of their operations and balance sheets, the significant improvement of the macroeconomic environment, including the depreciation of the euro, and the availability of debt financing buttressed by low interest rates, which are not expected to increase.

b. Spanish corporate and financial institutions are completing their deleveraging processes. Spanish banks and other financial institutions have continued selling non-core assets and branches, divested performing and non-performing loan portfolios, and have exited from industrial shareholdings.

c. Energy, healthcare, tourism, IT and telecommunications have also attracted significant investments due to an increased consolidation in those industries and changes in the regulatory framework. In 2018, real estate was also particularly relevant due to the continuous increase in prices over recent years.

d. Foreign strategic and financial investors remain focused on Spain and interested in both strategic and opportunistic investments. Europe is the main source of those investments, followed by North American and Latin American investments, mainly from the United States and Mexico. Certain Asian countries (Hong Kong and Singapore, mainly) have also been relevant players in terms of foreign investment.

e. Europe (and particularly Spain) is still experiencing an increase in private equity M&A transactions in comparison to previous years. Indeed, private equity investments have returned to pre-crisis levels, and exits have also increased as private equity sponsors continue to be under pressure to divest holdings acquired before the financial crisis.

f. Outbound foreign investments have also increased, focusing Spanish investments mainly on Europe, Latin America and the United States, and to a lesser extent Asia.

g. Initial public offerings (IPOs) remained strong in the Spanish market.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

i. Corporate law

The basic Spanish legal framework for corporate acquisitions, mergers and other types of corporate restructuring includes elements of both contract and corporate law.

Spanish contract law is mainly contained in the Civil and Commercial Codes of the 19th century. Seeking to modernise and update this legal framework, the Ministry of Justice worked on a new Commercial Code with the aim of codifying the entire body of law on commercial contracts into a single piece of legislation. The first draft was submitted for public consultation in June 2013, and the government approved the draft bill in May 2014. However, the draft bill has not yet been submitted to Parliament. Following the general elections in April 2019, and thus a possibly new and stable government, this pre-parliamentary activity is likely to resume.

Spanish corporate law, on the other hand, is primarily based on the Companies Law and the Law on Corporate Restructuring. The Companies Law governs, inter alia, joint-stock
companies (sociedades anónimas) and limited liability companies (sociedades de responsabilidad limitada), the most common corporate forms in Spain. It also sets out the basic legal framework for listed companies.

The Law on Corporate Restructurings regulates mergers, spin-offs, conversions, en bloc transfers of assets and liabilities, and international transfers of registered addresses. It also specifically regulates mergers following a leveraged buyout (LBO) (i.e., mergers between companies where one has incurred debt during the three years preceding the acquisition of control – or the essential assets – of the target company). The Law requires, inter alia, that an independent expert determines whether an LBO constitutes financial assistance, a circumstance the Companies Law generally prohibits. It does not, however, establish the effects of an independent expert's finding of financial assistance, a situation that creates uncertainty in LBOs, particularly due to legal interpretations by the Spanish commercial registries.2

The rules that must be taken into account in connection with the main regulated markets include the Consolidated Stock Market Law3 (framework for the securities market), the Law on Discipline and Intervention of Credit Institutions4 (framework for the credit market) and the Private Insurance Supervisory Law5 (framework for the insurance market).

ii Insolvency law

The general legal framework on insolvency is primarily contained in the Insolvency Law.

The Insolvency Law created a single insolvency procedure applicable to all insolvent debtors (i.e., debtors who are, or will imminently be, unable to regularly comply in a timely manner with their payment obligations). The single procedure has a joint phase with two potential outcomes: a creditors’ agreement (in which the debtor and creditors reach an agreement on the payment of outstanding claims), or the liquidation of the debtor's assets to satisfy its debts. It has also clarified the risks associated with the clawback (rescission) of transactions carried out within the two years preceding a declaration of insolvency that are considered detrimental to the debtor's estate.

The Insolvency Law was generally viewed as a positive development. Nevertheless, the legislation was passed in a completely different economic and financial climate, rendering it necessary to amend it in 2009, 2011, 2013, 2014 and 2015.

The most significant recent developments have been Royal Decree-Law 1/2015 of 27 February and Law 9/2015 of 25 May. These reforms generally sought to improve various aspects of the pre-insolvency institutions to ensure the viability of companies in an attempt to avoid insolvency (inter alia, to introduce the protective shields of refinancing agreements) and align the Insolvency Law with current practices and insolvency regulations in other comparable jurisdictions, as well as to eliminate specific rigidities and improve various technical aspects criticised by judges, legal scholars and lawyers alike.

According to recent statistics, the number of insolvency proceedings has increased with respect to 2017, breaking the downward trend since 2013.

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2 Translations (into English and French) of these laws are available on the Spanish Ministry of Justice website: www.mjusticia.gob.es.
3 The securities market is supervised by the National Stock Exchange Commission.
4 The credit market is supervised by the Bank of Spain and credit institutions by the ECB or the Bank of Spain.
5 The insurance market is supervised by the General Insurances and Pension Funds Directorate.
iii Other regulations
Other matters relating to, inter alia, tax, employment and competition law also form part of the M&A legal framework (see below).

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Due to parliamentary inactivity in recent years as a result of the difficulty of obtaining majorities in Parliament, there has been reduced legislative activity in terms of corporate and takeover law.

In 2018, the Companies Law and the Commercial Code were amended to further develop the information rights of shareholders in connection with non-financial matters. The goal of this amendment, inspired by the Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups, is to provide stakeholders with certain non-financial sensitive information, such as, inter alia, actions aimed at fostering respect for human rights and sustainable growth, anticorruption mechanisms and fighting against discrimination.

A Business Secrets Law was enacted in February 2019. This new regime, which is complemented by other existing regulations (such as unfair competition law or the law regarding the regulation of criminal breaches of confidence) provides companies operating in Spain with a useful mechanism to protect trade secrets from third parties’ illegal interference.

Likewise, it is worth noting Royal Decree Law 19/2018 on payment services, which provides comprehensive regulation of the professional activity of payment services; and Royal Decree Law 14/2018, which modifies Royal Legislative Decree 4/2015 of 23 October on the Consolidated Stock Market Law and introduces reinforced protection mechanisms for financial investors.

It is also foreseen that during 2019, a new regulation of the commercial registry will be approved (the current regulation dates back to 1996) that will modernise its mechanisms and organisation, and adapt this legislation to the current corporate legal regime.

Apart from these legislative developments, the most recent regulations, which were further analysed in previous editions, were the following: Royal Legislative Decree 4/2015 of 23 October on the Consolidated Stock Market Law; the Law 11/2015 of 18 June on credit institutions’ recovery and resolution; and Royal Decree 877/2015 of 2 October on legislative developments of the Savings Banks and Banking Foundations Law and the Circular of the Bank of Spain 6/2015 of 17 November (which further developed the provisions of Royal Decree 877/2015).

Finally, albeit not having an ad hoc regulation under Spanish law, during 2018 we witnessed a progressive increase in the use of formulas aimed at minimising the risks assumed by parties in M&A deals. From these formulas, it is worth noting the increasingly important role of warranty and indemnity (W&I) insurance, which covers losses arising from specific indemnities and the representations and warranties included in sale and purchase agreements.
IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In 2018 saw an increase in the interest of international investors in the Spanish real estate, energy, tourism, engineering and insurance sectors. Private equity investments continued to grow, and the outlook for 2019 both for inbound and outbound M&A remains strong. 2018 saw the following:

- The acquisition of Abertis Infraestructuras, SA by a consortium formed by ACS SA, Atlantia SpA and Hochtief AG, for €32.1 billion;
- Taiyo Nippon Sanso’s acquisition of the industrial gas and related machinery and equipment business of Praxair, Inc, for €4.9 billion;
- Lone Star’s €3.9 billion acquisition of an 80 per cent stake in the real estate business of CaixaBank SA as well as Servihabitat Gestion Inmobiliaria, SLU;
- The acquisition of a 20.07 per cent stake in Naturgy by CVC and Corporación Financiera Alba from Repsol SA for €3.8 billion; and
- The €3.5 billion acquisition of a 59.2 per cent stake in Itinere Infraestructuras, SA from Gateway Infrastructure Investments, LP, a US-based fund managed by Corsair Capital LLC, Liberbank SA and Sacyr SA, from APG Group NV, a Netherlands-based pension fund asset manager, and Corsair Capital LLC, a US-based private equity firm.

The following, among others, were announced in 2019 or are in the pipeline:

- The acquisition by LetterOne, an international investment business based in Luxembourg, of DIA Distribuidora Internacional de Alimentación, for €1.7 billion;
- PAI Partners SAS, a France-based private equity firm, through its PAI Europe VII fund, announced its acquisition of Areas, SA, a Spain-based company engaged in food and beverage services and travel retail business, from Elior SCA, a listed France-based company, for a consideration of €1.54 billion;
- The acquisition of Universidad Alfonso X el Sabio by CVC for €1.1 billion;
- The acquisition of 89.7 per cent of Hispasat SA by Red Eléctrica de España from Abertis Infraestructuras for €949 million; and
- The acquisition of Grupo Konectanet by Intermediate Capital Group (UK) from Santander and PAI Partners, for €700 million.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Public M&A

Public M&A also witnessed more activity, with the increased interest of international investors in real estate, construction and infrastructure and energy public megadeals:

- The aforementioned acquisition of Abertis Infraestructuras, SA by a consortium formed by ACS SA, Atlantia SpA and Hochtief AG;
- The €2.5 billion takeover bid for Saeta Yield, the Spain-based and listed renewable energy company, by Brookfield Asset Management, the Canada-based and listed alternative asset manager, through TerraForm Power;
- The Carlyle Group’s acquisition of a significant minority stake in Compañía Española de Petroleos, SAU (Cepsa), a Spain-based company engaged in the exploration for and production of petroleum, and the refining, distribution and sale of crude oil, natural gas and electricity, from Mubadala Investment Company PJSC, the UAE-based sovereign wealth fund, for €2.2 billion;
Spain

the acquisition by a group of investors of a 50.1 per cent stake in Redexis Gas SA from Goldman Sachs Infrastructure Partners for €2 billion; and

Minor International’s €2.7 billion offer for NH Hotel Group.

ii Real estate

As mentioned in previous editions, real estate has established itself as a prominent field for M&A activity after years of market corrections. Attractive prices combined with banks’ need to clear their balance sheets of real estate assets have catalysed the resurgence of real estate transactions in the Spanish market. To foster this resurgence, the government has not amended the tax framework applicable to the Spanish SOCIMIs, which are similar to real estate investment trusts and which are more attractive to investors.

Investor appetite made 2018 a good year in quantitative terms, including the following:

a the acquisition by Lone Star of 80 per cent of the real estate business of Caixabank for €3.9 billion;

b Minor International, a Thailand-based and listed hospitality group, launched an offer for NH Hotel Group for €2.7 billion;

c Blackstone Group, via Tropic Real Estate Holding, SL, acquired Testa Residencial from Merlin Properties Socimi, SA, BBVA SA, Acciona Inmobiliaria SL and Banco Santander, SA for €2.5 billion;

d Blackstone Group made a takeover offer to buy the remaining shares it did not own in Hispania Activos Inmobiliarios SOCIMI, SA for €2.29 billion; and

e Inmobiliaria Colonial, SA acquired a 22.19 per cent stake in Societe Fonciere Lyonnaise SA from Qatar Investment Authority for €718 million.

In addition, Santander sold Testa Residencial to Blackstone, while Cerberus acquired BBVA’s real estate business. The pipeline for such assets looks healthy, with both Banco Sabadell and SAREB reportedly looking to sell portfolios.

iii IPOs

Although we have witnessed the launch of Metrovacesa, Árima, Solarpack y Amrest IPOs, 2018 was a bad year for the Spanish Stock Exchange, both on the traditional continuous market and on the Mercado Alternativo Bursátil, a market (with a special set of regulations) for small companies seeking to expand.

In general, forecasts for 2019 are much more optimistic, as companies (some of which had to postpone IPOs initially planned for 2018), including Glovo, Cepsa, Via Célere, Tendam (formerly Cortefiel) and Cox Energy, among others, could launch IPOs during 2019 and become important actors on the Spanish Stock Exchange.

iv Private equity

Spanish private equity activity in 2018 increased compared to 2017, showing the highest ever number of buyouts (€26.7 billion in comparison to €13.5 billion in 2017) and the second highest ever number of exits (€16.6 billion).

Spain has had two consecutive years of record investment volume, which is positive news not only for private equity activity but for the Spanish economy as a whole. In 2018, more foreign investors (private equity, hedge funds and investment banks) landed in Spain looking for investment opportunities. Domestic private equity funds and asset managers remained interested in co-investment opportunities with foreign-funds, offering their ‘boots
on the ground’ approach and expertise to larger players, spurring M&A activity. According to the Spanish Venture Capital & Private Equity Association, the total investment volume in the Spanish private equity market last year reached a new record of over €6,000 million across 740 investments. This was driven by a number of big-ticket equity deals, the strong activity of international funds, the outstanding performance of the mid-market, a rise in investments made by private domestic firms and a clear dynamism on the divestment front.

International funds accounted for 77 per cent of the total investment volume (with €4.25 billion invested across 118 deals), which keeps suggesting that Spain is the ‘place to be’. However, domestic players have also been very active. On the divestment front, nearly 50 per cent of exits took the form of sales between private equity houses, while almost a quarter involved industrial operators.

The most active sectors for private equity deals by deal count were real estate, technology, media and telecommunications, and energy.

Technology sectors in Spain have made impressive progress in the past few years. They have showcased the greater number of deals per industry sector in 2018, with steady growth in deal value. The important international component of technology-driven transactions evidence how Spanish companies have developed experience at home that they have exported overseas with great success.

Some of the most active funds included Blackstone, KKR, CVC, Carlyle, Cinven, Lone Star, Apollo, Cerberus, Oaktree and TPG, while we saw increased activity by other international players such as Ardian, Bain Capital and EQT Partners. New landings of foreign investors in 2018 included Orient Hontai, Peninsula Capital or SK Capital Partners.

Average Iberian EBITDA buyout multiples stood at 16.5 times EBITDA in 2018, up from 11.8 times EBITDA in 2017.

2018 deals

a The acquisition by Lone Star of 80 per cent of the real estate business of Caixabank for €3.9 billion;
b the acquisition of a 20.07 per cent stake in Naturgy by CVC and Corporación Financiera Alba from Repsol SA for €3.8 billion;
c APG Group NV’s and Corsair Capital LLC’s €3.5 billion acquisition of a 59.2 per cent stake in Itinere Infraestructuras, SA from Gateway Infrastructure Investments, LP (managed by Corsair Capital), Liberbank SA and Sacyr SA;
d Blackstone Group’s €2.5 billion acquisition of Testa Residencial from Merlin Properties Socimi, BBVA, Acciona Inmobiliaria and Banco Santander; and
e the voluntary tender offer launched by Brookfield Asset Management over shares representing 100 per cent of the share capital of Saeta Yield for €2.45 billion.

2019 deals

a The previously mentioned Carlyle Group’s acquisition of a significant minority stake in Cepsa for €2.27 billion. As a part of the deal, Carlyle will acquire a stake of between 30 and 40 per cent.
b the acquisition of Areas, SA from Elior SCA for a consideration of €1.54 billion by PAI Partners through its PAI Europe VII fund; and
c a consortium led by EQT Partners comprising Groupe Bruxelles Lambert SA and Corporacion Financiera Alba SA launched a tender offer to acquire Parques Reunidos Servicios Centrales SA for €1.2 billion.
There have been no signs of a slowdown in the private equity industry in Spain in 2019: to the contrary, the fundraising carried out by international and domestic funds in previous years, the envisaged interest rates and investors’ demands for investment alternatives suggest that 2019 will continue to be buoyed by the strong tailwinds of the past two years.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

i General overview

In 2018, the acquisition finance market continued its expansion following the recovery from the financial crisis, establishing itself as an essential business within the M&A framework. Bank liquidity improved, and traditional lenders that were dominant prior to the crisis and that overcame the restructuring of the financial sector (e.g., BBVA, Caixabank, Sabadell, Banco Santander) are once again focused on their lending activity with a positive but prudent approach.

Market estimates suggest that corporate and business loans from Spanish financing entities will increase during the second half of 2019, and that the availability of funds from Spanish banks (especially for non-investment grade borrowers) will continue to improve.

Debt funds have taken advantage of investment opportunities and continued low prices. Shadow banking has significantly increased its presence in the Spanish market, and traditional private equity players have started new investment activities, including direct lending.

Debt issuance of Spanish companies in the flexible and liquid Anglo-Saxon markets were consolidated during 2018 and the first quarter 2019 (in spite of Brexit), most notably by real estate companies, which used to be a sector financed by traditional lenders. Specific Spanish companies (including financial entities) have also used the Spanish market for their debt issuances, some of a considerable volume.

Competition has forced Spanish banks to offer higher leverage, lower pricing and more flexible structures.

ii Financing conditions

Apart from these general trends, the following continued to be the main features of acquisition financings in 2018:

a The range of financing products available to borrowers is exceptionally broad: second-lien facilities, ancillary facilities, unitranche, mezzanine, bridge-to-equity facilities, bridge-to-bonds and equity-like facilities are being offered by Spanish banks due to stronger competition. Vendor loans and non-banking loans (e.g. those originating from debt funds) continue to be frequently used to finance acquisitions.

b Banks still refrain from agreeing to the certainty of funds provision in commitment letters, whereas the inclusion of material adverse change clauses and ‘diligence out’ provisions continue to be common. Limits to changes in pricing that can be arranged without the borrower’s consent have widened under the market flex provisions, and reverse flex provisions have not returned. Facility agreements still include broadly drafted market disruption clauses.

c Traditional lenders have made efforts to adapt covenants related to the disposal of assets, corporate restructuring transactions and guarantee thresholds provided by the
borrower’s group to covenants customarily used in high-yield bond transactions to offer more flexible financing that does not restrict the borrower’s capacity to take business decisions if the financial ratios are not breached.

### iii Other regulations

The enactment of Law 5/2019 on real estate credit agreements has improved the regulation of consumer protection in credit agreements relating to residential immovable property. Since the main goal of this regulation is to improve consumer protection in the field of real estate credit agreements willing to acquire real estate for residential purposes, it may not affect contracts between non-consumers.

Likewise, Royal Decree Law 17/2018 was enacted in November 2018 and established that lenders (and no longer borrowers) are liable in relation to the tax authorities to pay stamp duty upon the execution of mortgage-backed loans. In practice, however, lenders have increased the costs of financing to compensate for this new burden, which is often ultimately borne by the borrower.

### VII EMPLOYMENT LAW

The main legal framework of labour law in Spain is the Statue of Workers, which regulates the rights and obligations of employees and employers within the framework of labour relationships. The most recent relevant legislation in terms of labour law was Royal Decree-Law 8/2019 on urgent measures on social protection and against labour precariousness with regard to working hours, which was enacted on 8 March 2019. Royal Decree-Law 8/2019 introduced a set of measures aimed at improving the precariousness of the Spanish labour market and Spanish social security payments.

Transfers of undertakings are governed by Article 44 of the Statue of Workers on terms similar to other jurisdictions within the European Union:

a. the transferee company must assume all the transferor’s employees assigned to the transferred business or production unit, maintaining all their previous labour and social security rights (including pension commitments); and

b. transferor and transferee companies will be jointly and severally liable for three years after a transfer of undertakings takes place in relation to any labour and social security obligations not met before the transfer.

The legal regime for managing and executive directors is not provided for in the Statute of Workers, as these directors are not considered employees. Their service contract must be approved by the board of directors (without the involvement or vote of the relevant director). Such contract must include all the terms and conditions under which services are provided, especially all remuneration and compensation, and directors will not be allowed to receive any payment not expressly set out in their contracts. On 26 February 2018 the Spanish Supreme Court issued a very controversial judgment declaring that the remuneration of managing and executive directors is subject to the same requirements and formalities as those applicable to any other director. Their remuneration must therefore be included in the overall limit approved by the shareholders’ meeting for all directors.
VIII TAX LAW

The government approved a significant tax reform that entered into force on 1 January 2015 and that included significant amendments to the Spanish tax regulations through the approval of Law 27/2014 of 27 November on Corporate Income Tax (CIT Law) and Law 26/2014 of 27 November, which modified the Personal Income Tax Law and the Non-Resident Income Tax6 (Law 26/2014). Moreover, on 30 September 2016 the government approved Royal Decree Law 2/2016 of 30 September on tax measures to reduce the public deficit (RDL 2/2016), which also contained relevant measures. The most relevant novelties for the M&A practice were the following:

i Definition of business activity for CIT purposes

According to the wording of the CIT Law, a business activity exists for CIT purposes when there are sufficient human and material resources to carry out the corresponding business activity at the level of the group of companies to which the corresponding company belongs.

ii Non-deductibility of impairments

Impairments of company shares due to the depreciation of real estate assets are no longer tax-deductible.

iii Deductibility of financial expenses

Interest accrued on intragroup profit participating loans (PPLs) are treated as dividends for CIT purposes for the lender; consequently, expenses derived from PPLs (when granted to related entities) are no longer deductible by the borrower for CIT purposes. This measure affects PPLs signed after 20 July 2014.

Following the OECD recommendations included in the BEPS Actions reports, the CIT Law modified the treatment of hybrid instruments to tackle hybrid mismatches, stating that the expenses incurred in related-party transactions will not be tax-deductible if, as a result of a different tax classification in the country of residence of the recipient, no income is generated, or income is tax-exempt or subject to a nominal rate lower than 10 per cent.

The CIT Law maintained the general limitation on the tax deductibility of net financial expenses (30 per cent of operating profits), with a minimum deductibility threshold of €1 million.

An additional limitation on leveraged acquisitions was introduced: financial expenses derived from the acquisition of companies that join a CIT tax group after its acquisition or are subject to reorganisation transactions in the subsequent four years will be deductible from the buyer’s tax base up to the additional limit of 30 per cent of the operating profit of the acquiring company. This limit does not apply if the portion of the purchase price financed with debt does not exceed 70 per cent of the total purchase price and, in the following eight tax years, the debt is reduced annually by one-eighth of the principal amount until the principal amount is reduced to 30 per cent of the initial purchase price.

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iv  Transfer pricing rules
The CIT Law modified the definition of a related party between parent and subsidiary entities: the relevant shareholder's stake needs to be at least 25 per cent, or the relevant shareholder must be able to exercise decision-making powers (the threshold was 5 per cent before).

v  Participation exemption framework
The CIT Law extended the application of the participation exemption regime to dividends and capital gains from Spanish-resident companies, which previously was only applicable to non-resident companies. This essentially implied that, subject to further analysis on a case-by-case basis, capital gains realised on the sale of a Spanish company by its Spanish parent company may be exempt, provided that minimum ownership of 5 per cent or a cost of acquisition of at least €20 million is held during the year preceding the date on which the transfer is completed or, in the case of dividends, it has been maintained for the time required to complete that period. Additionally, if a foreign subsidiary is involved, the subsidiary must be subject to a minimum level of nominal taxation of 10 per cent in its home country. Although it is not expressly established in the CIT Law, the Spanish tax authorities also require the holding company to be incorporated for valid economic reasons and not merely as a conduit company with the main objective of avoiding taxation on the capital gains realised on the transfer of its subsidiary. Therefore, the holding company should be a real company that carries out a business activity for tax purposes and not a mere inactive income company.

The amendments to the participation exemption framework have also been introduced for the branch participation exemption. A minimum level of nominal taxation of 10 per cent under a foreign corporate tax system similar to the Spanish CIT is required. This requirement is considered to be met if the branch is resident in a country with which Spain has ratified a tax treaty for the avoidance of double taxation.

vi  Capitalisation reserve
The CIT Law replaced most of the tax credits currently in force (such as the reinvestment tax credit and the environmental investment credit) with a tax-deductible capitalisation reserve under which Spanish entities may, under certain circumstances, reduce their taxable base by 10 per cent of the increase in its net equity during the year. This is done by comparing the net equity at year-end (excluding the current year’s profits) with the net equity at the beginning of the year (excluding the previous year’s profits), and excluding any shareholder contributions and other items.

To be eligible to benefit from this tax relief, the amount of the net equity increase must be maintained for five years following the application of the tax deduction (except for accounting losses), and the company must report an accounting reserve in its annual accounts for the amount of the deduction. Except in certain situations, the capitalisation reserve cannot be distributed during the following five years.

vii  Carry forward losses
According to the CIT Law, offsetting accumulated tax losses is limited to 70 per cent of taxable income.

This limitation does not apply in the tax year in which a company is dissolved (except if derived from a restructuring transaction) or to specific types of income, such as that derived from debt cancellations without consideration when the creditor is not a related entity.
Despite introducing this limit to the offsetting of carry forward losses, the CIT Law removed the applicable 18-year limitation, allowing tax losses to be offset indefinitely.

The CIT Law also incorporated additional limitations to the use of tax losses for medium and large-sized companies. Thus, in the event that the company’s turnover in the preceding year is between €20 million and €60 million, offsetting the accumulated tax losses is limited to 50 per cent of the positive CIT base; and if the turnover is above €60 million, the use of losses is limited to 25 per cent of the taxable base of the company.

viii  Tax rate reduction
The CIT Law gradually reduced the CIT rate from 30 to 25 per cent. Moreover, a reduced 15 per cent tax rate was established for newly-created companies that carry out business activities. The rate applies during the first profitable tax year and the following year.

ix  CIT prepayments
RDL 2/2016 established new tax measures on CIT prepayments that applied to those whose payment period began after 30 September 2016. According to these measures, the CIT prepayment rate for CIT payers with a turnover exceeding €10 million in the prior fiscal year increased to 24 per cent (as opposed to the 17 per cent rate applicable to date) over the ongoing year’s taxable income. In any event, the CIT prepayment will amount to a minimum of 23 per cent (25 per cent for some types of entities) of the accounting result of the first three, nine or 11 months of each year; or, for taxpayers whose tax period differs from the calendar year, of the result of the period between the beginning of the tax period and the day before the start of each CIT prepayment period.

x  CIT group framework
Based on the ruling of the European Court of Justice of 12 June 2014, the CIT Law broadened the scope of companies eligible for the CIT group framework. Under the new framework applicable to CIT groups, all Spanish companies resident in Spain and permanent establishments of foreign-resident entities in Spain that have a direct or indirect common non-resident shareholder (insofar as the common shareholder meets specific requirements) may form a tax group for Spanish CIT purposes. In that circumstance, the common non-resident shareholder is considered the parent company of the CIT group, although it must appoint one of its subsidiaries as the group’s tax representative in relation to the Spanish tax authorities.

xi  Tax neutrality framework for mergers and demergers
The main amendments introduced by this framework were the following.

Unlike the previous regulation, the tax neutrality framework is now considered the framework applicable to mergers and demergers by default. A decision to not apply the tax neutrality framework must be communicated to the Spanish tax authorities.

The CIT Law extended the scope of the definition of partial demergers entitled to benefit from tax neutrality given that maintaining another business unit in the transferring entity is no longer required (i.e., the new CIT Law allows the application of tax neutrality when the transferring entity merely retains a controlling stake in a subsidiary).
In addition, the CIT Law allows carry forward losses to be transferred to the acquiring entity simultaneously with the going concern being transferred to the acquiring entity even if the transferring entity is not wound up.

Merger goodwill and other intangibles arising as a consequence of a merger are not recognised for tax purposes and will therefore no longer be deductible.

According to the current wording of the CIT Law, the tax authorities are only able to partly regularise a tax advantage unduly applied. The tax authorities are not able to claim taxes on unrealised gains by the transferring entity.

xii Non-resident income tax

Law 26/2014 reduced tax rates on income obtained by non-residents in Spain. The general tax rate is 24 per cent; the rate for EU residents is 19 per cent. Moreover, dividends, interest and capital gains are taxable at a rate of 19 per cent. The tax rate for permanent establishments was reduced to 25 per cent.

The most important development in relation to the EU Parent–Subsidiary Directive is that no Spanish withholding taxes are levied on dividends distributed by a Spanish subsidiary to its EU parent company when the EU parent company maintains a direct holding of at least a 5 per cent stake or €20 million in the Spanish subsidiary. The holding must have been held uninterruptedly for the year preceding the date on which the distributed profit is due or, failing that, for the time required to complete that period. The anti-avoidance rule was also amended, and applies when the majority of the parent company’s voting rights are directly or indirectly held by non-EU residents, unless it can be evidenced that the EU parent company has been incorporated and operated for valid economic purposes and substantial business reasons.

IX COMPETITION LAW

Under Law 15/2007 of 3 July on competition, transactions leading to a concentration that fulfil the following thresholds are subject to mandatory notification to Spain’s National Markets and Competition Commission (NMCC):

a as a consequence of a transaction, the undertakings obtain a market share of at least 30 per cent in a national market or a substantial part of it regarding a certain product or service. The market share threshold increases to 50 per cent if the target’s aggregate turnover in Spain was less than €10 million in the previous financial year; and

b the turnover of the undertakings in Spain in the previous financial year was at least €240 million, provided that at least two of the undertakings concerned had a minimum turnover of €60 million in Spain during the same period.

The Competition Law also includes a suspension obligation, requiring that the completion of a transaction meeting any of the thresholds be suspended until clearance is granted.

In 2018, the number of notifications filed was slightly lower (84) than in 2017 (96). Most of the notifications filed were cleared in the first phase without commitments, and only four of them were approved in the first phase with commitments. In one case, the NMCC initiated a second phase review and finally cleared the transaction with commitments. Real estate, the manufacturing sector, the chemical industry and the energy industry were the main sectors in terms of the number of transactions notified to the NMCC in 2018.
In terms of antitrust enforcement policy, in 2018 the NMCC continued to closely monitor companies’ compliance with its decisions through a specialised division within the Competition Directorate established to conduct such investigations. Within these proceedings, information requests are usually submitted to third parties enquiring about companies’ compliance with the conditions imposed.

As regards merger control, the NMCC has created a division to identify transactions that may be subject to merger control clearance in Spain in order to identify potential cases of gun jumping.

X OUTLOOK

Despite the political uncertainties and rumours of deceleration, M&A prospects in Spain for the second half of 2019 and 2020 are optimistic. The resilient macroeconomic scenario will continue to help M&A in general. Likewise, the improved improvement of the Spanish economy, continued deleveraging process, consolidation of key industries (tourism, telecommunications, energy, financial services), prospective political stability following the general elections in April, low interest rates and increased access to credit and other financing for Spanish corporations and private equity strengthen the belief that the volume and number of M&A transactions will be maintained in the short and medium term. On the negative side, high unemployment, despite the undeniable improvements in recent years, is still dampening consumer spending (although domestic demand has inched up). In this scenario, the government continues to struggle with a large deficit and some political instability.

The growing appetite of foreign investors for the Spanish economy, as well the global improvement of the economy and the high activity of M&A transactions worldwide, will continue to affect the high number of transactions involving foreign investors in Spain. European and US investors will continue to be the main players.

The new complexity of private M&A deals in Spain has led to multiple structures and formulas to determine the price of the transaction, such as rollovers, earn-outs and escrow mechanisms. W&I insurance has also become more prevalent, and not only in private equity sponsored transactions.

Finally, foreign private equity funds will continue investing in a wider range of industries including food and drink, retail, tourism, leisure, energy, infrastructure, real estate, and life sciences and pharma. Healthcare and pharmaceutical industries have potential, as public and private spending continues to increase in response to an ageing population. Renewables and technology have attracted investor interest in recent years. These investments are now appearing in a wider range of forms and vehicles.
I OVERVIEW OF M&A ACTIVITY

The number of M&A transactions involving Swiss businesses reached a peak in 2018, driven by strong activity in diverse sectors and an increase in private equity transactions, which constituted 32 per cent of M&A transactions in the period (up from 17 per cent in 2009). According to KPMG, there were 230 outbound deals in 2018, which was approximately double the number of inbound transactions. KPMG calculates the top 10 Swiss M&A transactions of 2018 as having a total transaction value of US$62.1 billion, with these transactions targeting the pharmaceutical, energy and utilities, consumer goods, logistics and fintech sectors. In the past five years, according to Dealogic, there has also been a steady growth in technology M&A transactions involving a Swiss buyer or target, with a total of 713 deals since 2014 offering an average transaction size of US$39 million.

These numbers show that relative to the size of its population, Switzerland plays a disproportionately important role in M&A in the DACH (Germany, Austria and Switzerland) region and offers interesting investment opportunities to foreign investors.

Some of the most notable deals in 2018 and Q1 2019 include the following:

a the spin-off by Novartis of Alcon Inc, with Alcon becoming dual-listed on the SIX Swiss Exchange and the New York Stock Exchange at a total valuation of 26.85 billion Swiss francs;

b Sunrise Communications’ announced indirect acquisition of UPC Switzerland from Liberty Global, with an enterprise value of 6.3 billion Swiss francs;

c the 2.9 billion Swiss franc acquisition of SIX Payment Services from SIX Group by Paris-listed Worldline;

d CMA’s acquisition of CEVA Logistics by way of a public tender offer at a deal value of 2.3 billion Swiss francs;

e the sale by EQT of a stake in Sportradar to CPPIB and Technology Crossover Ventures for 1.2 billion Swiss francs; and

f RenaissanceRe’s 1.5 billion Swiss franc acquisition of Tokio Millennium Re.

1 Manuel Werder, Till Spillmann, Thomas Brönnimann, Philippe Weber, Ulysses von Salis, Nicolas Birkhäuser and Elga Reana Tozzi are partners and Elga Reana Tozzi is a counsel at Niederer Kraft Frey Ltd.
II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A transactions are mainly governed by:

a the Swiss Code of Obligations, which provides the statutory framework for the acquisition and sale of companies (share deals) or of their assets and liabilities (asset deals);

b the Federal Act on Merger, Demerger, Transformation and Transfer of Assets, which regulates mergers, demergers, conversions and transfers of assets and liabilities; and


The FMIA applies to public cash and share exchange offers to holders of equity securities of companies whose equity securities are listed on a Swiss exchange (in the case of non-Swiss domiciled companies, the FMIA applies only to those companies with a primary, full or partial listing on a Swiss exchange). The rules and procedures applicable to public tender offers laid down in the FMIA and its implementing ordinances are designed to ensure fairness, equal treatment and transparency in voluntary and mandatory public tender offers. The obligation to launch a mandatory tender offer arises whenever a person or a group of persons acting in concert, directly or indirectly, acquires equity securities of a Swiss company listed in Switzerland, or a foreign company with a primary listing in Switzerland, and thereby exceeds the threshold of one-third of the voting rights (whether exercisable or not). In the case of a mandatory tender offer (including offers that would result in the triggering threshold being exceeded), the offer price per share may not be lower than the volume-weighted average stock price on the relevant Swiss exchange of 60 trading days prior to the formal announcement or publication of the offer or the highest price paid by the bidder (or persons acting in concert with the bidder) for equity securities (including options) of the target during the preceding 12 months.

The articles of association of listed companies may provide for a higher threshold of up to 49 per cent of the voting rights (opting up) or may declare the mandatory tender offer obligations to be not applicable (opting out). The Takeover Board (TOB) and its supervisory authority, the Swiss Financial Market Supervisory Authority (FINMA), monitor public tender offers. The TOB can issue binding orders against parties, which can be appealed to FINMA. FINMA’s decisions can be appealed to the Federal Administrative Court. The relevant decisions are published online.2

Various other rules may also be relevant for the acquisition and sale of corporate entities and of their assets and liabilities, including, among others:

a the listing rules of the respective stock exchange if the transaction results in the listing of new shares on a stock exchange;

b employment law (automatic transfer of employment relationships and information and consultation rights of employees);

c the Federal Act on the Acquisition of Real Estate by Persons Abroad, which contains regulations on the acquisition by foreign persons, or foreign-controlled companies, of residential property or land in Switzerland;

2 At www.takeover.ch.
the Federal Act on Cartels and other Restraints of Competition, which in combination with the Ordinance of Merger Control regulates merger control; and

industry-specific laws and regulations, such as financial services, telecommunications, insurance, and energy laws and regulations.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Private M&A

Corporate law is currently under revision in several aspects and with multiple aims. On 23 November 2016, the Swiss Federal Council issued a report on its amendment proposal. First, the Ordinance against excessive remuneration in listed stock corporations, which entered into force on 1 January 2014 as a transitional regulation, is to be adopted into federal law. Second, the rules on the incorporation of companies and the capital structure are to become more flexible. Third, the draft legislation contains a proposal for transparency rules for economically significant companies that are active in the extractive industries. Finally, guidelines on gender representation at board and senior executive level in major listed companies have been proposed.

The proposed new legal provisions that originate in the Ordinance against excessive remuneration in listed stock corporations foresee the following:

- Sign-on bonuses that do not offset any demonstrable financial disadvantage are to be prohibited or limited;
- Compensation for non-compete clauses that are not commercially justified are to be prohibited or limited;
- Shareholders may vote in advance or ex post on the remuneration for top managers. If shareholders vote in advance on the variable remuneration for top managers, they must also be presented with the annual compensation report for a subsequent consultative vote; and
- More effective ways shall be introduced for claiming the reimbursement of unlawful payments.

Furthermore, the Federal Council’s report provides for increased flexibility and simplification in a number of areas. Share capital may henceforth be denominated in a foreign currency. The new law introduces the possibility for a shareholders’ meeting to foresee a new capital band, which authorises the board of directors to freely increase (authorised capital increases) and reduce the share capital (authorised capital reductions) within the capital band without any need for further shareholder resolutions. In addition, the need for public certification by a notary for the incorporation of stock corporations, limited liability companies and cooperatives, and their dissolution and cancellation from the commercial register, will now be both possible and straightforward.

The Federal Council is further proposing reforms to other specific areas. For example, by revising the provisions on corporate restructuring, it aims to create incentives for companies to take necessary actions at an early stage and thus avoid insolvency. In addition, arbitral tribunals will be able to rule on disputes under company law as well to the public courts, as is the case at present.
Furthermore, in an effort to make financial flows in the commodities sector more transparent, the Federal Council has proposed, in an electronic report, the imposition of a requirement on significant companies that are active in the extractive sector to disclose payments to state bodies in excess of 100,000 Swiss francs per financial year.

Finally, the Federal Council proposed the introduction of gender guidelines for the boards of directors and executive boards of major listed companies, namely that women should account for at least 30 per cent of a board of directors and at least 20 per cent of an executive board. The law provides for a comply or explain approach, that is to say if these thresholds are not met, a stock corporation will be required to state the reasons, and the action that is being taken to improve the situation, in its remuneration report. The new law provides for transitory periods of five years for boards of directors and 10 years for executive boards.

The proposal has been discussed in one chamber of the Swiss Parliament but not yet in the other chamber. Only the legal commission of the second chamber has held discussions. It appears that the discussions may be extensive and time-consuming, and that the deliberations will result in changes to the proposed bill. It cannot therefore be anticipated when the new legislation will enter into force and in what exact form.

Public M&A

Public M&A activity was very active in 2018, and the Swiss Takeover Board issued a number of decisions. However, no major amendments were made to takeover legislation in 2018.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

There is no general foreign investment regime in Switzerland, on the basis of national interest and regardless of the industry sector, as it has been enacted in several other jurisdictions. In February 2019 the Federal Council decided against foreign investment controls for the time being. However, the Federal Council intends to conduct a monitoring procedure and review the matter within the next four years.

There are few foreign investment control restrictions applying to M&A transactions involving Swiss target enterprises. There are provisions in the legislation covering specific sectors. Restrictions apply to sectors such as banking, finance, insurance, telecommunication, transportation, energy, war materials, lotteries and gambling where approvals, state licences and concessions may be required (mostly on a federal level, but sometimes also on a cantonal level).

For example, for the acquisition by a foreign investor of a bank or financial institution that is prudentially supervised, an approval from FINMA is required, whereas different tests apply to the acquisition of a controlling stake (i.e., when foreigners holding qualified participations directly or indirectly hold more than half the voting rights or exert a controlling influence in any other way) and the acquisition of a minority interest. The approval of an acquisition of a controlling stake will depend, among other things, on the granting of reciprocal rights by the country in which the qualified participant is resident or domiciled.

Furthermore, for example, the Federal Law on the acquisition of real estate in Switzerland by non-residents (known as Lex Koller) restricts the direct or indirect acquisition of non-commercial real estate in Switzerland by foreigners. These rules may also apply to a target entity that has a commercial purpose and pursues commercial activities, if it owns residential real estate in its portfolio or if it has significant unused land reserve.
One of the most innovative and notable M&A transactions in Switzerland in recent years was completed in 2018: the takeover of Actelion Ltd, the Swiss-listed biotech company, by Johnson & Johnson. The purchase price of US$30 billion in cash makes this the largest biotech transaction in Europe. Johnson & Johnson agreed on 26 January 2017 to launch a public cash offer for all shares in Actelion, which is listed on the SIX. As part of the agreed transaction, Actelion made a spin-off of its promising drug discovery operations and early-stage clinical development assets into a newly created Swiss biopharmaceutical company, Idorsia Ltd. Before closing, the shares in Idorsia were, by way of an extraordinary dividend in kind, distributed to Actelion’s shareholders, and at closing the shares in Idorsia were listed on the SIX, thereby starting a biotech start-up with more than 600 employees, more than 1 billion Swiss francs in cash and an initial public offering (IPO) at its first business day. This transaction structure allowed the shareholders of Actelion to keep the potential profits of the research that Actelion had been nurturing for decades with its outstanding research team, bridging the problem that it would have been very difficult to agree with Johnson & Johnson on a reasonable valuation of this high-risk, early-stage research business. It also allowed a large number of the management team at Actelion, including chief executive officer Paul Clozel, to continue to work in an independent company with a very entrepreneurial spirit. Johnson & Johnson bolstered its product portfolio with Actelion’s blockbuster drugs while also receiving an option on Idorsia’s ACT-132577, a compound for resistant hypertension that is in development.

As part of the transaction, Actelion had to be split by spinning-off its drug discovery operations and early-stage clinical development assets into a new entity. This complex undertaking had to be fully implemented within less than six months, including splitting the intellectual property portfolio and finding solutions for business functions that both business units had been sharing. As part of the transaction, Johnson & Johnson also acquired a significant shareholding in Idorsia, whereby a well-designed governance structure had to be developed to address concerns from the competent merger control authorities. Finally, Johnson & Johnson is also providing a credit facility to Idorsia.

In general, low interest rates and high cash levels at companies and sponsors continued to underpin the strong M&A activity in 2018. Large Swiss leveraged acquisition finance transactions are usually arranged by international banks through the UK or US markets and placed with banks and institutional investors using Luxembourg or Netherlands acquisition vehicle structures. In most cases, funding is made through both loans and bonds. The domestic acquisition finance market is mainly driven by the large Swiss banks and some smaller ones, such as cantonal banks and other smaller financial institutions. Because of the particularities of the Swiss tax laws, bonds issued by Swiss issuers are less attractive, in particular in the context of leveraged acquisition finance transactions. In addition, because of the negative interest rates, the trend of institutional investors (in particular, insurance companies and pension funds) and other non-bank lenders providing lending has also continued. Such investors are particularly interested in real estate, infrastructure and energy investments offering relatively secure long-term and resilient cash flow and return profiles.
VII EMPLOYMENT LAW

No major amendments were made to Swiss employment law in 2018. In the context of M&A transactions, the relevant rules are those governing the transfer of employees in the event of a transfer of an enterprise by way of an asset transfer, merger or demerger. These rules do not apply to share transfers. In the event of a transfer of an enterprise, the employment agreements with the employees transfer by operation of law unless an employee refuses the transfer, in which case the employment agreements will transfer to the acquiring party but be terminated within the statutory periods (i.e., one to three months, depending on the number of years the employee has been employed).

The employee representative body or, if there is none, the employees themselves, must be informed in due time prior to an anticipated transfer about the reasons for the transfer and the legal, economic and social consequences. If measures affecting employees are contemplated as an outcome of the transfer, the employee representative body or, if there is none, the employees themselves, must be consulted prior to any decision on these measures being made. This may conflict with stock exchange rules, which require that transactions are kept confidential until they are executed and that only a confined circle of persons are involved in the transaction process on a need-to-know basis.

VIII TAX LAW

On 19 May 2019, the Swiss corporate tax reforms were approved by popular vote. As of 1 January 2020, various tax provisions will enter into force, such as the cantons having to abolish their preferential tax regimes (e.g., holding and domicile privilege, mixed company status), and as consequence will reduce their corporate tax rates (subject to cantonal referendum, and in some cantons this will be subject to a vote during 2019). The main new rules include those regarding the introduction of a patent box regime, a R&D super deduction and the tax-neutral step up of the tax basis for migration to Switzerland. For companies losing their privileged tax status, a step up of the tax basis would be possible.

Under the Federal Direct Tax Act (FDTA), capital gains arising from the sale of privately held shares of a Swiss tax-resident person are tax-free. However, the tax law states some exemptions whereby a capital gain would be subject to income tax and withholding tax in the following two basic cases:

- a indirect partial liquidation, i.e., capital gains arising from the sale of at least 20 per cent of the capital of a company if the purchaser was a company or an individual person holding those shares as a business asset. It is a well-known practice that the seller asks for tax warranties and representations in the sale and purchase agreement, whereas the purchaser cannot merge the target with the acquisition company or declare a dividend from distributable non-business-related reserves (available at the date of the purchase) during a five-year blocking period; and

- b a transposition, that is to say a realisation of a nominal value gain if a shareholding of at least 5 per cent was contributed by an individual shareholder to a company in exchange for shares, with the result that the individual shareholder would own at

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3 Article 1b, Paragraph 3 of the FDTA.
4 Article 20a, Paragraph 1(a) FDTA.
5 Article 20a, Paragraph 1(b) FDTA.
least 50 per cent. The minimum shareholding quota of 5 per cent will be reduced to zero as of 1 January 2020 (i.e., even a contribution of one share into a controlled company could result in a transposition treatment). This should not only be considered for family-owned businesses but also in the case of an IPO. In practice, shareholder agreements and the execution of call options could also trigger a transposition and requalify a nominal value gain into taxable income.

In recent years, the Swiss Federal Tax Administration (SFTA) has developed a new practice for cases of substitutional liquidation, that is to say when a non-Swiss holding company would sell its Swiss subsidiary to a company that is tax-resident in a third country and the Swiss subsidiary would be merged with the non-Swiss tax resident acquisition company, which would result in the distributable reserves of the Swiss subsidiary being transferred to the non-Swiss tax resident company and, accordingly, no longer being subject to Swiss withholding tax. The SFTA could in such a case levy a withholding tax at a rate that is the difference between the residual tax rate applicable pursuant to the applicable double tax treaty between the seller state and Switzerland and the applicable double tax treaty between the state of the acquisition company and Switzerland.

The SFTA could in some cases also refuse the refunding of withholding tax if it is deemed that there has been an international transposition, that is to say if a surplus was to be returned to a shareholder through the repayment of loans or by distributing capital contribution reserves instead of a dividend distribution that would be subject to Swiss withholding tax: for example, a Swiss company held by non-Swiss individuals, which cannot benefit from a full refund of the Swiss withholding tax, would be transferred to another Swiss company that could benefit from a full refund of the Swiss withholding tax.

Attention should also be given if a target company has an employee share option plan in place. The relevant practice is very strict in respect of the requalification of a capital gain into salary income. In particular, if an employee buys shares (cash settlement of the purchase, i.e., not when shares are issued as a bonus compensation) at a value that is calculated based on an agreed formula, and those shares would be sold to a third party based on a different fair market value calculation, the surplus gain (i.e., the difference between the actual formula value and the effective fair market value) would be requalified as salary income and be subject to income tax, and to social security and eventually to pension funds (or even source taxes), which might be a liability of the company.

Furthermore, the facts and circumstances of purchase price payments related to certain earn-out clauses need to be analysed carefully given that such payments could also be requalified as a salary income.

Switzerland still levies stamp duty of 1 per cent on the issue of shares, but restructuring exemptions are available. Based on a recent Federal Supreme Court case, stamp duty would be due in the case of a quasi-merger if no new shares were issued (i.e., shares in one company would be contributed to another company). In practice, until now it has been possible to contribute to another company without issuing new shares (i.e., in cases of internal reorganisations), but going forward, it is mandatory to issue at least one share.
Under the current merger control legislation, the following transactions are deemed to be a concentration of undertakings subject to merger control:

- a statutory merger of two or more previously independent undertakings;
- the acquisition of control over one or more previously independent undertakings or parts of undertakings through any transaction, in particular the acquisition of an equity interest or the conclusion of an agreement; and
- the acquisition of joint control over an undertaking (joint venture).

Control is assumed if an undertaking can exercise a decisive influence over the activities of the other undertaking by the acquisition of rights over shares or by any other means. The means of obtaining control may, in particular, involve the acquisition of the following:

- ownership rights or rights to use all or parts of the assets of an undertaking (if those assets constitute the whole or part of an undertaking, which is a business with a market presence to which a market turnover can be attributed); or
- rights or agreements that confer a decisive influence on the composition, deliberations or decisions of the organs of an undertaking.

Partial interests and minority shareholdings are only covered if they allow an undertaking to exercise a decisive influence over another undertaking (this can also be in combination with contractual agreements between the parties or factual circumstances). There is a risk that the acquisition of a minority interest may qualify as an anticompetitive agreement if the undertakings concerned agree to cooperate.

Planned concentrations of undertakings must be notified to the Competition Commission before their implementation if in the financial year preceding the concentration (cumulatively) the undertakings concerned together reported a worldwide turnover of at least 2 billion Swiss francs or a turnover in Switzerland of at least 500 million Swiss francs; and at least two of the undertakings concerned each reported a turnover in Switzerland of at least 100 million Swiss francs.

In the case of insurance companies, turnover is replaced by annual gross insurance premium income, and in the case of banks and other financial intermediaries by gross income.

The Secretariat decided that a joint venture is exempted from notification (even if the parent companies meet the thresholds) if the following two conditions are both met: the joint venture does not have activities in Switzerland or does not generate any revenues in Switzerland; and those activities or revenues are not planned in Switzerland and are not expected to take place in the future.

In addition to turnover, notification is mandatory if one of the undertakings concerned in proceedings under the Cartel Act in a final and non-appealable decision was held to be dominant in a market in Switzerland, and if the concentration concerns either that market, or an adjacent market or a market upstream or downstream of that market.

There is no applicable triggering event or time limit. However, notification must be made before the concentration is implemented. For public bids for acquisitions of undertakings, the notification must be made immediately after publication of the offer and before the acquisition is implemented. The Competition Commission should be contacted in advance so that it can coordinate the proceeding with the Swiss Takeover Board.

Under the current merger control legislation, the Competition Commission may prohibit a concentration or authorise it subject to conditions and obligations if the
investigation indicates that the concentration both creates or strengthens a dominant position liable to eliminate effective competition; and does not improve the conditions of competition in another market such that the harmful effects of the dominant position can be outweighed.

The following is currently being debated in Switzerland: the Federal Council has commissioned the Department of Economic Affairs, Education and Research to draw up a consultation proposal for adapting the merger control test. It is proposed that the current market dominance test applicable in Switzerland (under Article 10 of the Cartel Act) should be replaced by the significant impediment of effective competition test.

X OUTLOOK

Swiss M&A activity continues to punch above its weight, with particularly strong activity in the traditional powerhouses of the pharma, energy and utilities, consumer goods and fintech sectors. A steady increase in private equity involvement in Swiss M&A transactions has also contributed to growth in the market.
I OVERVIEW OF M&A ACTIVITY

Ukraine has experienced adverse economic and geopolitical conditions since 2014 that have had a negative effect on overall M&A activity in the country. Following recent economic and political stabilisation, deal activity significantly picked up, and starting from 2017, the market has started growing at a double-digit pace per annum.

M&A activity has been largely driven by major domestic Ukrainian players, which generated the majority of M&A activity in Ukraine and increased their outbound M&A activities. Foreign investors are also showing growing interest in investing into Ukraine. The most active sectors for M&A activities in 2018 were metals and mining and agriculture. The largest M&A transaction in 2018 was a transaction between domestic players in the metals and mining sector: the US$714 million acquisition of Donetsksteel by Industrial Coal Holding LLC.

There has been a lot of M&A activity in Ukraine’s agricultural sector, which sector has been historically the most resilient to the crisis. Agro deals involved land banks, processing and infrastructure facilities, the largest of which being the acquisition of Mria Agroholding by Saudi company SALIC UK Ltd, resulting in the investor increasing its land bank in Ukraine to a total of 210,000 hectares. Another landmark transaction in the agricultural sector involving outbound investment was the acquisition by MHP SE, a leading international agro-industrial group, of Perutnina Ptuj, an international meat-processing company and the largest producer of poultry and poultry meat products in Southeast Europe.

The real estate sector saw a lot of activity in commercial real estate in 2018, majorly driven by the acquisitions of retail and office spaces by the domestic investment fund, Dragon Capital, and other domestic players.

A lot of M&A activity is currently ongoing in the consumer good and retail sector. The landmark transaction in the sector was the merger of the Ukraine’s largest e-commerce players, Rozetka and EVO, aimed at the creation of a combined e-commerce platform and the optimisation of the suppliers’ base.

In the energy sector, foreign investors have shown increased interest in investing in Ukraine’s oil and gas sector through participation in tenders for concluding production sharing agreements.

In 2016, the government announced the privatisation of several large state enterprises, including Ukraine’s largest producer of nitrogen fertiliser, the state-owned Odessa Portside...
Plant, referred to by many as the crown jewel of Ukraine’s privatisation. Unfortunately, both attempts to auction off the plant failed to attract any bids from strategic investors. The privatisation of other large state enterprises, such as Centerenergo, has been put on hold.

II  GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Civil Code, the Commercial Code, the Company Law, the Limited and Additional Liability Companies Law (Law on LLCs), the Joint-Stock Company Law (JSC Law), the Law on the Securities Law and the Law on State Registration constitute the legal framework for M&A in Ukraine. The merger control rules and merger notification thresholds are set out in the Competition Law.

A corporate merger or an acquisition involving a joint-stock corporation (JSC) would also trigger the application of the Depository System Law and the Securities Market Law. Moreover, there are a number of additional rules and principles that are to be taken into account when preparing or conducting an acquisition of a JSC, such as:

- the rules relating to the disclosure of significant shareholdings in JSCs and ultimate beneficial owners;
- the rules relating to insider dealing;
- the rules relating to the public offer of securities and the admission to trading of these securities on a regulated market; and
- the general rules on the supervision of and control over the financial markets.

The Securities Commission supervises compliance with the takeover and JSC-specific regulations.

At the same time, JSCs have become less popular as a vehicle for conducting business activities in Ukraine. As of 1 May 2019, only 14,195 JSCs were registered in Ukraine according to the official statistics. In contrast, the statistics show that there were 646,928 companies in the form of limited liability companies (LLCs) in Ukraine on 1 May 2019, which is the most common vehicle for conducting business activities in Ukraine. Legal entities in Ukraine may also be established in the form of a general partnership, a limited partnership and an additional liability company.

Acquisitions of businesses and companies are usually carried out through the purchase of the participatory interests of an LLC or through the acquisition of the shares of a JSC. The majority of M&A deals are privately negotiated deals, as Ukrainian companies usually

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12 The National Securities and Stock Market Commission of Ukraine.
have one or several significant shareholders. JSCs may be public or private: the shares of a public JSC may be both privately and publicly placed, whereas the shares of a private JSC are privately placed among its shareholders. Asset acquisitions are also common, but they are technically more burdensome and time-consuming, and involve the imposition of VAT.

Because of the mandatory provisions of Ukrainian law and an imperfect court system, shareholders and participants in Ukrainian companies have traditionally preferred to set up holding companies in foreign jurisdictions such as Cyprus or the Netherlands, and to choose foreign law (mainly English) as the governing law of transaction documents. While recent developments in corporate and takeover law are intended to increase the attractiveness of structuring M&A deals in Ukraine and expose them to Ukrainian law, we do not expect a major change in deal structuring in the near future. In those cases where an investment has already been structured as a joint venture on the Ukrainian level, shareholders may choose to benefit from the new legislation and conclude Ukrainian law-governed shareholders’ agreements.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

The corporate and takeover laws in Ukraine were significantly amended between 2016 and 2018 in the course of the ongoing corporate reform.

i New takeover rules for JSCs and escrow accounts, and other important changes

The Corporate Governance Law,13 which became effective on 4 June 2017, introduced into Ukrainian law new takeover rules that are based on EU Directive 2004/25/EC of 21 April 2004 on takeover bids. The Law changed the rules for the acquisition of controlling stakes, introduced the concepts of squeeze-out and sell-out, and increased the disclosure requirements and thresholds for the approval of interested-party transactions.

Investors and shareholders should consider the new takeover rules when structuring M&A transactions that may result in the direct or indirect acquisition of shares in Ukrainian JSCs (even if such JSCs are not the direct acquisition targets), including:

a disclosing information on acquiring different stakes (for public JSCs: 5 per cent and more, 50 per cent and more, 75 per cent and more, and 95 per cent and more; for private JSCs: 10 per cent and more, 50 per cent and more, and 95 per cent and more);

b disclosing information on the highest acquisition price for controlling stakes (50 per cent plus one share, 75 per cent and more, and 95 per cent and more);

c complying with the procedure for submitting other notices on acquisitions of shares;

d complying with the obligation to make a mandatory bid to the remaining shareholders to purchase their shares at a fair price in cases of acquisition of the controlling stakes (50 per cent plus one share, or 75 per cent and more), including the timing of an irrevocable mandatory bid and the formula for determining the fair price (i.e., the price to be paid by the majority shareholder for the shares of the minority shareholder);

e squeeze-out: that is, the right of the dominant stakeholder (95 per cent and more) to require the holders of the remaining shares to sell him or her their shares; and

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sell-out: that is, the right of minority shareholders to require the dominant stakeholder to buy their shares at a fair price.

The long-awaited squeeze-out procedure entitles a shareholder that acquired the dominant controlling stake of 95 per cent and more of shares to require the holders of the remaining shares to sell him or her their shares within 90 days following the date of disclosure of the information on the acquisition of the shares. The dominant stakeholder intending to exercise its right to squeeze-out should first comply with the mandatory bid procedure. The price for the mandatory purchase of shares of minority shareholders should be determined according to the formula set out in the Corporate Governance Law.

An important highlight of the Corporate Governance Law is the introduction of the concept of escrow accounts into Ukrainian law. Escrow accounts are a commonly used instrument for securing payments among parties. Settlement of payment of the purchase price to minority shareholders as a result of the squeeze-out procedure should be made via escrow accounts without engaging a securities broker. This mechanism allows the elimination of ‘dead souls’ (i.e., minority shareholders (often deceased persons)) with whom any connection has been lost. As a result of the introduction of the concepts of squeeze-out and escrow accounts, dominant stakeholders will be able to consolidate 100 per cent of the shares in their hands.

According to information publicly available as of 31 May 2019, 259 JSCs have already launched squeeze-out procedures in Ukraine. Several court and administrative proceedings have also been initiated disputing the squeeze-out price, while the respective court practice is yet to be formed.

Another revolutionary development in Ukrainian corporate law is the introduction of the sell-out procedure. Minority shareholders now have the right to require a dominant stakeholder to buy their shares at a fair price to be determined similarly to the squeeze-out price. According to the transitional provisions, minority shareholders may exercise their sell-out right at any time following the acquisition of at least one additional share of a JSC by the dominant stakeholder after 4 June 2017.

At the same time, the Corporate Governance Law allows private JSCs to disapply rules or establish different rules in their charters regarding acquisitions of controlling stakes, squeeze-out and sell-out procedures, subject to having complied with the majority voting requirements set out in law.

Additionally, the materiality thresholds in excess of which interested party transactions should be approved by the respective corporate body of a JSC were changed from 100 minimum wages to 1 per cent of the assets value, based on the latest financial statements of a JSC.

The implementation of the Corporate Governance Law has facilitated changes in the types of JSCs from public to private, and cleared the market of quasi-public JSCs, particularly because the acquisition of shares in private JSCs is subject to less stringent regulation. In addition, private JSCs may disapply rules or establish different rules in their charters regarding the acquisition of controlling stakes, and squeeze-out and sell-out procedures.
ii New transparency rules for JSCs

Further to the Corporate Governance Law, the Parliament adopted the Law on Business Simplification\(^\text{14}\) on 16 November 2017, aimed at reloading the Ukrainian stock market, mainly through clearing it of quasi-public JSCs and aligning the requirements regarding public JSCs to the EU regulations.

According to the Law on Business Simplification, all JSCs in Ukraine are considered to be private JSCs as of 6 January 2018, except for public JSCs whose shares are listed at a stock exchange or that make a public announcement that they shall remain public.

Public JSCs are now required to be more transparent by, inter alia, disclosing more extensive information, maintaining a supervisory board with independent members (the new requirements on such independence were introduced), and establishing supervisory board committees on appointments, remuneration and audit. On the other hand, wholly owned private JSCs are exempt from disclosure requirements, while other private JSCs shall disclose less information in comparison to public JSCs. Moreover, private JSCs may choose whether to elect independent members to their supervisory board or establish supervisory board committees, or both.

Public JSCs and banks had to align their charters and by-laws with the Law on Business Simplification by 1 January 2019, while other JSCs shall make the respective changes by 1 January 2020, unless a JSC’s charter is amended earlier.

The Law on Business Simplification also improves corporate governance in JSCs by, inter alia, prohibiting general shareholders’ meetings from deciding any matter about a company’s activities falling under the exclusive competence of the supervisory board by virtue of law or a JSC’s charter. This rule may be disapplied in a private JSC. The new corporate governance rules are expected to provide foreign investors with more comfort when investing into Ukraine.

The Law on Business Simplification also introduces the possibility for legal entities to provide disclosure-of-information services on behalf of stock market participants, including JSCs, disseminate information on financial instruments and stock market participants, and submit reports or administrative information, or both, to the Securities Commission. Legal entities wishing to provide these services need an authorisation from the Securities Commission that enables them to provide these services from 1 January 2019.

The Law also implements the major requirements of the EU Prospectus Directive\(^\text{15}\) into Ukrainian law.

iii Introduction of corporate agreements into Ukrainian law

Another recent development in corporate law is that concluding corporate agreements among the shareholders of JSCs and participants in LLCs is now expressly permitted by the Corporate Agreements Law\(^\text{16}\) and the Law on LLCs, respectively. The Laws allow participants


\(^{15}\) Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC.

(founders) in LLCs and shareholders of JSCs to conclude corporate (shareholders’) agreements. Corporate agreements may establish, inter alia, an obligation for parties to vote at general meetings in the manner determined by such agreement, to approve the acquisition or disposal of participatory interests or shares in a company according to the pre-determined price, and to undertake other actions related to a company’s management. Parties may include in corporate agreements transfer instruments common in other jurisdictions such as tag-along rights, drag-along rights, call options and put options.

While information on the content of a corporate agreement is confidential under both Laws, the JSC Law requires a party to a corporate agreement to notify a JSC on the conclusion of the corporate agreement within three business days of its conclusion, and in the case of a shareholder acquiring voting rights attached to more than 10, 25, 50 or 75 per cent of shares under a corporate agreement. A public JSC must also publicly disclose information on concluding a corporate agreement. If a shareholder concludes an agreement in breach of the terms of a corporate agreement, such agreement will be null and void if a third party knew or ought to know about such breach.

In addition, the creditors of a company shall have the right to conclude a corporate agreement with the participants and shareholders of such companies. The Laws also provide for a possibility to issue an irrevocable power of attorney to ensure the fulfilment of the obligations of participants and shareholders.

The express permission and regulation of corporate agreements is important for Ukrainian M&A deals. The use of this instrument by market participants will greatly depend on subsequent court practice.

iv Increased investor protection rules

The Investor Protection Law,17 which came into effect on 1 May 2016, introduced important developments, inter alia, as to the liability of corporate officers of companies and the ability of minority shareholders to bring a lawsuit against a corporate officer on behalf of a company. According to the Investor Protection Law, corporate officers are responsible for damage they cause to the company through their actions. Such damage will be compensated if incurred through:

- actions committed by officers in excess of their authority or through an abuse of their powers;
- actions committed by officers in violation of the procedure of their prior approval or other decision-making procedures as established by the constituent instruments of a company;
- actions committed by officers in line with the procedure of their prior approval or other decision-making procedure where such officer has filed false information to obtain such approval or decision;
- omissions of a corporate officer when he or she was obliged to take certain actions in accordance with his or her duties; and
- other abusive actions of corporate officers.

Before these changes, the liability of corporate officers was limited in most cases by the amount of their monthly salary.

Moreover, the notion of a derivative action has been introduced into Ukrainian law. A minority shareholder (participant) holding at least 10 per cent of all shares (participatory interests) in a company may file a claim with a commercial court on behalf of a company against a corporate officer for recovery from damage caused by such corporate officer to a company. The derivative action may be brought against individuals falling under the definition of a corporate officer. For JSCs, the corporate officers are the head and the members of the supervisory board, executive body, audit commission and auditor of a JSC, and the head and members of other bodies if the creation of such body is envisaged by a company’s charter. In LLCs, the members of the executive body, the supervisory board and any other individuals occupying a post named in the company’s charter are considered to be the corporate officers. If a derivative action was brought against a corporate officer, he or she may neither represent the company in the proceedings nor appoint a representative to participate in the proceedings on behalf of the company.

**v Simplified M&A for banks**

Starting from 29 April 2017 and running until 1 August 2020, banks in Ukraine may benefit from a simplified procedure for their capitalisation and reorganisation according to the Simplified Bank Reorganisation Law. Under the Law, banks may either use the simplified procedure to merge with another bank or withdraw a banking licence without liquidating the company. The second option will enable banks to exit the banking market and continue their operation in the financial or other sector.

The duration of capitalisation and reorganisation procedures was shortened by way of accelerated terms for regulatory and corporate approvals, as well as a reduction in the paperwork to be submitted to the regulators: the National Bank of Ukraine, the Antimonopoly Committee, the State Fiscal Service and the Securities Commission. The Simplified Bank Reorganisation Law also disapplies the list of rules in cases of the capitalisation and reorganisation of banks under simplified procedures, such as:

- the requirements to notify all creditors of decisions of the general assembly on mergers;
- the satisfaction of creditors’ claims;
- the obligatory purchase of shares upon the request of participants in banks participating in a merger; and
- determining the market price.

**vi The new Law on LLCs**

The new Law on LLCs, which became effective on 17 June 2018, fundamentally changed the regulation of LLCs. The previous regulation of LLCs was very restrictive, and mandatory provisions left little room for participants to adjust the rules on LLC operation to their business needs. The Law on LLCs provides participants with wide discretion in establishing the rules on LLC corporate governance and transfers of participatory interests.

The Law on LLCs expressly permits the establishment of a supervisory board for the purpose of controlling and supervising the management of an LLC. This change means that LLCs are now able to follow the two-tier corporate governance model, which has historically

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been widely used in JSCs in Ukraine. Moreover, LLC participants may appoint independent members to the supervisory board and determine requirements for such independence. The establishment of an audit commission is no longer required.

The Law introduces a number of changes to the rules on conducting general participants’ meetings, including the following developments:

a new majority vote requirements instead of quorum: the decisions of participants may be adopted by a unanimous vote of all LLC participants, by three-quarters of all LLC participants or by a simple majority of all LLC participants;

b limitations to decisions, which can be adopted by written polling;

c the ability to conduct meetings via video conference, provided all participants have the ability to see and hear all other participants;

d the introduction of absentee voting (i.e., the ability of an LLC participant to take part in a meeting by providing his or her written decisions on the matters on the meeting’s agenda; and

e simplified rules for conducting meetings where the LLC is wholly owned. In this case, the sole LLC participant prepares a written decision without complying with the rules on holding the meeting.

The Law on LLCs also establishes new duties and obligations of corporate officers, namely duties to declare a conflict of interest and of confidentiality, and non-compete obligations. Breaching any of these obligations is a ground to terminate a corporate officer without payment of compensation. In addition to the duties of a corporate officer, the executive body members will also be responsible for monitoring the LLC’s net assets, while the LLC’s obligation to maintain positive net assets no longer exists.

The Law on LLCs provides participants with discretion in establishing the rules for transfers of participatory interests, including the ability to:

a modify or disapply the preemptive right of participants;

b restrict the disposal of a participatory interest;

c improve the procedure for the exit and expulsion of participants; and

d introduce an anti-dilution mechanism in an LLC’s charter.

The Law on LLCs has also introduced the notion of significant and interested-party transactions to the regulation of LLCs. LLC participants may modify the default rules on significant transactions in a company’s charter, while the rules on interested party transactions will not apply to an LLC unless such mechanism is expressly established by a company’s charter.

Other important changes introduced by the Law on LLCs include:

a the abolishment of the anti-chaining rule;

b the abolishment of restrictions on the number of LLC participants;

c new restrictions on dividend payments;

d the abolishment of the prohibition on debt-for-equity swaps; and

e changes to the charter capital increase procedure.
vii Other changes

Another development in foreign investment regulation in Ukraine is the adoption of the Law on Attraction of Foreign Investments.\(^{19}\) The Law simplifies the procedure of acquiring and storing securities (including shares of JSCs) by foreign investors by providing an alternative to opening a securities account in Ukrainian depository institutions. Foreign investors may use the services of a global custodian (a nominal holder) who shall, in turn, open a nominal holder securities account with a Ukrainian depository institution and disclose information on the foreign investor for financial monitoring purposes.

Among other positive developments in corporate M&A regulation aimed at facilitating the conducting of business in Ukraine by both local and foreign investors are the cancellation of the registration of foreign investments in Ukraine, which was previously required for the application of guarantees under Ukrainian law, the final abolishment of the requirement for a legal entity to use a corporate seal and improvements in corporate governance in state-owned companies.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

According to the information provided by the Ministry of Foreign Affairs,\(^ {20}\) in 2018 foreign investments into the Ukrainian economy came mainly from Cyprus, the Netherlands, the United Kingdom, Germany, Austria, the British Virgin Islands and Switzerland.

Since Cyprus and the Netherlands are popular jurisdictions for setting up holding companies for large Ukrainian groups, investments coming from these countries are most likely to see the return of Ukrainian capital that flowed out of the country at the outset of the crisis in 2014. This is a good sign, proving that Ukrainian investors believe that the economy is past the worst of the downturn. This positive trend has also become possible because of the gradual relaxation by the National Bank of Ukraine of certain capital control and foreign currency restrictions relating to the repatriation of dividends, repayment of cross-border loans, and import and export transactions involving foreign currency.

As for outbound investment, Ukrainian companies that are leaders in their respective industries are currently looking at possible acquisition targets abroad, in particular within the EU and in Gulf countries.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

The hottest industries in 2018 and to date in 2019 have been the metal and mining, agricultural, consumer goods and retail and real estate sectors.

The highest value M&A deal of 2018 was the US$714 million acquisition of the assets of Donetsksteel, which is the largest coking coal extraction and production business in Ukraine, by Industrial Coal Holding LLC.

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There have been a number of major M&A developments in the agricultural sector involving land banks, processing and infrastructure facilities. The most significant transactions were the previously mentioned acquisition of Mria Agroholding by SALIC UK Ltd and the acquisition by MHP SE, of Perunovina Ptuj.

The highest-value transaction in the consumer goods and retail industry was the increase of the stake of Ukrainian investment company ICU in Burger King Russia of up to 35 per cent. The landmark transaction in this sector was the previously mentioned merger of Rozetka and EVO.

Dragon Capital Investments Limited, a Ukrainian private equity fund, has been actively acquiring assets in Ukraine. In 2018, it acquired 160,000m² of prime office space, as well as the Aladdin Retail Complex from Meyer Bergman, a British investment fund. The highest-value deal in 2018 in real estate was the sale of Renaissance Business Centre (17,100m²) by Alfa Bank.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Financial institutions such as the European Bank of Reconstruction and Development, the International Finance Corporation and the Overseas Private Investment Corporation have been actively investing into Ukraine-focused private equity funds.

Other than international financial institutions investing in private equity funds, no foreign commercial banks have been financing acquisitions in Ukraine: current risks would make the cost of acquisition financing impermissibly high. Furthermore, no bank would lend money over the long term. For example, since 2014, the Ukrainian hryvnia has lost more than 60 per cent of its value. This sharp depreciation has significantly inflated all foreign currency-denominated loans. Accordingly, most M&A deals are financed by acquirers from their own funds. In those cases where big multinational companies with access to cheap financing abroad acquire a company in Ukraine, they may use foreign financing to refinance expensive Ukrainian debt upon completion. This financing is not available to most Ukrainian investors.

VII EMPLOYMENT LAW

The Labour Code of Ukraine, dated 10 December 1971, remains the principal legislative act governing employment relationships in Ukraine. Due to numerous amendments to the Labour Code in the recent years, the document is generally adequate for current business needs. For this reason, developments in employment legislation are not usually seen as the hottest topic in an M&A context in Ukraine.

On 27 September 2017, a law simplifying the procedure for obtaining work permits and temporary residence permits for foreigners came into effect.¹ The law facilitates the engagement of foreign managers and skilled employees serving Ukrainian companies by establishing clear, transparent and foreigner-friendly work permit and temporary residence permit procedures. The adopted law contains a number of novelties. In particular:

a  it extends the list of grounds to apply for a temporary residence permit;

b  it permits parallel employment of a foreign employee by two or more Ukrainian companies;

it simplifies the procedure for obtaining a work permit by reducing the number of documents to be submitted to the state authorities;

- it extends the term of a work permit from one to three years for certain categories of foreign employees, including highly paid foreign professionals, founders and beneficial owners of Ukrainian companies, and IT professionals;

- it establishes an affordable minimum salary that must be paid to certain categories of foreign employees; and

- it establishes a possibility for an employer to amend a work permit in certain cases instead of applying for an entirely new one.

Since 1 June 2018, temporary residence permits are issued in the form of a card with a contactless electronic chip. Because the chip contains certain biometric data (the digitalised signature, photograph and fingerprints of a foreign national), which are obtained at the time of filing the application, the foreign national is required to file an application for a temporary residence permit in person. A temporary residency permit for a foreign employee will be issued for the term of the relevant work permit (i.e., for up to three years) and must be exchanged after it expires (previously, a temporary residency permit could be extended).

In recent years, the minimum monthly salary has been increased significantly, from 1,600 hryvnias in December 2016 to 4,173 hryvnias in January 2019. This change may affect the purchase price of target companies with a significant amount of low-paid employees, especially in the agricultural and manufacturing sectors.

A new Labour Code of Ukraine has been developed and prepared for a second reading in Parliament. It is expected to make Ukrainian labour law more investor-friendly, but does not contain any game-changing provisions, thus ensuring predictability for businesses with respect to labour relations and obligations toward employees in the future.

VIII TAX LAW

The Tax Code of Ukraine, dated 2 December 2010, as amended, remains a comprehensive legal act regulating tax matters in Ukraine. There have been no significant changes to the Tax Code in recent years that are relevant to M&A transactions.

Ukraine has the double tax treaty network with around 70 jurisdictions, with treaties with Luxembourg, Malta and Qatar being the most recent. While historically Luxembourg, and, in certain cases, Malta were used in multilayer group structures, ratification of these double tax treaties has a positive effect on the structuring of M&A deals in Ukraine.

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The Ministry of Finance has also started to gradually review the existing tax treaty network, specifically targeting those offering full exemptions from withholding tax (WHT). This issue should be taken into account while structuring M&A deals.

Among the most significant developments, mention should be made of the Ministry:

- signing a protocol amending the Ukraine–Netherlands double tax treaty with the domestic ratification procedures still in progress;
- signing a protocol amending the Ukraine–UK double tax treaty with the domestic ratification procedures still in progress;
- signing a protocol amending the Ukraine–Switzerland double tax treaty with the domestic ratification procedures still in progress; and
- signing a protocol amending the Ukraine–Cyprus double tax treaty with the domestic ratification procedures still in progress.

Ukraine has also recently signed and ratified the Multilateral Convention to Implement Tax-Treaty-Related Measures to Prevent Base Erosion and Profit Shifting (MLI). The application of the MLI is aimed at combating abuse of bilateral tax treaties in a synchronised and efficient way by amending about 40 of Ukraine’s treaties. Among other novelties, it introduces the principal purpose test concept, requiring companies seeking treaty benefits to substantiate the commercial rationale behind relevant structures and transactions. The MLI also broadens the definition of permanent establishment, expanding the profits base taxable in Ukraine. Ukrainian and foreign entities operating in Ukraine should reassess their current corporate structures to be in compliance with the new rules.

On a separate note, some of Ukraine’s tax treaties currently extend the taxing authority of Ukraine to capital gains derived from the direct or indirect disposal of shares deriving their value directly or indirectly from immovable property located in Ukraine. These provisions have not been transposed into Ukrainian legislation yet. Thus, Ukraine does not levy WHT on such capital gains. However, the Ministry of Finance considers a fundamental redevelopment of the tax rules landscape in Ukraine, including, inter alia, a legislative initiative aimed at the introduction of the above provisions into Ukrainian legislation. If such provisions were to be adopted, capital gains realised on the disposal of shares deriving their value from Ukrainian real estate would generally be subject to WHT at a rate of 15 per cent in Ukraine.

Ukraine has also committed to implement the de-offshorisation package, which will affect the corporate aspects of structuring Ukrainian M&A transactions. More specifically, in April 2016, the President established a working group with a view to transposing anti-BEPS measures into Ukrainian legislation. While the draft law on the implementation of the anti-BEPS measures (e.g., controlled foreign company rules, enhanced transfer pricing rules) has been developed, to date it has not been adopted in Ukraine.

Additionally, in November 2016, Ukraine became a member of the Inclusive Framework on the OECD/G20 base erosion and profit shifting (BEPS) project, thus committing to implement four minimum standards of the BEPS package:

- Action 5 (countering harmful tax practices);
- Action 6 (prevention of treaty abuse);
- Action 13 (implementation of country-by-country reporting); and
- Action 14 (enhancing dispute resolution mechanisms).

It is worth mentioning that recently, Ukraine reformed its currency control legislation with an aim to harmonise the Ukrainian rules on the movement of capital with the EU standards (the
undertaking prescribed in the EU–Ukraine Association Agreement). This step has liberalised and significantly changed the Ukrainian currency control rules. Lifting some of the existing currency control restrictions is still conditioned on the implementation of various anti-BEPS measures (e.g., controlled foreign company rules, new rules on the taxation of permanent establishments, enhanced transfer pricing rules) and mechanisms for the automatic exchange of information.

IX COMPETITION LAW

Although the economic crisis has slowed M&A activity, the Antimonopoly Committee of Ukraine (AMCU) has demonstrated its strong desire to adjust the merger control rules in line with the best practices of other European countries. As a result, a number of significant and long-awaited reforms to competition law have taken place during the past few years. Following the recommendations of the OECD and the United Nations Conference on Trade and Development, in January 2016 the Parliament amended the rules on merger control.24 The changes increased the merger notification thresholds that had been in effect for over 15 years. In particular, since May 2016, transactions are subject to prior approval of the AMCU if:

- the parties’ combined worldwide turnover or assets exceeds the hryvnia equivalent of €30 million, and the domestic turnover or assets of either of the two parties exceeds the hryvnia equivalent of €4 million;
- the target’s domestic assets or turnover exceeds the hryvnia equivalent of €8 million, and the buyer’s worldwide turnover exceeds the hryvnia equivalent of €150 million; or
- in the case of the establishment of a business entity, the domestic assets or turnover of one of the parties exceeds the hryvnia equivalent of €8 million, and the worldwide turnover of the other party exceeds the hryvnia equivalent of €150 million.

All thresholds are to be calculated on a group level for the last financial year preceding the contemplated transaction.

In addition to amending the rules on merger control, the merger control procedures have been simplified by allowing parties to conduct preliminary consultations with the AMCU. Furthermore, the new merger control procedures have significantly simplified the disclosure requirements for parties during the course of filing preparation, but at the same time they require profound economic analysis for transactions that may impact competition in Ukraine. A further sign of liberalisation has been the introduction of a fast-track procedure for certain cases, with decisions to be issued within 25 calendar days instead of 45 calendar days.

As part of the reform in the antitrust sphere, the AMCU’s transparency has been enhanced. Previously, AMCU decisions did not have to be published; however, a law adopted in November 2015 requires the publication of all decisions on the AMCU’s official website within 10 working days from the adoption of a decision.25

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In September 2015, the AMCU approved fining guidelines that make its process of calculating fines more predictable and transparent.26

In November 2017, the Parliament adopted changes to the Ukrainian competition and sanctions laws that allow the AMCU to deny merger clearance of transactions involving entities included in the sanctions list.

Another step towards the alignment of the Ukrainian competition legislation to the EU competition legislation was the AMCU’s approval of the Guidelines on the Assessment of Horizontal Mergers at the end of December 2016 and the Guidelines on the Assessment of Non-Horizontal Mergers in March 2018.

In November 2018, the AMCU adopted the new Guidelines on Definition of Control, which were developed around a concept of control similar to that of the EU competition legislation.

The completed reforms represent a broader effort to harmonise Ukrainian competition law with that of the EU, and generally make Ukraine a more business friendly place. In addition to these initiatives, a number of legal changes are making their way through the legislative process. Several are responses to recommendations cited in reviews carried out by the OECD and the United Nations Conference on Trade and Development. These legislative proposals address, for example, a revision of the concerted actions regulation, the AMCU’s increased discretion in determining which cases to investigate and the establishment of a specialised court chamber for hearing antitrust-related disputes.

X OUTLOOK

The Ukrainian M&A market is certainly showing signs of recovery, and we expect positive developments in future years. While the majority of purchasers on the M&A market are domestic investors, foreign investors are once again showing interest in the Ukrainian M&A market and considering Ukraine as a prospective investment opportunity.

26 Recommendation No. 16-pp approved by the Antimonopoly Committee of Ukraine on 15 September 2015.
I  OVERVIEW OF M&A ACTIVITY

Despite a relatively strong start to the year, M&A activity appears to be facing strong headwinds in 2019. Geopolitical and regulatory developments appear to have encouraged both purchasers and sellers to delay or reconsider the particular value proposition that a deal presents. With the advent of ever-increasing regulation (including in the UAE), M&A transactions are becoming more complex to structure and to implement, and consequently have also become significantly more expensive.

In the UAE, headline M&A transactions continue to be driven by government-owned or controlled businesses, in particular the banking and finance industry. Of note, the much-rumoured three-way merger between Abu Dhabi Commercial Bank, Union National Bank and Al Hilal Bank was completed in the second quarter of 2019. The merged entity has an asset base exceeding 420 billion dirhams and is the third-largest lender in the UAE. The merger follows a trend of consolidation in the banking sector and represents the desire of the UAE authorities to see consolidation in sectors where cost-saving synergies can be made. On a similar note, media reports suggest that Dubai Islamic Bank and Noor Bank are currently engaged in merger talks. Talks are said to be ongoing and it is not yet certain whether a deal will materialise.

II  GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The UAE is a federation of seven emirates that was formed on 2 December 1971 by Abu Dhabi, Ajman, Dubai, Fujairah, Sharjah and Umm Al Qaiwain following the end of the British protectorate over the ‘Trucial States’. The Emirate of Ras Al Khaimah joined the federation the following year.

The currency is the UAE dirham. The exchange rate is pegged at approximately 3.67 dirhams per US dollar since 1997. There are no currency import or export controls.

The UAE Federal Constitution apportions powers between the federal government (based in Abu Dhabi) and the governments of the constituent emirates. Some fields are regulated only at the federal level (e.g., immigration and labour relations) although local interpretations and practices sometimes differ from one emirate to another. Other matters are regulated only at the emirate level (e.g., each emirate retains sovereignty over its own natural resources, including its crude oil and natural gas reserves). Still other matters are regulated at both the emirate and federal levels (e.g., company formation and registration).
Any business operating in the UAE must hold a licence authorising its business activity in the UAE. These licences are issued by the concerned authorities in each emirate. A licence allows the licensed entity to carry on the business it is licensed to conduct within the emirate that issues the licence from the business premises identified in the licence. For example, a Dubai business licence authorises the conduct of business in the Emirate of Dubai. If the licence holder wishes to conduct business in the Emirate of Abu Dhabi (for example), then it must apply for and obtain a business licence in Abu Dhabi.

In addition to the licensing rules that are imposed in each emirate, there is a separate layer of federal regulation that a business must comply with. Business licences are available to foreign and local businesses, although there are restrictions that vary from emirate to emirate on the types of business activities that are available to foreign businesses and to local businesses with partial foreign ownership. A foreign business is required to appoint a UAE national shareholder as part of its application for a licence. Companies that are incorporated in the UAE (outside a free zone) must be at least majority-owned (51 per cent) by a UAE national or wholly Gulf Cooperation Council (GCC)-owned. Companies established in any of the UAE’s many free zones may be wholly foreign-owned. No corporate or personal income tax is currently imposed anywhere in the UAE, except for the income taxes that are paid by foreign banks and foreign petroleum companies.

A business that wishes to operate in a free zone must obtain a licence from the authority for that free zone. The resulting licence authorises the conduct of the licensed activity within the geographical limits of the free zone. For example, a company licensed to trade certain goods in the free zone can import its goods into the free zone and re-export to destinations outside the free zone (and the wider UAE). However, the free zone licence does not authorise it to engage in any of these commercial activities in the UAE (outside the geographical limits of the free zone). No local ownership requirements are imposed in the free zones. An additional feature of most of the free zones is that they are not part of the customs territory of the UAE. The import of goods into a free zone from overseas does not attract customs duty. Instead, customs duty (5 per cent on most items) is paid when goods move from the free zone into the UAE proper. The free zones also observe a simplified process for hiring personnel. Shares in onshore and free zone entities can be freely transferred, but it is important to note that any transfers are subject to approval by the relevant authority of the incoming shareholder.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

The government has recently introduced changes to the foreign ownership requirements under UAE law for companies that are registered outside a free zone.

Federal Decree-Law 19 of 2018 (FDI Law) was issued on 23 September 2018. The FDI Law adopts a similar approach to majority foreign ownership as the UAE Commercial Companies Law.² An amendment to Article 10 of the UAE Commercial Companies Law adopted in September 2017 (pursuant to Federal Decree-Law 18 of 2017) stipulated that the Federal Cabinet may adopt resolutions permitting foreign nationals to hold in excess of 49 per cent of the share capital of UAE companies. The Federal Cabinet remains responsible for making key decisions with respect to the administration of the FDI Law. In addition to the Federal Cabinet, the Foreign Direct Investment Committee (to be presided over by the

² UAE Commercial Companies Law (Federal Law 2 of 2015, as amended).
Ministry of Economy and appointed by the Federal Cabinet) has been made responsible for reviewing and making recommendations to the Federal Cabinet in respect of matters concerning foreign direct investment. Any recommendations made by the Foreign Direct Investment Committee shall continue to be subject to the approval of the Federal Cabinet. The FDI Law contains a negative list of 13 sectors that will not be subject to the proposed relaxation of the current foreign ownership restrictions. These sectors are the following:

- exploration and production of petroleum products;
- investigations, security, military sectors and manufacturing of weapons, explosives as well as military hardware, equipment and clothing;
- banking and financial activities and payment and cash handling systems;
- insurance services;
- hajj and umrah services\(^3\) and labour supply and recruitment services;
- water and electricity services;
- services related to fisheries;
- postal, communication and audiovisual services;
- land and air transport services;
- printing and publishing services;
- commercial agents services;
- retail medicine (such as private pharmacies); and
- poison centres, blood banks and quarantines.

The Federal Cabinet is empowered to add to or remove activities from the foregoing list. The FDI Law stipulates that the Federal Cabinet shall, in consultation with the Foreign Direct Investment Committee, propose a positive list of sectors in which foreign nationals shall be permitted an ownership interest of up to 100 per cent. On 2 July 2019, the Prime Minister issued a statement announcing the Federal Cabinet’s approval of this positive list of 122 economic activities in sectors such as agriculture, manufacturing, renewable energy, electronic commerce, transportation, arts, construction and entertainment. The list of 122 economic activities is divided into 51 industrial activities, 52 service activities and 19 agricultural activities. While allowing up to 100 per cent foreign ownership, the positive list does not do this unconditionally. On the contrary, the list imposes additional requirements such as minimum capital requirements on some activities, obligations to employ advanced technology on other activities and requirements to contribute to the emiratisation of the workforce on others. For many business and service activities, existing restrictions and qualifications are expressly retained. Despite these requirements, this relaxation of the foreign ownership restrictions could act as trigger for a fresh wave of inbound M&A activity into, and also assist in the development of homegrown businesses in, the UAE. It is expected that the licensing authorities in each emirate will ultimately determine the permitted foreign ownership percentages for specific projects.

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\(^3\) Hajj and umrah are forms of pilgrimage that Muslims undertake and that comprise visits to Mecca in the Kingdom of Saudi Arabia. While Hajj is considered obligatory to perform at least once in a lifetime of an adult and physically able Muslim, and must be performed at a prescribed time every year, Umrah is optional and can be performed at any time of the year.
IV FOREIGN INvolvEMENT IN M&A TRANSACTIONS

Despite recent headwinds, the year in review witnessed substantial M&A activity, with many transactions concerning foreign involvement. Reports indicate that 77 cross-border deals worth US$14.21 billion were completed in 2018 in the Middle East and North Africa region, making it the year with the highest volume of inbound M&A. Deals in the UAE more than doubled in 2018 to US$10.4 billion, with the energy sector being a key sector of interest for foreign acquirers. As noted above, substantial M&A activity (including transactions involving a foreign party) continues to be driven by businesses and sectors with significant government involvement or investment. Examples include the oil and gas and banking sectors.

In April 2019, it was announced that Emirates NBD (a commercial bank majority-owned by the government of Dubai) would be acquiring Denizbank for US$2.8 billion with combined assets of about US$180 billion. Denizbank is the fifth-largest bank in Turkey. Due to the depreciation of the Turkish lira and in light of the ongoing political and economic uncertainty in Turkey, the deal was ultimately revised and completed at a 20 per cent discount to a previously agreed price of US$3.2 billion.4

In the oil and gas sector, Italy’s Eni and Austria’s OMV have agreed to pay a combined US$5.8 billion to buy a stake in Abu Dhabi National Oil Company’s (ADNOC) refining business and establish a new trading operation owned jointly by all three. Eni and OMV will acquire 20 and 15 per cent shares in ADNOC Refining.5 Similarly, KKR and BlackRock are reported to have formed a consortium to hold a 40 per cent stake in a new entity known as ADNOC Oil Pipelines, with ADNOC owning the remainder. The deal has been reported to have been completed at a value of US$4 billion.6

In March 2019, the much-anticipated deal between Uber Technologies Inc and Careem Networks FZ-LLC (Uber’s key competitor in the Middle East) was announced. This transaction is discussed further in Section V.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

As discussed further in Section VIII, the UAE, Saudi Arabia and Bahrain have introduced VAT to their respective local markets. In a first (at least for the UAE), vendors and purchasers must consider, seek advice on and address tax matters in their transaction documentation. Furthermore, the advent of VAT will no doubt put pressure on the cashflows of many small and medium-sized businesses, and it remains to be seen whether this will in turn have an effect on distressed M&A activity.

Furthermore, we have seen the Federal Ministry of Economy (the regulator in charge of administering the competition regime) become active in accepting and reviewing merger control notifications filed in connection with UAE transactions. Although still a developing area of law, the very fact that merger control notifications are now being submitted and reviewed indicates that the relevant authorities are serious about ensuring that those who are party to transactions concerning the UAE market consider and, where required, notify their

transactions. It is also of note that the lack of publicly available decisions concerning such notifications creates a degree of uncertainty for transactions that are caught by the relevant filing requirements.

In terms of key trends and active industries, we continue to see transactions take place in the financial services sector, with the ongoing consolidation in the banking industry continuing to be a driver of M&A activity. The insurance industry also remains an industry of interest insofar as M&A transactions are concerned, with consolidation being a continuing trend.

In the technology sector, a number of UAE free zones (in particular the Dubai International Financial Centre (DIFC) in the Emirate of Dubai and the Abu Dhabi Global Market (ADGM) have made an effort to attract, support and grow technology-related business. The government of Dubai has also launched the Dubai future accelerators programme aimed at encourage young entrepreneurs to address the challenges we are currently facing. Similarly, the DIFC has introduced a fintech accelerator programme aimed at providing startups access to leading accelerator programmes and mentorship from leading financial institutions and insurance partners, along with a dedicated space to work alongside a community of like-minded individuals. In Abu Dhabi, the ADGM has introduced a licensing regime specifically catered towards tech startups that allows entrepreneurs to obtain an operational licence in the ADGM and that gives them access to a professional services support programme aimed at allowing entrepreneurs’ entry to a community of businesses, financial services and professional advisers. Given these developments and the stated aim of the UAE government to encourage and support hi-tech businesses and startups, technology businesses will likely also continue to be a source of M&A activity in the UAE.

A transaction of note in the technology sector was the acquisition by Uber Technologies Inc of Careem Inc, with the result that Careem will (upon completion of the acquisition) operate as a wholly owned subsidiary of Uber, while at the same time maintaining its own brand and independent operations. The acquisition is reported to have been agreed for a price of US$3.1 billion, consisting of US$1.7 billion in convertible notes and US$1.4 billion in cash. Similarly, in May 2018, Dubai-based The Entertainer (a lifestyle and coupon application based in the UAE but operating across the Middle East, Europe, Asia and Africa) reported that GHF Financial Group, a Bahrain-based investment bank listed on the Dubai financial market, had acquired an 85 per cent stake in The Entertainer. Media reports suggest that the investment was agreed at a price of at least US$100 (although further details were not disclosed).

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

External financing for acquisitions continues to be less prevalent in the UAE in comparison to other jurisdictions, and a large majority of acquisitions continue to be financed in cash.

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10 https://www.uber.com/newsroom/uber-careem/.
Where acquisition financing is made available on a transaction, it is usually structured as a long-term loan, which is almost always secured by personal or corporate guarantees, including securities over target assets. In addition to the primary facility documentation, borrowers may also issue a promissory note, a subordination agreement for any remaining debt and an assignment of certain identified assets depending on the nature of the acquisition.

Although most acquisitions that are financed are funded through conventional finance, various other Islamic finance structures are used as well, particularly the *murabahah*, 12 *musharakah*, 13 *mudarabah* 14 and *ijarah* 15 structures. However, note that the financial covenants of these Islamic structures are often more onerous than those found in conventional facilities.

In terms of the availability of private equity investment, the private equity market continues to feel the effects of global financial uncertainty, including the US and European sovereign debt crises. Regionally, the UAE continues to lead the market in terms of volume and value, partly due to the stability and availability of investable companies. However, gaps are still visible between company valuations and investors’ expectations for returns, which hinder activity. A move away from traditional sectors such as oil and gas was witnessed in 2017, with an uptrend into consumer-driven sectors such as education, retail, food and beverages and healthcare, where added-value opportunities have arisen.

**VII EMPLOYMENT LAW**

The UAE Labour Law 16 regulates most employment relationships in the UAE. The Labour Law imposes minimum standards on termination of employment, working hours, annual leave and safety standards, among other things, which cannot be contracted out of. In addition to the Labour Law, certain UAE free zones have implemented their own employment regulations, which apply to all companies licensed to operate in that free zone. In general, these employment regulations act as a supplement to the Labour Law, with the exception of the Dubai International Financial Centre free zone, where DIFC Law No. 4 of 2005 applies, and the Abu Dhabi Global Market, where the ADGM Employment Regulations 2015 apply.

On the sale of a business, there is nothing in the UAE that is akin to the Transfer of Undertakings (Protection of Employment) Regulations 2006 of the United Kingdom. Consequently, for employees to be transferred to a purchasing entity, the employees’ employment contracts with the selling entity must be terminated and new employment contracts entered into with the purchasing entity.

On the termination of employment, transferring employees must be paid their share of service gratuity in accordance with the Labour Law, their salary for any accrued but unused annual leave, and any other entitlements as set out in their employment contracts.

End-of-service gratuity payments must be paid to any employee who completes one year or more in continuous service. If an employer has terminated his or her employment

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12 A shariah-compliant form of financing that involves a sale contract in which the seller includes a profit margin in the sale price along with the actual cost of the subject matter of the contract.

13 A shariah-compliant joint venture or partnership.

14 A shariah-compliant form of financing in which two or more investors collaborate and pool their capital and appoint an agent to manage their investment in return for the payment of a fee.

15 A shariah-compliant lease, most commonly used to finance the acquisition of assets, for example in the context of a sale and leaseback arrangement.

16 The UAE Labour Law (Federal Law No. 8 of 1980 on Regulating Labour Relations (as amended)).
contract, the gratuity is 21 days’ basic salary for each of the first five years of employment and 30 days’ basic salary for each additional year over five years. The Labour Law caps the end-of-service gratuity to an amount equal to an employee’s basic salary for two years. An employee will also be entitled to a gratuity payment for fractions of the year worked provided that the employee has completed one year in continuous service. The selling entity would therefore be required to make payment of the end-of-service gratuity and all other contractual payments to employees when they are transferred to the purchasing entity. Alternatively, the end-of-service gratuity and all other contractual payments due to employees could be paid by the purchasing entity and then deducted from the consideration payable for the business. However, one practical matter to consider with the latter approach is that the transferring employees will, on termination of their employment with the selling entity, be required to sign an undertaking confirming receipt of all amounts due by the employer. An employee will be reluctant to do so unless this is in fact the case, and it is unlikely that a prospective purchaser will want to make any payments in connection with the transferring employees until after the completion of the transfer of the business.

Transferring employees may also raise concerns about the termination of their current employment contracts and the payment of their end-of-service gratuity as this will result in the end of their period of continuous service, and they will therefore be required to work for the purchasing entity for a year before being entitled to an end-of-service gratuity payment. Generally there is no procedure for the transfer of the continuous service period from one employer to another. However, depending on where within the UAE the employee is employed, it may be possible for a period of continuous service to be acknowledged by the new employer and thereby preserve valuable end-of-service benefits for the employee.

As part of the sale of a business in the UAE and the transfer of employees, the amendment or cancellation and reissuance of UAE residence visas for each transferring employee will also need to be considered. As the number of employees that a company can sponsor for visa purposes is dependent on the space that it leases or owns, a purchasing entity will also need to ensure that it occupies sufficient space to sponsor all transferring employees.

In addition, the applicability of the Pensions Law17 (as amended) will also need to be considered in any transfer of a business in the UAE. The Pensions Law will have implications for any company that employs UAE or GCC nationals.

In a noteworthy development, the DIFC has recently initiated consultations on a proposed reform of the system of end-of-service gratuity payments in respect of employees that work in the DIFC. The DIFC has proposed that the current regime (which consists of a lump sum payment to employees at the termination of their employment relationship, and which is generally unfunded) be replaced with a DIFC employment workplace saving scheme into which DIFC employers contribute on a monthly basis. The proposed saving scheme shall be administered by the DIFC Authority. While the proposal is still at an early stage, the DIFC proposes implementing the new structure for end-of-service benefits by January 2020. As previously noted, changes to DIFC employment law will not have an effect on employers operating outside the DIFC (e.g., in other free zones or onshore in the UAE). It remains to be seen whether the UAE federal government will follow the DIFC in introducing similar reforms.

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17 The Pensions Law (Federal Law No. 7 of 1999 concerning Pensions and Social Securities) (as amended).
The UAE issued a substantive law on value added tax (VAT) in 2017. Pursuant to the VAT Law, the imposition of VAT in the UAE commenced on 1 January 2018 at a rate of 5 per cent.

Registration for VAT is mandatory for any taxable person or business if the total value of its taxable supplies made within the UAE exceeds the mandatory registration threshold of 375,000 dirhams during the previous 12 months, or if it is anticipated that the taxable supplies will exceed the threshold in the next 30 days.

A taxable supply refers to a supply of goods or services made by a business in the UAE that may be taxed at a rate of either 5 or zero per cent. Reversed charge supplies and imports are also taken into consideration for this purpose if a supply of such imported goods and services would be taxable if it were made in the UAE.

Entities that are not based in the UAE but that provide goods or services in the UAE are also required to apply for registration if they meet the threshold requirements.

The supply by a taxpayer of either exempt or zero-rated goods or services will not attract VAT; however, a supplier of zero-rated goods or services will be able to claim a refund on any VAT paid on their purchases, unlike a supplier of exempt goods or services who will be unable to recover any VAT paid on their purchases. The VAT Law sets out a list of zero-rated and exempt supplies.

The VAT Law also permits tax grouping, which allows group companies to be treated as one entity for the purposes of VAT. Each group company will be jointly and severally responsible for each other group company’s VAT liabilities, and no VAT will be payable on transactions between entities within the group.

Generally a VAT-registered customer must account for VAT paid in respect of purchases; however, certain transactions between entities within the GCC will be subject to VAT by reverse charge. The concept of reverse-charging VAT allows the simplification of transactions within a single market (i.e., the GCC states). The reverse charge removes the obligation to account for VAT on a sale from a supplier and places it on the customer. It should be noted that for the purposes of a single market VAT treatment, only those countries that have implemented VAT at the relevant time will be taken into account; non-implementing countries would be treated like any foreign country.

Cabinet Decision No. 59 of 2017 specifies all designated zones for the purposes of implementing the designated zone provisions in the VAT Law. A designated zone is required to be a specific fenced area with security measures and customs controls in place to monitor the entry and exit of individuals and the movement of goods to and from the area. Concessional VAT treatment may be available for transactions involving the supply of physical goods within designated zones. No VAT concessions are available for transactions involving the supply of services within designated zones. The Cabinet has the authority to amend the list of designated zones as required.

With respect to the applicability of the VAT Law to M&A transactions, it provides that ‘the transfer of the whole or independent part of a Business from a Person to a Taxable Person for the purposes of continuing the Business that was transferred’ shall not be considered a supply, and therefore will not be subject to VAT. Consequently, in common with some

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18 The VAT Law (Federal Decree Law No. 8 of 2017).
19 Article 7 of Federal Decree Law No. 8 of 2017.
European jurisdictions, the sale and purchase of a business in the UAE should not attract VAT. Note, however, that there is no clear guidance in the law as to what continuing a business involves; nor is there any detail on what constitutes the whole or independent part of a business.

Note also that pursuant to Article 42 of Cabinet Decision No. 52 of 2017, a transfer of title to equity securities is exempt from VAT.

It is noteworthy that in May 2019, the Minister for Justice issued a number of executive resolutions concerning the establishment of the requisite government machinery for the consideration and resolution of tax disputes. This includes the establishment of a specialised tax department in the Abu Dhabi Federal Court of First Instance and one in the Abu Dhabi Federal Court of Appeal. At present, these resolutions are limited to the Emirate of Abu Dhabi; accordingly, it is expected that similar specialised departments will be established in other emirates (the courts of the Emirates of Dubai and Ras al Khaimah are not a part of the UAE federal court system) to consider tax disputes.

IX COMPETITION LAW

The Competition Law\(^{20}\) was introduced into the United Arab Emirates as a means of regulating anticompetitive practices. The Competition Law deals with three key areas: a restriction on anticompetitive agreements, the regulation of dominant market positions and a requirement that acquisitions over a threshold combined market share obtain merger clearance from the UAE Ministry of Economy (Ministry).

Although the Competition Law was introduced in 23 February 2013, it initially had minimal impact as a result of it failing to establish the market share thresholds at which its restrictions became applicable. It also failed to define the small and medium-sized establishments that were stated to be outside the purview of the Law.

In 2016, two new Cabinet decisions were introduced that supplemented the Competition Law and provided guidance on these outstanding aspects: Cabinet Decision No. 13/2016 (Ratios Decision) in respect of market share thresholds and Cabinet Decision No. 22/2016 (SME Decision) in respect of small and medium-sized establishments.

As a result of the Competition Law and the two Cabinet Decisions, merger clearance will be required in advance of any proposed merger, acquisition or other consolidation of two or more entities that would result in a market share of 40 per cent or more. The concerned market is broadly defined in the Competition Law to comprise markets in which commodities or services are replaceable or may be substituted to meet specific needs according to price, properties and use. Although it is difficult to define the relevant market in legislation, and more often than not markets are only identifiable on a case-by-case basis, on a practical level the application of the Ratios Decision is somewhat difficult because the concerned market is not clearly defined.

In addition, as a result of the SME Decision, the Competition Law does not apply to certain small and medium-sized establishments as detailed in the SME Decision. The definition of small and medium-sized establishments varies according to whether the relevant entity operates in the trade, industry or services sector. Small and medium-sized establishments are also identified in the Ratios Decision according to turnover and number of employees.

\(^{20}\) The Competition Law (Federal Law No. 4 of 2012 on the regulation of competition).
Finally, note that the Ministry also has the power to investigate a potential violation of the Competition Law on its own initiative or following a complaint brought before it. Failure to notify a reportable economic concentration may result in a fine of between 2 and 5 per cent of turnover generated by the relevant undertaking in the UAE in the last financial year or, if data is not available, a fine of between 50,000 and 5 million dirhams.

X OUTLOOK

The legal framework for corporate transactions with a UAE element has no doubt changed drastically over the past year. With the advent of the FDI Law, the implementation in earnest of VAT and the proposed introduction of key corporate governance and employment law reforms, those looking to buy, sell or invest in businesses that have a presence in the UAE would be well advised to consider the new regulatory landscape before concluding such transactions.

With more realistic valuations now being seen across the spectrum of M&A activity, potential purchasers may indeed find that deals that were not practicable in the past are now possible (and are potentially also more lucrative). There is therefore cautious optimism that M&A activity will remain buoyant through the next 12 months.
I OVERVIEW OF M&A ACTIVITY

In the UK, 2018 was truly a year of two halves: after the first six months of record-breaking levels of activity, deal-making plummeted by a remarkable 47.6 per cent in H2.2 Nevertheless, thanks to the exceptional start to the year, the total value of UK M&A activity in 2018 still reached £182.6 billion, the highest annual value since 2015. Of this figure, £119.9 billion was recorded in H1.

There were 1,560 recorded deals in 2018. The largest of these was Comcast Corporation’s high profile takeover of Sky plc, which, after months of dramatic negotiations, ultimately resulted in a deal valued at over €42 billion. Other high-value deals included GlaxoSmithKline’s acquisition of the remaining 36.5 per cent stake in its consumer healthcare joint venture with Novartis for €10.5 billion – the largest deal in the rapidly growing pharmaceutical, medical and biotech sector – and Melrose’s hostile takeover of GKN for €9.8 billion.3 One of the most notable deals in the second half of 2018 was the shake up in the European telecoms sector as a result of Vodafone’s £16 billion acquisition of Liberty Global’s operations in Germany, the Czech Republic, Hungary and Romania, Vodafone’s largest acquisition for almost two decades.4

The value of inward M&A, which was driven by US investment, increased from £35.2 billion in 2017 to £71.1 billion in 2018, largely due to the number of high profile deals in the first half of the year. By contrast, the value of outward M&A fell from £77.5 billion in 2017 to £22.7 billion in 2018. None of these outward acquisitions were ranked as very high value deals (above £10 billion).5 These trends are consistent with the fall in the value of the pound.

Although public M&A deal volume decreased slightly in 2018 compared with 2017, with 42 firm offers announced for Main Market or Alternative Investment Market (AIM) companies, it was still a driver of much of the deal-making. Indeed, there was a substantial rise in deal value, with an aggregate deal value of £122.1 billion in 2018 in contrast to £45 billion recorded in 2017.6 Schemes of arrangement remained the most popular choice of structure, accounting for 74 per cent of all firm offers announced in 2018.

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1 Mark Zerdin is a partner at Slaughter and May.
2 Mergermarket, ‘Deal Drivers EMEA 2018’.
3 Mergermarket, ‘Deal Drivers EMEA 2018’.
4 Experian Market IQ, ‘United Kingdom and Republic of Ireland M&A Review, H1 2018’
At the time of writing, there is still significant political uncertainty in the United Kingdom, particularly concerning the final stages of negotiations to leave the European Union and the looming threat of a no deal Brexit. This lack of clarity has subdued the market, and dealmakers are likely to remain cautious while this uncertainty persists.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Companies Act 2006 provides the fundamental statutory framework, and with the law of contract forms the legal basis for the purchase and sale of corporate entities. In addition, the City Code on Takeovers and Mergers (Takeover Code) regulates takeovers and mergers of certain companies in the United Kingdom, the Isle of Man and the Channel Islands. The Takeover Code has statutory force and the Takeover Panel (Panel) has statutory powers in respect of transactions to which the Takeover Code applies. Breach of any of the Takeover Code rules that relate to the consideration offered for a target company could lead to the offending party being ordered to compensate any shareholders who have suffered loss as a consequence of a breach. In addition, breach of the content requirements of offer documents and response documents may constitute a criminal offence. The Panel also has the authority to issue rulings compelling parties who are in breach of the requirements of the Takeover Code to comply with its provision, or to remedy the breach. These rulings are enforceable by the court under Section 955(1) of the Companies Act. The Takeover Code has a wider scope than the EU Takeovers Directive, and applies if the offeree (or potential offeree) is a UK public company and, in some instances, if the company is private or dual-listed.

The Financial Services and Markets Act 2000 (FSMA 2000) regulates the financial services industry and makes provision for the official listing of securities, public offers of securities, and the communication of invitations or inducements to engage in securities transactions. Following substantial amendments to the FSMA 2000, brought about on 1 April 2013 when the Financial Services Act 2012 (FS Act) came into force, financial regulation is split between two bodies: the Financial Conduct Authority (FCA), which regulates conduct in the retail and wholesale markets, and the Prudential Regulation Authority, which is responsible for the prudential regulation of banks and other systemically important institutions. As a consequence of the FS Act, more than 1,000 institutions (including banks, building societies, credit unions and insurers) are now dual-regulated. The UK Listing Authority Sourcebook of Rules and Guidance (which includes the Listing Rules, the Prospectus Rules and the Disclosure Guidance and Transparency Rules (DTRs)), promulgated by the FCA in its capacity as the UK Listing Authority (the competent authority for the purposes of Part VI of the FSMA), includes various obligations applicable to business combinations involving listed companies, and contains rules governing prospectuses needed for public offers by both listed and unlisted companies. The Listing Rules, in particular, set out minimum requirements for the admission of securities to listing, the content requirements of listing particulars and ongoing obligations of issuers after admission. The Criminal Justice Act 1993 contains the criminal offence of insider dealing and, from 3 July 2016, the EU Regulation on Market Abuse (MAR) (with the Listing Rules, the DTRs and the Takeover Code) regulates the civil regime for insider dealing.

Merger control rules are contained in the Enterprise Act 2002, although they do not generally apply to mergers in relation to which the European Commission (Commission) has exclusive jurisdiction under the EU Merger Regulation. In addition, specific statutory
regimes apply to certain areas, including water supply, newspapers, broadcasting, financial stability, telecommunications and utilities, and these separate regimes may have practical implications in merger situations.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Takeover Panel: changes to the Takeover Code and practice

There have been relatively few changes to the Takeover Code since the last edition of The Mergers & Acquisitions Review. The two main updates this year were the amendments to Rule 29 and the approval of provisional legislation that will come into force if and when the UK leaves the EU.

In addition, while there have been no further legislative changes to the Code regarding the increased disclosure obligations, which, as outlined in the previous edition, came into force on 1 January 2018, there has been a shift in practice in reaction to this legislation. It has been noticeable that the Panel does now expect parties to disclose substantially more information – about, for example, the future of their business – than they may previously have been accustomed to providing.

It is also worth considering how wider trends impact takeovers in practice. In particular, the increasing influence of the Pensions Regulator (which now has greater powers to intervene in transactions) and the global rise in protectionism are both likely to affect how takeovers are conducted. It is foreseeable that legislation will be updated in the future to reflect these trends, but in the meantime practitioners should consider how such changes may impact the structure of their transactions.

Rule 29

On 17 October 2018, the Takeover Panel introduced a series of amendments to Rule 29 (on asset valuations). The amendments do not materially alter the current application of Rule 29; rather, the changes primarily codify existing practice and provide increased clarification. Subject to some remaining variations, the amendments broadly bring Rule 29 in line with Rule 28 (on profit forecasts). These variations include, for example, the requirement for parties to undertake asset valuations fully; unlike Rule 28, there is no cover for ordinary course profit forecasts, which enable parties to circumvent the reporting requirements under Rule 28. The Panel has justified this on the basis that asset valuations are more subjective than profit forecasts. Additionally, Rule 29 requires the parties to produce a valuation report. This has always been the case, but the amended Rule 29 now sets out the requirements for this report in much more detail.

Brexit – provisional amendments

On 6 March 2019, Response Statement (RS 2018/2) was published, in which the Panel adopted the majority of the changes proposed by the Code Committee in relation to the UK's planned withdrawal from the European Union. The amendments will take effect on exit day (within the meaning of Section 20 of the European Union (Withdrawal) Act 2018). Two particularly notable points arise from the Response Statement. First, the rules regarding shared jurisdiction and the rules aligning the treatment of EEA shareholders with other
overseas shareholders will be removed. Secondly, it is interesting that the Panel decided not to get rid of the EU conditions, a decision that the Panel has acknowledged is for purely pragmatic reasons.

ii Contractual interpretation

Contractual interpretation is an ever-changing landscape, and it is important for M&A practitioners to keep abreast of recent developments, which may provide useful lessons when drafting transaction documents. A selection of noteworthy cases that have come before the courts in the past year are highlighted below.

In *Rock Advertising v. MWB Business Exchange*, the Supreme Court held that a variation clause in a contract, which required modifications to be in writing, invalidated a subsequent oral agreement to vary a contract. The Court gave effect to the contractual provision and reasoned that it would be contrary to party autonomy if parties were not able to bind themselves as to the form of future variations. This means that, from the point that a contract is made, the parties’ autonomy is qualified according to what the parties have agreed. While *Rock Advertising* does not disturb the general law that parties are able to vary a contract subject to the necessary conditions being met, the decision does mean that parties can now be more certain that their written agreements fully reflect the terms of their agreement.

The Court of Appeal considered a dispute concerning the interpretation of a force majeure clause in *National Bank of Kazakhstan v. BNY Mellon*. The appellants, NBK, sought declarations to the effect that BNY Mellon was not entitled to freeze assets located in London on the basis that Belgian and Dutch orders were not recognisable in England. BNY Mellon relied upon a clause in a global custody agreement that excused any non-performance (here, the failure to follow the NBK’s instructions) caused by ‘any order [. . .] imposed by any [. . .] judicial [. . .] authority’. The Court interpreted the clause broadly, giving the words their plain meaning, and held that the scope of the clause did extend to the Belgian and Dutch orders. This case is also an important reminder that international parties may be exposed to (potentially) conflicting laws in the different jurisdictions in which they operate.

*Chudley v. Clydesdale Bank* concerned the identification of a class for the purposes of the Contracts (Rights of Third Parties) Act 1999 (Act). The Court of Appeal ultimately held that, where a bank had (wrongfully) entered into a contract with an investment company that specified how investors’ money should be held, the investors were entitled to claim the benefit of the contract, despite being unaware of the existence of the contract at the time of their investment. Crucially, the Court confirmed that the use of the term client account in the contract was sufficient to expressly identify a class (namely clients investing in the scheme) for the purposes of the Act, and that the appellant investors were within that class. This case is of particular interest because, in reaching this decision, the Court determined that the identification of a class relied on the construction of the contract as a whole.

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7 *Rock Advertising Ltd v. MWB Business Exchange Centres Ltd* [2018] UKSC 24
IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Inward M&A increased notably in 2018: foreign acquisitions of UK companies were valued at a total of £71.1 billion, compared with £35.2 billion in 2017. Foreign investment was largely driven by the US, and resulted in a number of high profile deals such as US media firm Comcast’s acquisition of Sky. Nevertheless, although the UK retained its position as the top investment destination in Europe, research indicates that foreign direct investment (FDI) to the UK has fallen by 19 per cent since the vote in favour of leaving the EU. In contrast, neighbouring countries appear to be reaping the benefits of Brexit-related uncertainty, as FDI into other western European economies (such as Luxembourg, France and the Netherlands) has been on the rise. While the UK remains in its current state of limbo, investors are likely to adopt a more cautious approach to investing in the UK.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Technology, media and telecoms

The technology, media and telecoms (TMT) sector was a particularly fruitful area for M&A activity in 2018, with some of the largest deals ever recorded in this industry. The strong performance in the UK was mirrored globally: the TMT sector increased by 4 per cent, the biggest growth worldwide. In the Americas, for example, the TMT sector was by far the highest in terms of deal volume, and the second highest (behind the energy, mining, oil and gas sector) in terms of deal value in 2018.

The focus of the media industry was dominated by two headlines in 2018: the merger between Disney and 21st Century Fox, and the battle for Sky. Disney’s US$71.3 billion acquisition of the film and TV assets held by 21st Century Fox, which was approved by shareholders in July 2018 and completed in March 2019, was one of the biggest media mergers ever recorded. While Fox does still exist independently of Disney, the direction of the corporation has now shifted away from entertainment to focus on news and sports. Commentators have speculated that this transaction will trigger a wave of similar mergers in the media business, as media providers react to the ever-growing influence of streaming films and television online.

In September 2018, Comcast outbid rival 21st Century Fox in a US$39 billion takeover of the broadcaster Sky, acquiring more than 75 per cent of shares in the British telecommunications company. After months of negotiations, the deal was ultimately struck by means of a blind auction with three rounds, an unusual process for a deal of this nature.

Another megadeal in the TMT sector was Vodafone’s €18.4 billion purchase of Liberty Global’s cable assets in the Czech Republic, Germany, Hungary and Romania. This was the largest telecom deal and the second-largest deal in the TMT sector in 2018. Subject to regulatory approval – which at the time of writing has not yet been confirmed – the deal will make Vodafone the largest provider of high-speed broadband and cable services in Europe.

12 Ibid.
13 CityAM, ‘UK bags Europe’s M&A top spot with $247 billion of deals in 2018 as TMT mergers grow’.
Driven by the continued growth of AI, cloud computing and advanced security solutions, the importance of the TMT sector looks set to continue into 2019. Within the TMT sector, areas such as 5G, smart speakers, radio and 3D printing are predicted to prove popular among dealmakers in the coming year.15

ii Shareholder activism

As noted in the previous edition, the past few years have seen a considerable increase in shareholder activism. Looking forward into the remainder of 2019, US-style activism in the UK and across Europe is likely to continue, with activists both affecting the course of, and acting as a catalyst for, future deals. The influence of activists has been particularly notable in transactions structured as schemes of arrangement. As schemes of arrangement allow the bidder to acquire 100 per cent control of the target if the scheme is approved, the statute governing them contains a series of protections for minority shareholders. Activist investors have been making increased use of these statutory provisions in the hope of securing more favourable economic terms in a trend known as ‘bumpitrage’.16

In 2018, activist investors launched campaigns at 25 companies (spending £5.72 billion on shares), in contrast to the 11 companies targeted in 2017.17 Notable examples of activist shareholder involvement in 2018 include Elliott’s influence both in Melrose’s takeover of GKN and in a campaign prompting UK retailer Whitbread to offload Costa Coffee to Coca-Cola. Elliott was also publicly hostile to Temenos’s recommended offer for Fidessa, and came out in support of the competing bid from ION investments instead.

iii Protectionism and national security implications in the M&A context

One of the major trends that has emerged over the past 12 months has been the rise in protectionism, both within the UK and globally. The recent upsurge in protectionist measures has been fuelled by heightened concerns about national security and chiefly relates to foreign investment restrictions, antitrust regimes and takeover rules enabling regulators to influence, or even prevent, the outcome of a deal. It is predicted that this emerging trend will cause a sharp slowdown in takeover activity over the course of 2019 and add to trade tensions as the government increases its power to scrutinise investments.

Under the Enterprise Act 2002, the government has powers to intervene in relevant merger situations that are deemed to affect national (or public) security, media plurality or the stability of the financial system. Recently, there have been growing concerns that national security is insufficiently protected under the current regime as, for example, the CMA can only assess a proposed merger referred to it by the government if two or more enterprises have ceased to be distinct enterprises, and one of two tests is satisfied: the acquired company’s annual turnover exceeds £70 million; or the merged entity would have a minimum 25 per cent share of sales or purchases in the United Kingdom of goods or services of a particular description.18

Against this background, during the past year the government made a series of short-term and long-term proposals to address national security concerns, and on 15 March 2018, the

15 Deloitte’s TMT UK Report.
17 Lazard’s Annual Review of Shareholder Activism, 2018
18 Enterprise Act 2002, Section 23.
Department for Business, Energy and Industrial Strategy (BEIS) published the government’s response to its consultation on short-term proposals, which amend the merger control jurisdictional thresholds.19

On 15 March 2018, the government confirmed its decision to lower the turnover threshold from £70 million to £1 million in the dual use and military use sector, and in parts of the advanced technology sector. Lowering the threshold to £1 million means that the turnover threshold will obviously be easier to meet, and a higher number of deals will be open to review by the CMA. Second, the government decided to introduce a new share of supply test in these two sectors. The new test, instead of only looking at the share of sales that a merged entity has, will also look at the share of sales of the target business before the merger. If the pre-merger share of sale of the target is 25 per cent or more, then the new share of supply test will be met, and the transaction will be subject to CMA scrutiny. These two changes will not replace the existing turnover and share of supply tests, but will exist alongside the existing CMA referral regime. The proposals will be brought into effect by the Enterprise Act 2002 (Share of Supply Test) Amendment Order 2018 (which has been laid before Parliament) and the Enterprise Act 2002 (Turnover Test) (Amendment) Order 2018.20

On 24 July 2018, the government went a step further by publishing proposals to review transactions on national security grounds. The proposals are directed at investments from potentially hostile foreign states, which are seen as more risky than UK-based acquirers, particularly in sectors such as national infrastructure and advanced technologies. The proposals would give the government the power to call in transactions for review (which could be a lengthy process), and parties would be able to voluntarily notify their transactions. The proposed national security regime would, where legal, take priority over applicable merger control regimes. For example, the government could clear an anticompetitive transaction in circumstances where it had national security grounds for allowing the transaction to proceed. In June 2018, for example, the government intervened, on grounds of national security, in the proposed £44 million acquisition of Northern Aerospace Limited by a subsidiary of China’s Shaanxi Ligeance Mineral Resources. Although this transaction was ultimately cleared, it lapsed on account of the delay and uncertainty. Thus, in an increasingly challenging regulatory environment, parties may be less inclined to engage in large, transformative deals.

Melrose Industrial’s hostile takeover of GKN plc in the first quarter of 2018 is the best recent example of increased levels of government scrutiny over deals with public interest implications. In the final stages of this dramatic acquisition, the CEOs of Melrose and GKN were required to appear before the BEIS Committee and, 48 hours before the GKN shareholder vote, the UK government intervened by writing a letter demanding binding commitments from Melrose. The intervention was justified on the grounds that GKN was important to the UK’s national security. The demands, including commitments to continue operating GKN as a UK business and investing in research and development projects, were considered the latest example of the government being increasingly willing to intervene in

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In addition to the post-offer undertakings agreed with the Panel, Melrose also entered into deeds of covenant and undertakings in favour of the Ministry of Defence and the BEIS with respect to the GKN business. As a result of these commitments, the government ultimately decided that statutory intervention was not required.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

In 2018, 42 firm offers were announced for AIM or Main Market companies that were subject to the Takeover Code. The use of debt financing to fund or part fund offers rose when compared to 2017, with 21 offers involving a debt portion (compared to 15 in 2017). The use of short-term bridge facilities remains popular, particularly for larger deals; the facilities are typically refinanced in the bond markets or with longer-term loan refinancing.

Rule 24.3(f) of the Takeover Code requires that offer documents must contain a description of how an offer is to be financed and the source or sources of the finance. In particular, an offer document must provide details of the key terms of the debt, including the interest rates and any step up or variation provided for (which would include market flex rights). Following the publication of the announcement of a firm intention to make an offer, any documents relating to the financing of the offer must be published on a website no later than 12 noon on the following business day (Rule 26.2(b)). The disclosure of any market flex provisions included in the financing arrangements can therefore be a contentious issue. Disclosure of negotiated flex rights pursuant to Rule 26.2 may lead to higher funding costs, as it can put potential syndicate members on notice of the arrangers’ ability to increase the interest payable (within the agreed parameters).

Rules 24.3(f) and 26.2 were introduced in 2011; in its 2012 review of the 2011 amendments to the Takeover Code, the Panel noted that as a result of the concerns outlined above, dispensation had been granted from the Rule 26.2 requirement in relation to disclosure of flex rights. This gives the parties a period of up to 28 days to complete syndication before publication of the offer document, which must then include details of the flex in accordance with Rule 24.3(f). Whether this 28-day concession will be long enough to complete syndication will depend upon the proposed timetable.

VII PENSIONS AND EMPLOYMENT LAW

i TUPE risk in M&A transactions

Although a pure share transfer typically does not engage the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), two key cases in 2017 highlighted the risk of employees successfully arguing that TUPE applies in relation to intra-group integration activities following completion of an M&A deal.

In ICAP Management Services Limited v. Dean Berry and BGC Services (Holdings) LLP, the court considered the application of TUPE in the context of a share sale of a parent company. The court held that the TUPE argument failed on the basis that there was no

transfer of the business in which employees were employed, as opposed to control of that business. The mere fact of control is insufficient to show that a transfer has taken place from the target subsidiary to the new parent company. The critical test is whether the new party has become responsible for carrying on the business, has incurred the obligations of the employer, and has taken over the day-to-day running of the business. The relevant test can be summarised as whether the new party has ‘stepped into the shoes of the employer’.

This test was expounded by the Employment Appeal Tribunal (EAT) in Guvera Ltd v. Ms C Butler and others,\(^\text{24}\) in which the EAT rejected the idea that it is a necessary condition of a TUPE transfer that the transferee has assumed the obligations of employer towards the employees of the undertaking (for example, by paying the employees’ wages). Rather, the factors outlined in ICAP Management were said to be important, but not necessary, aspects of a multifactorial test to find a TUPE transfer has taken place. In Guvera, the parent company went beyond exercising ordinary supervision of the subsidiary, including making and directly implementing key business decisions and directly handling a redundancy process. The EAT therefore found this gave rise to a TUPE transfer.

From a practical perspective, it is important to analyse the TUPE risk at the level of the day-to-day management of the business. While the purchaser may have a clear commercial interest in integrating the target’s business into its own, integration affecting day-to-day management (such as hirings and firings) will lead to a greater risk of a TUPE transfer occurring. In contrast, the kind of global strategic oversight that is inevitable in group companies with shared ownership will not be sufficient. Having group-wide policies on HR and remuneration matters, for example, should be seen as low risk, provided that implementation of those policies is a matter for each individual company.

Businesses should therefore be aware of this potential TUPE risk when structuring a transaction and planning post-completion integration steps.

**ii Employment status**

Employment status remains a hot topic, particularly in those sectors (such as the gig economy) in which workers have traditionally been classified as self-employed but are now claiming to be entitled to certain employment rights. The government commissioned Matthew Taylor, the Chief Executive of the Royal Society of Arts, to conduct a review of modern employment practices;\(^\text{25}\) the result report was published in July 2017.\(^\text{26}\) The Taylor Review recommended significant reforms to the current categorisation of workers and self-employed individuals, and the rights attaching to each status.

The government issued its response in February 2018,\(^\text{27}\) in which it generally agreed with the Taylor Review, but has chosen to consult on many of the recommendations before setting firm policy changes. It therefore launched a number of consultations in conjunction with its response, including regarding employment status.\(^\text{28}\)

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24 Guvera Ltd v. Ms C Butler and others UKEAT/0265/16/DM.

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The employment status consultation contemplated new legislation that would set out the test to be met for an individual to be categorised as an employee, either using existing case law criteria or on the basis of new criteria. The paper also considered the possibility of aligning the definitions of employed and self-employed under the employment rights system and the tax system. However, the consultation makes clear that no decisions have been made about whether or how to reform employment status, so imminent legislative change appears unlikely for the moment. The consultation closed on 1 June 2018.

The government responded to the Taylor Review consultations in December 2018, publishing a policy paper – the Good Work Plan. This included a commitment by the government to legislate to improve the clarity of the employment status tests and tackle misclassification. There will also be proposals on how to align the employment status framework for tax and employment rights. However, the government said it first needs to conduct yet more research into employment status, so imminent legislative change appears unlikely for the moment.

For now, businesses should remain alive to the risk that the individuals within their workforce may be incorrectly classified, and that the rights and responsibilities attaching to those individuals may be subject to change. This could have significant financial and reputational implications for businesses, particularly in the current political climate. Purchasers should therefore conduct thorough due diligence on the employment status of a target’s workforce and seek appropriate indemnity protection where necessary.

iii Minimum contribution rate increases under auto-enrolment
There is mandatory auto-enrolment in the United Kingdom. This means that companies are required to offer (most) workers at least a defined contribution tax-registered pension plan providing a minimum level of contributions. These requirements have been introduced on a staged basis. Since 6 April 2019, the minimum total contribution is 8 per cent of an employee’s qualifying earnings (of which the employer must contribute at least 3 per cent). This recent increase to the cost of auto-enrolment will need to be taken into account by purchasers as part of a target’s continuing employment costs.

iv Abolition of contracting out for defined benefit schemes
On 6 April 2016, contracting out of the state pension in defined benefit schemes was abolished as part of the introduction of the reformed UK state pension system. Employers have therefore lost the national insurance rebate to which they were previously entitled as a result of contracting out of the state pension.

The abolition of contracting out could be a relevant consideration for those purchasers considering taking on a target’s (now formerly contracted out) defined benefit scheme that is still open to future accrual (although such schemes are now rare), as the employer would be required to pay a higher level of national insurance contributions.

However, a statutory modification power has been introduced that allows employers unilaterally to amend scheme rules governing accrual rates and member contribution levels.

30 The contribution rates do not apply to all of an employee’s pay, but only to the amount falling within the qualifying earnings band. For the 2019–2020 tax year, qualifying earnings are gross annual earnings between £6,136 and £50,000.
so far as is necessary to compensate the employer for the loss of its national insurance rebate. This power is subject to certain restrictions and would require consultation with employees. The power is available until 5 April 2021.

v Transfers of previous service benefits
A seller may require the purchaser to continue to offer a target’s employees membership of a defined benefit pension scheme, including accepting a transfer of the employees’ (and possibly former employees’) previous service benefits into that scheme, although this is now relatively unusual.

If a transfer is to be carried out on a without consent basis, certain requirements must be met. Prior to 6 April 2018, it was not possible to transfer contracted-out rights without consent to a scheme that had never been contracted out. The abolition of contracting out on 6 April 2016 meant that newly established schemes could not therefore receive a without-consent transfer of contracted-out rights. Since 6 April 2018, such transfers are permissible, but only if certain conditions are met. On acquisitions, transfers would usually be made with members’ consent, but they could be made on a without-consent basis, particularly if it is intended also to transfer the benefits of any former employees.

vi Further scrutiny planned of corporate activity impacts on pensions
The government is planning to intensify the Pensions Regulator's scrutiny of how corporate activity may affect pension provision. A number of changes (announced in a response to consultation, published in February 2019) may be introduced through the 2019 Pensions Bill.

One change will introduce a requirement for employers or parent companies to make a declaration of intent, addressed to the pension scheme trustees and shared with the Pensions Regulator, ahead of certain business transactions, such as the sale of the controlling interest in a sponsoring employer, stating how the employer proposes to mitigate any detrimental impact on the pension scheme.

There will also be new civil penalties of up to £1 million, and new criminal penalties involving unlimited fines, up to seven years’ imprisonment (the custodial sentence could be imposed for wilful or reckless behaviour in relation to a pension scheme), or both. The targets of some of these new punitive measures would be the employer sponsoring the pension scheme and anyone associated or connected with that employer.

Changes are also planned for the Pensions Regulator's financial support direction (FSD) regime, including an extension of the regime's scope to capture employers’ controlling, individual shareholders, and a broadened range of targets for a contribution notice (issued where an FSD has not been complied with) to include persons associated or connected with the FSD recipient.

vii Guaranteed minimum pension equalisation requirement
Purchasers taking on a target’s defined benefit scheme containing a form of contracted-out benefit known as guaranteed minimum pensions (GMPs) will need to understand any funding implications of an equal treatment ruling. Every pension scheme containing GMPs is affected by the 2018 ruling because the unequal design of GMPs is mandated by legislation.

31 That is, without the consent of the members whose benefits are to be transferred.
The High Court decided that schemes must address the sex inequalities brought about by GMPs earned by service from 17 May 1990 (the ability of members to earn GMPs stopped on 6 April 1997).

VIII TAX LAW

While Brexit loomed large in 2018, we have seen some significant (non-Brexit-related) changes to the UK’s domestic tax landscape. Among others, the taxation of non-residents in respect of UK land was overhauled, a new tax charge on offshore receipts from intangibles was introduced and the transferable tax history, an innovative measure in the oil and gas area, became reality.

i Brexit

HM Revenue & Customs (HMRC) have published a large volume of information setting out, in particular, how businesses should prepare for a no-deal Brexit, but a lot is still to play for. Given the uncertainty at the time of writing, the precise tax consequences of Brexit remain unclear.

It should, however, be noted that, in addition to creating potential VAT and customs issues on cross-border transactions, Brexit may mean that UK companies are no longer able to avail themselves of certain tax-related benefits of the UK’s membership of the European Union, for example benefits under the Parent–Subsidiary Directive. If UK parent companies can no longer rely on this Directive (which abolishes withholding taxes on payments of dividends between associated companies of different Member States), dividends would be received subject to withholding tax at the relevant double tax treaty rate, and this is not necessarily zero (for instance, in respect of dividends from German and Italian subsidiaries, it would be 5 per cent). Intra-group payment flows should, therefore, be reviewed, and holding structures for future acquisitions designed, with this in mind.

ii Investing in real estate, equity or debt

Over the past year, the government has introduced a number of changes to the taxation of non-residents investing in UK land. With effect from April 2019, any gain on a disposal of an interest in UK land (irrespective of whether it is a residential property) by a non-resident is subject to UK capital gains tax or corporation tax. The charge also applies in respect of a disposal of assets (such as shares) that derive at least 75 per cent of their value from UK land if a non-resident has a substantial indirect interest in that land. Offshore corporate landlords will be subject to corporation tax rather than income tax from April 2020 (although the non-resident corporate landlord scheme will continue to apply). It should also be noted that, from 1 March 2019, the time limit for filing a stamp duty land tax return has been shortened from 30 to 14 days.

Private equity structures are often set up so as to allow managers to benefit from entrepreneurs’ relief (ER) in respect of capital gains realised on an exit. Broadly, ER is available where an individual has held a minimum 5 per cent interest in a company for a certain minimum period, and its effect is to reduce the capital gains tax rate to 10 per cent.

For disposals on or after 6 April 2019, qualifying for ER has become more difficult. The minimum holding period has been extended from 12 to 24 months, and an economic substance requirement has been added to the 5 per cent interest test; previously, this test was satisfied if an individual held 5 per cent of the voting rights and 5 per cent of the ordinary share capital in a company. The application of this test may be further complicated by a recent decision that preference shares with cumulative and compounding return count as ordinary share capital. On a more positive note, if, on or after 6 April 2019, an individual’s stake is diluted to below 5 per cent, he or she may be able to elect to protect the availability of ER in respect of gains accrued before such dilution. Raising additional capital is likely to be more straightforward as a result.

With effect from 29 October 2018, the government introduced a market value rule for transfers of listed securities to a connected company. It is likely that this measure is only the first step towards the introduction of a broader market value rule, given that the government has already consulted on extending it to transfers of unlisted securities and transfers to connected persons that are not companies.

From 1 January 2019, the regulatory capital securities regime has been replaced by the hybrid capital instruments regime. At a debtor’s election, the new regime applies a favourable tax treatment to instruments under which the debtor is entitled to defer or cancel a payment of interest, but that do not contain any other significant equity features. Under the new regime, it is irrelevant whether the instrument forms part of the debtor’s regulatory capital, as the regime is open to non-regulated as well as regulated entities. This may result in more diverse investment opportunities as other players, such as utilities, move into a space previously reserved for banks and insurers.

iii Withholding tax on interest
The UK imposes a 20 per cent withholding tax on yearly interest arising in the UK. The concept of yearly interest was considered by the Supreme Court in the Lehman Brothers case. The case concerned statutory interest that did not accrue from day to day, but was payable at the end of the Lehman Brothers administration. Given that the administration lasted more than one year, the Supreme Court decided that the statutory interest was yearly interest and subject to withholding tax. On this basis, it is possible that contractual interest on late payments could be subject to withholding tax if the period of default runs for a year or more.

iv Using tax losses
As part of the overhaul of the relief of corporate income losses that took effect in 2017, the UK introduced provisions limiting the set-off of carried forward losses to 50 per cent of a group’s profits above £5 million (with stricter restrictions for banks). On 29 October 2018, the government announced its intention to introduce a similar limitation in respect of the relief of carried-forward capital losses. The measure is intended to take effect from 1 April 2020 and, based on HMRC’s consultation on its delivery, anti-forestalling rules are likely to be introduced in respect of transactions signed before, but completing after, that date.


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In the previous edition of *The Mergers & Acquisitions Review*, we noted that the use of tax losses through surrenders as group or consortium relief may be affected by the *Farnborough* case,\(^{35}\) in particular in the context of joint ventures, because the case called into question whether, for the purposes of the grouping rules, a shareholders’ agreement is a constitutional document, and therefore whether its provisions can be taken into account to determine an entity’s controller. During the case’s appeal, the appellate court\(^ {36}\) did not, unfortunately, address this point. Therefore, joint venture partners may wish to consider locating provisions on voting rights in the joint venture entity’s articles of association rather than the shareholders’ agreement.

### v Anti-avoidance, transfer pricing and controlled foreign companies

Buyers may want to focus due diligence on, and seek robust warranties in respect of, remuneration structures for UK employees. In 2017, the government introduced the loan charge, a tax charge on certain disguised remuneration loan balances outstanding as at 5 April 2019. Given the recent public backlash following reports of a number of suicides linked to the measure and calls for action against employers, there is a risk of financial and reputational damage for companies that made use of the relevant disguised remuneration schemes.

Under the off-payroll working rules commonly known as IR 35, individuals providing services through a personal services company may be treated as employees for tax purposes. Currently, the service provider determines whether IR 35 applies where services are provided to a private sector client. The government intends to change this such that, from April 2020, the determination must, instead, be made by the client – a move likely to substantially increase compliance burdens.

Shareholder transactions also call for caution. The recent *Union Castle* case\(^ {37}\) indicated that share issues are within the scope of the transfer pricing rules. It remains to be seen whether HMRC would seek to use this decision to re-characterise shares issued by a fatly capitalised subsidiary as debt and what ramification this may have for other shareholder transactions, such as the payment of dividends.

The government has amended the group financing exemption under the UK controlled foreign companies regime with effect from 1 January 2019, so as to exempt finance income that would otherwise be brought into charge as a result of it being derived from UK-connected capital, but not finance income that would otherwise be brought into charge as a result of it being derived from UK activity. Given the Commission’s recent decision in this area,\(^ {38}\) it is expected that the exemption, as amended, should not be state aid.

### vi VAT

The UK’s VAT grouping rules have been amended so as to allow certain eligible individuals and partnerships to join a VAT group. However, at the time of writing, these amendments have not yet taken effect, and the date on which they will become effective has not yet been confirmed.

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35 *Farnborough Airport Properties Ltd and others v. HMRC* [2017] UKUT 394.
36 *Farnborough Airport Properties Company & others v. HMRC* [2019] EWCA Civ 118.
37 *Union Castle Mail Steamship Company v. HMRC* [2018] UKUT 316 (TCC).
The European as well as the UK courts have had to grapple with questions around holding companies’ ability to recover input tax. In the Ryanair case, the Court of Justice of the European Union held that a holding company intending to provide management services to a takeover target can recover input tax on the cost of an abortive takeover. In contrast, input tax on the cost of a share sale was held to be irrecoverable. A recent UK case concerned a holding company that provided management services to its two subsidiaries on the condition that it would not invoice for the services until the subsidiaries became profitable. It was decided that the holding company did not carry on an economic activity and was, therefore, unable to recover input tax.

vii Intangibles, offshore receipts and digital services

The tax treatment of intangibles is bifurcated. Broadly, depending on the date of their creation or acquisition, intangibles are either treated as capital assets (CGT regime) or their tax treatment follows their accounting treatment (IFA regime). In an M&A context, the differences between the de-grouping rules under the two regimes has been a major point of criticism. In circumstances where CGT de-grouping charges would be added to the seller’s disposal proceeds and covered by the substantial shareholding exemption (SSE), the IFA regime imposed de-grouping charges on the target, thereby increasing the tax costs associated with the transaction. It is welcome that, with effect from 7 November 2018, IFA de-grouping charges are disappplied where a SSE is available to the seller. In addition, a limited tax relief in relation to goodwill has been introduced with effect from 1 April 2019.

Where the due diligence process reveals that the target group holds its intangibles in a jurisdiction with which the UK does not have a double tax treaty containing a non-discrimination provision, the application of the UK’s new income tax charge on offshore receipts from intangible property should be considered. Where a group’s UK sales exceed £10 million, the new charge applies to the extent that the relevant offshore receipts are derived from UK sales. While it is imposed on the offshore recipient, the tax can be collected from its UK affiliates. It should be noted that transfers of intangibles made to avoid the new charge may be caught by anti-avoidance rules.

The government has further announced that, with effect from 1 April 2020, it will introduce a digital services tax chargeable at a rate of 2 per cent on revenues derived by certain digital businesses, such as search engines, social media platforms and digital marketplaces, from activities linked to UK user participation. The tax will not apply unless certain revenue thresholds are exceeded, and it is intended as an interim measure until an international consensus on the taxation of the digital economy has been reached.

viii Oil and gas

As announced in November 2017, the government has introduced certain measures to facilitate the transfer of late-life oil and gas assets, including the innovative transferable tax history.

Previously, pure mature field specialists with little prior activity in the North Sea were unable to obtain effective corporation tax relief for decommissioning costs. This was because the

39 Ryanair Ltd v. The Revenue Commissioners (case C249/17).
41 W Resources PLC v. HMRC [2018] UKFTT 746.
resulting losses would sit in the specialist buyer whereas the capacity to use those losses (by way of carry-back against tax previously paid) would be locked away in the seller. The government has addressed this by introducing the transferable tax history with effect from 1 November 2018. This measure allows a seller to transfer all or part of its tax history to the buyer.

The petroleum revenue tax rules have also been amended to allow a buyer to obtain tax relief for decommissioning costs incurred by the seller where the seller retains the decommissioning liability.

IX COMPETITION LAW

i The UK merger regime

The CMA has the power to carry out an initial Phase I review, and has a duty to refer any qualifying transaction for a detailed Phase II investigation if it believes that the merger will or may give rise to a substantial lessening of competition. Phase I decision-making is undertaken by the Senior Director of Mergers (or another senior CMA official). Phase II decision-making is undertaken by an independent panel of experts drawn from a pool of senior experts in a variety of fields.

Notification is voluntary in the sense that there is no obligation to apply for CMA clearance before completing a transaction. The CMA may, however, become aware of a transaction through its market intelligence functions (including through the receipt of complaints) and impose interim orders preventing further integration of two enterprises pending its review. There is a risk that it may then refer the transaction for a Phase II investigation, which could result in an order for divestment.

The CMA strongly encourages parties to enter into discussions in advance of formal notifications to seek advice on their submission to ensure that a notification is complete and to lessen the risk of burdensome information requests post-notification. The CMA aims to start the statutory clock within 20 working days (on average across all cases) of submission of a substantially complete draft merger notice. The average length of the total pre-notification period was 33 working days in the 2018 to 2019 financial year. Some cases, however, require much longer pre-notification periods.

Once a transaction is formally notified, Phase I begins, and the CMA has a statutory time limit of 40 working days to reach a decision. The average length of Phase I was 36 working days during the 2018 to 2019 financial year. The CMA may extend the 40 working day period in certain exceptional circumstances, such as if it is waiting for information from the merging parties. The CMA formally paused the statutory timetable in two Phase I cases during the 2018 to 2019 financial year.

If the CMA’s duty to refer a transaction to a Phase II investigation is engaged, the parties have five working days from the substantial lessening of a competition decision (SLC decision) to offer undertakings in lieu of a reference to the CMA (although they may offer them in advance should they wish to do so). If the parties offer undertakings, the CMA has until the 10th working day after the parties receive the SLC decision to decide whether the offer might be acceptable, in principle, as a suitable remedy to the substantial lessening

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42 Mergers updates, Law Society Competition Section seminar, 12 March 2019. This figure was accurate as at 28 February 2019.
43 Ibid. This figure was accurate as at 28 February 2019.
44 Ibid. This figure was accurate as at 28 February 2019.

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of competition. If the CMA decides the offer might be acceptable in principle, a period of negotiation and third-party consultation follows. The CMA is required to decide formally whether to accept the offered undertakings, or a modified form of them, within 50 working days of providing the parties with the SLC decision, subject to an extension of up to 40 working days if there are special reasons for doing so.

At Phase II, the CMA must issue its decision within a statutory maximum of 24 weeks; this period is extendable in special cases by up to eight weeks. If remedies are required, the CMA has a statutory period of 12 weeks (which may be extended by up to six weeks) following the Phase II review within which to make a decision on any remedies offered by the parties.

The CMA has significant powers to impose interim measures to suspend or reverse all integration steps and prevent preemptive action in relation to both completed and anticipated mergers. This ensures that, although notification is voluntary in the United Kingdom, the CMA is able to prevent action being taken that would result in irreversible damage to competition. Severe financial penalties may be imposed for breaches of any interim orders or undertakings (capped at 5 per cent of the aggregate group worldwide turnover).

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The CMA levies substantial filing fees in respect of the mergers it reviews (between £40,000 and £160,000), depending on the turnover of the target business.

ii Treatment of mergers by the CMA

The number of Phase I merger decisions made by the CMA in the 2018 to 2019 financial year (56) was down from the 62 taken in the preceding financial year, and significantly down from the peak of 210 merger decisions made by the Office of Fair Trading in the 2005 to 2006 financial year. Since the 2005 to 2006 financial year, 56 is the lowest annual figure for Phase I decisions, the average being 90 decisions per year over that period.

Of the 56 cases decided during 2018 and to date in 2019, 41 were cleared unconditionally, representing around 73 per cent of cases, up from around 66 per cent in the preceding year (including cases cleared under the de minimis exception). Eleven cases were referred for Phase II review (around 20 per cent), up from 15 per cent in the preceding year. Undertakings in lieu of a reference were accepted in two cases, down significantly from the 12 see in the preceding year. Of the 11 transactions referred to Phase II, one was prohibited, three were cleared unconditionally, four were cleared with remedies and three were cancelled or abandoned. Overall, the CMA intervened (i.e., prohibited or accepted remedies) in around 13 per cent of cases in the 2018 to 2019 financial year, which is around twice the rate of intervention from the Commission over a similar period. The higher intervention rate may be explained by the voluntary nature of the UK merger control regime, which means that parties may elect not to notify transactions that do not give rise to significant competition issues.

iii Recently published statements and consultations relevant to mergers

Lord Tyrie, the current Chair of the CMA, outlined proposals for the significant reform of the UK’s competition policy in February 2019. With regards to merger control, the proposals include mandatory notification in the case of larger mergers that are likely to be the subject of review by multiple competition agencies globally while maintaining the voluntary system for smaller mergers. The rationale for the change is to avoid a situation post-Brexit whereby parties focus on notifications in mandatory regimes, which could put the CMA at a disadvantage when seeking remedies for UK-specific competition concerns if a global remedy package has already been agreed with other competition authorities.

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Further proposals to change the merger control regime were included in the ‘Unlocking digital competition’ report published in March 2019 by the Digital Competition Expert Panel that was appointed by HM Treasury. The report recommends that the largest digital companies with strategic market status should be required to make the CMA aware of all their intended acquisitions. The report also recommends the introduction of a balance of harms approach to the UK regime, which would require the CMA to assess the likelihood and the magnitude of the impact of a merger (both positive and negative), with mergers being prohibited where the harmful effects are expected to outweigh any merger benefits. The proposal follows from the review’s conclusion that there has been under-enforcement in UK merger control in the past, especially in digital markets. The CMA is not, however, in favour, and has warned about the unintended consequences of introducing such a test.

The CMA also aims to continue to tidy up its existing guidance in the year ahead, with a focus on ongoing consolidation and refreshing its guidance to reflect current practice (at the time of writing, a consultation on interim measures has been reissued). The CMA also intends to consider further revision of its jurisdictional and procedural guidance and merger assessment guidelines depending on the status of the UK’s exit from the European Union following the vote to leave on 23 June 2016.

iv Brexit and merger control

At the time of writing, it is expected that the United Kingdom will withdraw from both the European Union and the European Economic Area, which could cause significant changes to merger control regulation. It is likely that businesses will need to submit parallel notifications in the United Kingdom and European Union to obtain clearance for a deal, as the one stop shop principle should no longer apply (that is, the principle that if a merger has an EU dimension as defined in the EU Merger Regulation, it falls under the exclusive jurisdiction of the Commission). This could lead to a number of challenges for merging businesses, including increased regulatory burden. The CMA has emphasised in its Annual Plan for 2019 and 2020 that, from its perspective, the removal of the one stop shop principle would lead to an increased workload and may have an impact on its ability to cover other priority (but discretionary) areas such as market studies and investigations. In addition, the CMA expects its role in global mergers to change, with more extensive engagement with international regulators on both substance and potential remedies anticipated.45

X OUTLOOK

2018 was a lopsided year for M&A in the United Kingdom: following a bumper start to the year, activity fell dramatically during the second half of the year as political headwinds dampened deal-making spirits. Going into 2019, UK M&A suffered a third successive quarterly decline, hitting its lowest value since the EU referendum in June 2016. Q1 2019 saw just £27.4 billion spent on UK assets – a 36.6 per cent decrease from Q1 2018 – and no deals over the £5 billion mark were recorded.46

While Brexit uncertainty rages on, UK dealmakers are likely to remain cautious until greater political clarity is reached. Nevertheless, the availability of cheap debt, attractive

45 Competition and Markets Authority Annual Plan 2019/20.
46 Mergermarket, ‘EMEA MA Activity Q1 2019’.
bid financing costs and a weak sterling means that the UK is likely to remain a favourable environment for foreign investors. The rise in shareholder activism and developments in the technology sector – which supplied 16 per cent of the UK’s deal count in Q1 2019 – are also likely to fuel M&A activity for the remainder of the year.
I OVERVIEW OF M&A ACTIVITY

Following declines in 2016 and 2017, US M&A activity reversed trajectory in 2018. Aggregate US M&A deal value increased significantly, although the number of transactions fell. With US$1.73 trillion in M&A activity during 2018, deals for US targets increased by 32.1 per cent compared to 2017. However, the number of deals for US targets decreased 7.8 per cent from 13,500 in 2017 to 12,442 in 2018. These figures demonstrate a trend toward fewer, larger deals, reversing the trend seen in 2016 and 2017 of a larger number of lower-value deals. Narrowing in on acquisitions of US public companies valued at US$100 million or more, there were 165 such deals announced in 2018, a decrease of 5.2 per cent from 2017 (174 deals). Looking further back, the 165 deals signed in 2018 constituted a decrease of 12.2 per cent (188 deals) and 13.6 per cent (191 deals), and an increase of 9.3 per cent (151 deals) from 2016, 2015 and 2014, respectively.

Consistent with the trend in overall US M&A value versus volume, large-cap US M&A saw marked increases in 2018. There were 34 announced US public M&A deals valued over US$5 billion announced in 2018, and 65 valued between US$1 billion and US$5 billion, compared to 26 and 58, respectively, in 2017. Much of the 2018 large-cap activity was in the first half of the year (21 deals, compared to 13 deals in the second half of the year). Announced US public M&A deals valued between US$100 million and US$500 million decreased in 2018, from 56 in 2017 to 34 in 2018. M&A activity in 2018 varied throughout the year, with more active first and fourth quarters and a relatively quieter third quarter. There were 46 announced deals for public US companies valued over US$100 million in the first and fourth quarters of 2018, compared to 40 and 33 in the second and third quarters, respectively.

1 Richard Hall and Mark I Greene are corporate partners at Cravath, Swaine & Moore LLP. The authors would like to acknowledge the contributions of fellow partners Daniel Slifkin, Eric Hilfers, Len Teti and Margaret D’Amico and associates Philip Cernera, Andrew Davis, Aaron Feuer and Amanda Lamothe-Cadet.
3 Id.
5 Id.
6 Id.
7 Id.
8 Id.
For a discussion of cross-border deal volume, see Section IV.

US public M&A in 2018 was dominated by strategic rather than financial acquirers in 2018, as was the case in 2017. Approximately 136 US public M&A deals valued over US$100 million, or 82 per cent, involved strategic acquirers, up very slightly from 2017 (81 per cent). However, financial sponsors, including private equity buyers, have become well-established players in the US M&A landscape with relatively stable participation for the past few years. For example, the percentage of US public M&A transactions valued over US$100 million that involved private equity buyers has ranged between 13 and 21 per cent over the past four years. These numbers remain stable, among other reasons, because private equity activity is constrained by a cycle of low supply of quality targets, increasing levels of dry powder, and resultant competition among private equity buyers that contributes to high prices. Meanwhile, robust debt financing and stable equity markets have offered viable financing options to strategic buyers. Strategic buyers are even more dominant among large-cap deals. Of the 34 large-cap deals for US public targets entered into in 2018 (valued at US$5 billion or more), 31 were strategic (91 per cent), again up from 2017 (85 per cent).


Compared against the fourth quarter of 2018, the first quarter of 2019 saw a decrease in volume and an increase in the value of announced US M&A deals. There were 3,219 deals worth US$475.5 billion announced in the first quarter of 2019, compared to 3,422 deals worth US$393.9 billion in the fourth quarter of 2018 (a decrease of 5.9 per cent and an increase of 20.7 per cent, respectively). Compared against the first quarter of 2018, the first quarter of 2019 saw an increase in volume and a decrease in the value of announced US M&A deals. There were 3,137 deals worth US$545.2 billion in the first quarter of 2018 (an increase of 2.6 per cent and a decrease of 12.8 per cent compared to the first quarter of 2019, respectively). Globally, while worldwide M&A activity reached a record high of US$1.0 trillion in value during the first quarter of 2018, it decreased 30.7 per cent to US$693.4 in the first quarter of 2019, and the number of announced deals fell from 9,023 to 8,727. While 2017 brought increased certainty on the tax reform front, 2018 saw additional uncertainty related to US policies regarding trade tariffs on Chinese imports and national security (including President Trump’s executive order blocking the US$128.5 billion
proposed acquisition of Qualcomm Inc (Qualcomm) by Singapore-based Broadcom Ltd (Broadcom) in March. It remains to be seen how M&A activity, globally and in the US, will progress for the remainder of 2019.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A in the US is governed by a dual regulatory regime, consisting of state corporation laws (e.g., the Delaware General Corporation Law (DGCL)) and the federal securities laws (primarily, the Securities Act of 1933 (Securities Act) and the Securities Exchange Act of 1934).18 The Securities and Exchange Commission (SEC) is the regulatory agency responsible for administering the federal securities laws. Federal securities laws apply in the context of a merger, including federal proxy rules governing solicitation of target shareholder approval and federal securities laws relating to tender offers in the context of an offer to purchase shares of a publicly held target company. Furthermore, an acquisition or merger will imply fiduciary duties, as developed and applied in the target company’s state of incorporation.

Unlike most other jurisdictions, the US patchwork of federal and state acquisition regulation is not focused on substantively regulating changes of control of target companies. Rather, US regulation focuses on disclosure, ensuring that target company shareholders have the time and information required to make a fully informed decision regarding accepting a tender offer or voting in favour of a merger.

Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act), an acquirer is normally required to make a filing with US antitrust authorities prior to completing an acquisition if the transaction size exceeds US$90 million (adjusted annually for inflation); the requirement was increased in April 2019 from US$84.4 million in 2018.19

There is no general statutory review process governing foreign investment in the US. Under the Exon-Florio Amendment to the Defense Production Act of 1950, however, the President, through the Committee on Foreign Investment in the United States (CFIUS), has the power to review, investigate, prohibit or unwind transactions involving investments by non-US entities that threaten to impair national security.20 The 1992 Byrd Amendment requires CFIUS to conduct a full Exon-Florio investigation whenever CFIUS receives notice of a foreign government-led takeover of a US business that may affect national security.21 A CFIUS review is formally a three-step process. The initial informal review step has evolved over time to give both transaction parties and CFIUS additional time to resolve any national security concerns without the time constraints imposed by the formal review process.22 Historically, parties would pre-file a draft notice, address any initial comments and questions from CFIUS, and then formally file approximately one week later. However, CFIUS now regularly conducts detailed pre-filing reviews, asking extensive questions that must be

answered before the formal filing is made, which often takes several weeks.\textsuperscript{23} The formal review process is usually (although not exclusively) initiated based on voluntary notice filings, with an initial 45-day period during which CFIUS reviews a transaction to consider its effects on US national security. If CFIUS still has national security concerns after the initial period, a second 45-day investigation is launched (with a potential 15-day extension). Few transactions progress to the third step: presidential review and final determination, which determination is not subject to judicial review.\textsuperscript{24} Except for certain transactions, filing a notice to CFIUS is a voluntary measure. CFIUS may, however, review a transaction at its discretion, even after it is completed, which may affect the parties to an M&A transaction’s anticipated benefits, and the rise in CFIUS reviews is pushing parties to address their possibility early in the transaction process.

On 13 August 2018, President Trump signed the John S McCain National Defense Authorization Act for fiscal year 2019 into law, which included the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA).\textsuperscript{25} The legislation expands both the scope of activities subject to CFIUS review and the level of scrutiny directed towards transactions involving certain ‘countries of special concern’.\textsuperscript{26} Significantly, FIRRMA extends CFIUS’s jurisdiction to include the review of non-controlling investments in certain US businesses, and imposes mandatory filings for transactions in certain industries involving a foreign investor in which a foreign government has a substantial interest. The legislation also extended the time frame for the review of transactions. While formal regulations have not yet been proposed to implement all of the FIRRMA modifications to CFIUS, a pilot programme was rolled out in November 2018 mandating notification for certain critical technology transactions. After playing an active role in 2017 and 2018, CFIUS continues to be a substantial player in the US M&A landscape moving forward (see Section IV for a discussion of recent executive action and CFIUS review).

There are also additional industry-specific statutes that may require advance notification of an acquisition to a governmental authority. Examples of regulated industries include airlines, broadcasters and electric and gas utilities.


\textsuperscript{26} Id.
III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Fair value in appraisal actions

In the wake of the 2013 Dole Food Company, Inc management buyout, hedge funds added the battle for appraisal rights to their activist repertoires.27 As hedge funds sit on large reserves of cash, they continue to seek ways to earn returns. While appraisal rights are generally not a lucrative pursuit for the average shareholder, activist funds have the resources to make it worthwhile, and the values involved in appraisal arbitrage rose substantially in recent years. Appraisal arbitrage claims were valued at US$1.5 billion in 2013.28 Claims continued to rise through 2016, with 76 petitions challenging 47 deals.29 However, after years of steady increases, the tide turned in 2017.30 Appraisal petitions fell even further in 2018, with 26 petitions challenging 22 deals.31

Developments in the law governing appraisal actions in recent years, both legislative and judicial, have had a substantial impact on an appraisal’s upside and therefore on the incentive to bring appraisal actions in Delaware. In 2016, the Delaware legislature passed two amendments to Section 262 of the DGCL aimed at curbing appraisal arbitrage. The first imposed a de minimis exception for certain appraisal claims, requiring that more than 1 per cent of the outstanding shares entitled to appraisal perfect their appraisal rights or that the merger consideration for shares with perfected appraisal rights exceed US$1 million.32 The second allows a corporation to prepay the claimant any portion of the transaction price, limiting the principal on which interest accrues while the claim is disputed.33

Delaware judicial decisions have also significantly undermined appraisal arbitrage. In several 2015 decisions, the Delaware Court of Chancery relied entirely upon, or gave substantial weight to, the merger price in determining fair value in shareholder appraisal actions where there was a robust, conflicts-free sales process.34 Subsequently, three important 2016 Delaware Court of Chancery decisions cut back on what had appeared in 2015 to be strong deference to valuations based on per-share merger price minus any merger-related synergies, suggesting that other financial analyses would still be used.35 In 2017, however, Delaware courts reinvoked 2015’s deference to deal price. First, in May 2017, the Delaware Court of Chancery in In re Appraisal of PetSmart, Inc gave zero weight to the proffered

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30 Id.
31 Id.
33 Id.
discounted cash flow (DCF) analyses, finding them speculative and that the claimants had not shown they were reliable, whereas the deal price resulted from a robust pre-signing auction with well-informed, appropriately incentivised bidders.\(^{36}\)

In August 2017, the Delaware Supreme Court reversed the Court of Chancery’s 2016 decision in *In re Appraisal of DFC Global Corp*, disagreeing that future uncertainty of the private equity buyer undermined the deal price and finding that the Court of Chancery was not justified in giving the deal price equal, rather than substantially more, weight relative to the other valuation methods proffered.\(^{37}\) With regard to future uncertainty, the Court stated that absent any academic or empirical evidence to the contrary, there was no reason to think market participants would be incapable of factoring regulatory uncertainty into their analysis, and that the market’s collective judgment would be more likely to be accurate in assessing the related risk than any individual’s estimate.\(^{38}\) The Court also found no logical basis for the notion that the deal price deserves less weight in the context of a private equity buyer, stating that all buyers take the potential return on equity into account to justify the costs and risks of an acquisition, and the fact that a private equity buyer may demand a certain rate of return does not mean that the price it is willing to pay is not a meaningful indication of fair value.\(^{39}\)

Similarly, in December 2017, the Delaware Supreme Court reversed the Court of Chancery’s 2016 decision in *In re Appraisal of Dell Inc* on the basis that the Court of Chancery did not afford the deal price any weight, stating that the deal price need not be shown to be the ‘most reliable’ indicator of fair value for it to receive any weight at all and that ‘[t]he issue in an appraisal is not whether a negotiator has extracted the highest possible bid. Rather, the key inquiry is whether the dissenters got fair value and were not exploited.’\(^{40}\) The Court criticised several components of the trial court’s reasoning. First, the Court found that any perceived ‘valuation gap’ based on investor ‘myopia’ was contrary to the proffered evidence, which indicated that analysts considered the company’s long-range outlook, as well as to the efficient market theory, which suggests that for widely traded companies lacking a controlling shareholder, the market is well informed and able to digest available information to adjust its valuation for a long-range outlook.\(^{41}\) As in *DFC*, the Court rejected the proposition that the absence of strategic bidders undermined the deal price, seeing no rational connection between status as a financial sponsor and fair price.\(^{42}\) The Court also rejected the proposition that the go-shop was fatally flawed, including due to the alleged ‘winner’s curse’ in management buyouts, because bidders had full access to requested data and affirmative steps were taken to remedy the inherent information asymmetry.\(^{43}\) Furthermore, the Court rejected the proposition that Michael Dell’s alignment with one bidder had meaningfully deterred rival bidders absent evidence that he would not participate with such rival bidders.\(^{44}\) In July 2018, the Chancery Court in *In re Appraisal of Solera Holdings, Inc* applied *Dell* to conclude that deal price was the best evidence of fair value.\(^{45}\) The Court accepted Solera’s valuation, which

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38 Id. at 349.
39 Id. at 349-50.
41 Id. at 24-25.
42 Id. at 28.
43 Id. at 32.
44 Id. at 34-35.
excluded synergies from the deal price and resulted in a valuation that was 3.4 per cent below deal price. The Court found that Solera was ‘sold in an open process that, although not perfect, was characterized by many objective indicia of reliability’, and that such process therefore provided the most reliable evidence of fair value.

Further undermining appraisal prospects, when Delaware courts have found flaws in a sale process, they have increasingly, although not universally, found fair value below rather than above the deal price, emphasising the statutory mandate to exclude synergies. In May 2017, the Delaware Court of Chancery in In re Appraisal of SWS Group, Inc found the US$6.92 per share merger price unreliable in light of a number of factors, including that the buyer, Hilltop Holdings, Inc, was a major creditor of the target’s, and informed the target board that it would not waive its credit agreement’s merger covenant for any alternative transaction. The Court also found flaws with the proffered company comparables due to substantial differences in size, business lines and performance. The Court instead relied on its own DCF analysis to reach a value of US$6.38 per share. Similarly, in ACP Master, Ltd et al v. Sprint Corp et al, Clearwire Corp was purchased by Sprint Corp (Sprint), its majority shareholder, for US$5 per share, but the Delaware Court of Chancery came to a valuation of US$2.13 per share. The parties had not argued for use of the transaction price for fair value, and the Court acknowledged that while Sprint had in some ways controlled the sales process, Sprint’s DCF analysis provided a better proxy for fair value than the dissenting shareholders’ because it was prepared by management in the ordinary course of business and pertained to the stand-alone company, without synergies. In two 2018 decisions, Blueblade Capital Opportunities LLC v. Norcraft Cos and In re Appraisal of AOL Inc, Delaware Chancery Courts found significant flaws in the respective sales processes and assigned no weight to the deal price in determining fair value. In each instance the Court instead applied its own DCF analysis, resulting in fair value determinations that were 2.5 per cent above the deal price in Norcraft and 2.6 per cent lower than the deal price in AOL.

The Delaware Court of Chancery continued to explore new theories of fair value in 2018. Regardless of the soundness of the sales process, one Delaware court articulated a preference for unaffected market price over deal price as a means to exclude synergies, at least where the target’s stock is widely traded and absent evidence that the market was not well informed at the time. In February 2018, the Delaware Court of Chancery in Verition Partners Master Fund Ltd v. Aruba Networks found fair value equal to the 30-day unaffected market price of US$17.13 per share, well below the US$24.67 per share deal price. The Court found that the deal price was reliable even though, unlike Dell and DFC, there was only one bidder but, citing the statutory mandate to exclude synergies, instead utilised the 30-day average unaffected market price. Absent expert testimony against the efficient market theory, and given that the company was widely traded and lacked a controlling shareholder, the Court

46 In re Appraisal of SWS Group, Inc, WL 2334852 (Del. Ch. 30 May 2017).
47 Id. at 30.
48 ACP Master, Ltd v. Sprint Corporation, WL 3421142 (Del. Ch. 8 August 2017).
49 Id. at 48-49.
found unaffected market price to be more direct and less speculative than deal price less synergies. The Court’s decision in Aruba would have both undermined appraisal prospects for public targets and also encouraged expert testimony challenging market efficiency.

In April 2019, the Delaware Supreme Court reversed the Court of Chancery’s decision in Aruba on the basis that the Court of Chancery abused its discretion in arriving at Aruba’s 30-day average unaffected market price as the fair value of the appellants’ shares. In a per curiam decision that was ‘stunningly tough on Vice-Chancellor Laster’, the Court thoroughly rejected the idea of trading price as a proxy for fair value and awarded the petitioners US$19.10 per share, a price which reflected Aruba’s estimation of the deal price excluding synergies.

Appraisal will continue to be an important area of Delaware corporate law as courts will continue to address which methods produce the best indication of a company’s fair value, with a particular emphasis on merger price (with potential adjustments for synergies or reduced agency costs). As courts delineate the circumstances in which sale processes should be respected, they will alter the appraisal landscape, deterring appraisal actions in circumstances where the merger price is likely to be treated as a ceiling, with adjustments reducing recoveries. Based on Delaware rulings in 2017, 2018 and early 2019, the territory where appraisal remains profitable is shrinking, and may well ultimately be confined to private company transactions and controller squeeze-outs, for which the deal price may be deemed unreliable.

ii Standard of review in fiduciary duty actions

The success of a claim that the members of a board of directors have breached their fiduciary duties, or that a financial adviser has aided and abetted such breach, is largely dependent upon the standard of review applied to the relevant directors’ actions. In recent years, Delaware courts have expanded the territory in which the business judgment rule, requiring gross negligence, applies, thereby drastically increasing deference to boards of directors and discouraging fiduciary duty actions. In 2015, the Delaware Supreme Court in Corwin v. KKR Financial Holdings LLC clarified that the voluntary approval of a merger (other than with a controlling shareholder) by fully informed, disinterested shareholders invoked the business judgment rule standard of review in post-closing damages actions even where Revlon-enhanced scrutiny would otherwise apply. According to the Court, Unocal and Revlon were designed as tools of injunctive relief to address important M&A decisions in real time and not as tools for obtaining post-closing money damages.

53 Id. at 30.
54 Verition Partners Master Fund Ltd v. Aruba Networks, Inc, No. 368, 2018 (Del. 16 April 2019) at 3.
56 Verition Partners Master Fund Ltd v. Aruba Networks, Inc at 3, footnote 54.
59 Corwin v. KKR Fin Holdings LLC at 312, footnote 58.
Subsequently, in 2016 and early 2017, Delaware courts continued to apply *Corwin* to fiduciary duty cases in a manner that clarified and extended the application of the decision. For example, in *Singh v. Attenborough*, the Delaware Supreme Court clarified the *Corwin* ruling by holding that the business judgment rule applies irremediably to any post-closing judicial review of a merger that received the uncoerced, fully informed vote of disinterested shareholders. Then, in *In re Volcano Corporation Stockholder Litigation*, the Delaware Supreme Court affirmed the Court of Chancery’s holding that if fully informed, uncoerced and disinterested stockholders tender their shares to approve a merger under Section 251(h) of the DGCL, such approval has the same effect as a vote under *Corwin* and the business judgment rule applies irremediably to the transaction.

However, in cases in 2017, Delaware courts applied *Corwin* more narrowly, demonstrating the limits of *Corwin*’s reach. This narrowing continued in 2018. In *Appel v. Berkman*, the Delaware Supreme Court overruled a Court of Chancery finding that a stockholder vote was adequately informed. In reviewing the stockholder vote approving the acquisition of Diamond Resorts International, the Delaware Supreme Court found stockholders were not fully informed because the board failed to disclose that the Diamond’s chair, the company’s founder and largest stockholder, was opposed to the transaction. The Supreme Court found that the ‘Chairman’s views regarding the wisdom of selling the company were ones that reasonable stockholders would have found material in deciding whether to vote for the merger or seek appraisal, and the failure to disclose them rendered the facts that were disclosed misleadingly incomplete’.

In November 2018, the Delaware Court of Chancery decided the *In re Tango, Inc Stockholders Litigation*, denying directors who approved a sale of the company *Corwin* protection because stockholders were inadequately informed when tendering into the transaction. Audited financials were not available at the time of the transaction due to a pending restatement, and while neither federal securities nor Delaware law mandated disclosure of audited financials in this particular context, the Court found that the absence of audited financials supported a reasonable inference that stockholder approval of the transaction was not fully informed. The Court stated that directors making “difficult decisions amid a ‘regulatory storm’” (such as a restatement of financials) may still achieve business judgment rule deference if they carefully and thoroughly explain all material aspects of the situation to stockholders. This may require providing information to stockholders beyond what is legally required.

Subsequently, in December 2018, the Delaware Court of Chancery denied a motion to dismiss fiduciary duty claims against the CEO of Xura, Inc in the *In re Xura, Inc Stockholder Litigation*. The CEO was involved in negotiating the sale of the company, and the Court...

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62 ‘Recent Developments in Delaware Corporate Law’, footnote 60.
63 See, e.g., *In re Saba Software, Inc Stockholder Litigation*, WL 1201108 (Del. Ch. 11 April 2017); *Sciacabacucchi v. Liberty Broadband Corporation*, WL 2352152, 3 (Del. Ch. 31 May 2017); and *In re Massey Energy Company Derivative and Class Action Litigation*, 160 A.3d 484, (Del. Ch. 4 May 2017).
65 Id. at 2.
67 *In re Xura, Inc Stockholder Litig*, 2018 WL 6498677 (Del. Ch. 10 December 2018).

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found that *Corwin* protection did not apply because stockholders were not fully informed about aspects of the negotiations when they approved the deal. The Xura CEO had pursued his own interests (including employment) over those of stockholders in undisclosed negotiations.

After Delaware courts’ 2015 and 2016 decisions seemed to nearly sound the death knell for post-closing fiduciary duties actions challenging transactions that had been approved by disinterested shareholders, cases in 2017 and 2018 suggest at least some continued vitality. One could argue that the facts in certain of these instances were extreme, but courts have now shown a repeated willingness to deny *Corwin* cleansing. It remains to be seen if Delaware courts continue to find shareholder votes uninformed or coerced in other contexts to preclude the application of *Corwin*, or if the trend will reverse.

### iii Material adverse effect clauses in Delaware

October 2018 marked the first time that a Delaware court found that an M&A target had suffered a material adverse effect (MAE) such that an acquirer could walk away from a deal. The Delaware Court of Chancery issued a 246-page opinion in *Akorn, Inc v. Fresenius Kabi AG*, holding that Fresenius had validly terminated its merger agreement with Akorn on multiple independent grounds. The Court found that Akorn had breached its representation concerning regulatory compliance, which could reasonably be expected to amount to an MAE; materially breached a covenant to operate its business in the ordinary course; and suffered a general MAE as a result of its financial performance. The Delaware Supreme Court upheld the decision in December 2018 on the grounds that Akorn’s breach of its regulatory representation could reasonably be expected to amount to an MAE, and separately that Akorn had suffered a general MAE as a result of its financial performance.

Akorn and Fresenius entered into a merger agreement shortly after the announcement of Akorn’s results for the first quarter of 2017. During the second quarter of 2017, Akorn’s business performance, in the words of the court, ‘fell off a cliff’, delivering results that fell materially below Akorn’s prior-year performance on a year-over-year basis despite the fact that Akorn had reaffirmed its full-year guidance on the day the merger agreement was announced. Akorn’s performance fell well below that guidance, forcing management to adjust Akorn’s full-year guidance downward. Additionally, following signing, Fresenius received multiple anonymous letters regarding regulatory and data-integrity issues at Akorn, and initiated an investigation. Two days prior to the outside date, Fresenius delivered notice to Akorn that it was terminating the merger agreement because of, among other reasons, Akorn’s breach of its regulatory representation and warranty, which could reasonably be expected to amount to an MAE; Akorn’s material breach of a covenant to operate its business in the ordinary course; and Fresenius’ right not to close once the outside date passed because Akorn had suffered an MAE. The court agreed that Fresenius was within its rights to terminate the merger agreement.

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70 *Akorn, Inc v. Fresenius Kabi AG* at 2, footnote 68.
71 Id.
72 Id. at 4.
The court found that Akorn’s performance decline was significant. In the five quarters following signing but prior to Fresenius’ termination of the merger agreement, Akorn’s revenue was down between 25 and 34 per cent each quarter, its operating income was down between 84 and 292 per cent each quarter, and its earnings per share was down between 96 and 300 per cent each quarter, in each case year-over-year. With respect to the finding that Akorn had suffered a general MAE, the court called Akorn’s dramatic downturn in performance ‘durationally-significant’, having ‘already persisted for a full year and show[ing] no sign of abating’,73 and noted that the problems were specific to Akorn rather than industry-wide.74

The court also found that Akorn’s regulatory issues were significant. In reviewing whether Akorn had breached representations it made regarding its compliance with regulatory requirements and whether such breach could reasonably be expected to result in an MAE, the court found that there was ‘overwhelming evidence of widespread regulatory violations and pervasive compliance problems at Akorn’.75 The court found the problems to be qualitatively and quantitatively significant, with the regulatory issues expected to result in a decline in value of Akorn of 21 per cent.76

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Like US M&A overall, US cross-border activity increased in value in 2018. There was a 12.6 per cent increase in the value of US cross-border M&A from 2017.77 For the first time since 2011, the US was a net acquirer in the context of cross-border M&A, with US companies acquiring US$321 billion of foreign companies, and foreign companies acquiring US$260 billion of US companies.78 As a percentage of all US M&A, US inbound cross-border deals had a relatively smaller presence in 2018. As tracked by What’s Market, compared to total deals, only 25, or 15.1 per cent, were reached with foreign buyers, compared to 36, or 20.7 per cent, in 2017.79 China announced outbound M&A continued to fall in 2018, compared to its record levels in 2016, slowing to US$116.6 billion in deal value, a 5.3 per cent decline from 2017.80 The depressed US–China deal volume was because of risks pertaining to deal certainty due to potential failures to receive regulatory approvals from Chinese regulators or CFIUS.81

73 Id. at 137.
74 Id. at 144.
75 Id. at 163.
76 Id. at 184.
78 Id.
80 Id.
i  Acquisition inversions and earnings stripping

Acquisition inversions, whereby US corporations reincorporate in low-tax jurisdictions via cross-border M&A (hereinafter, inversions), have in previous years been fundamental to foreign involvement in US M&A. Historically, US tax rates were some of the highest globally, and US-based companies consistently looked for ways to shield their international earnings from those rates. In the past, US-based companies could accomplish this by reincorporating in a foreign jurisdiction, or by moving to a country in which it was already doing a substantial amount of business in order to benefit from that country’s lower tax rate.  

For this to work, 25 per cent of the company’s sales, assets and employees had to be domiciled in the new jurisdiction. This was a difficult burden for most companies to meet and, as a result, inversions became popular. Under the rules governing inversions, a foreign target company and acquirer can be combined under a new holding company formed under the laws of a lower-tax foreign jurisdiction, whether or not it is the target company’s jurisdiction of organisation, if less than 80 per cent of the combined entity’s stock is owned by the former shareholders of the US company. By 2015, acquisition inversions accounted for 66 per cent of all proposed US outbound deals, up from 1 per cent in 2011.

Recent statutory and regulatory changes, however, have made inversion transactions substantially less attractive. In December 2017, massive US tax reform through the passage of the Tax Cuts and Jobs Act of 2017 (TCJA) substantially undercut the advantages of inversions and earnings stripping. On the one hand, the lower corporate tax and the dividend exemption reduced the tax benefits associated with inverting by excluding foreign earnings from US tax or taxing them at a lower rate. On the other hand, the legislation contains a number of provisions that specifically penalise inverters. These include further limitations on the deductibility of interest expense, increased transition taxes, and the BEAT tax (as defined below), a minimum tax that is calculated without taking into account certain deductions from related-party transactions (like earnings stripping) (see Section VIII for a detailed discussion of the TCJA and its implications for US M&A).

ii  CFIUS review

CFIUS plays a key gatekeeping role when it comes to foreign involvement in US M&A. In 2017 and 2018, CFIUS review has presented an increasingly significant obstacle, as CFIUS continues to interpret its jurisdiction broadly and Congress has broadened its authority. As discussed in Section II, new legislation has expanded the reach of CFIUS. Evidence suggests CFIUS received over 235 filings in 2017, compared to 172 in 2016 and 143 in 2015. CFIUS

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84 Id.


has interpreted its jurisdiction to include deals between non-US companies with a US nexus. For example, in 2016, the proposed acquisition of Lumileds by a Chinese consortium from Philips NV (a Dutch company) was abandoned by the parties at CFIUS’ request. CFIUS also requested that the parties abandon the acquisition of Aixtron SE (a German company) by a Chinese investor due to national security concerns. The parties refused to abandon the deal and opted to submit the matter to President Obama for review, which led to the first-ever presidential order proactively blocking an acquisition. Additionally, the parties abandoned the sale of Global Communications Semiconductors, LLC to San’an Optoelectronics Co, Ltd (a Chinese semiconductor company) due to CFIUS’ concerns. In September 2017, President Trump issued an executive order to block the acquisition of Lattice Semiconductor Corporation by Chinese private equity fund Canyon Bridge Capital Partners (Canyon Bridge). Finally, on 12 March 2018, President Trump again stepped in with an executive order following CFIUS review, blocking Broadcom’s US$128.6 billion proposed acquisition of Qualcomm on the basis that it threatened US national security. Although Broadcom is a Singapore-based company, the order came during a period of intense technological competition between the US and China, and CFIUS expressed concerns that Broadcom would undergo its typical cost-cutting measures to stymie research and development (R&D) and therefore undermine Qualcomm’s ability to compete with Chinese and other foreign rivals in the domain of wireless technology.

CFIUS’ recent history of enforcement demonstrates a focus on national security concerns, and increasingly general competition concerns, implicated in the context of Chinese buyers. In addition to Canyon Bridge, the Trump administration opposed billions of dollars worth of takeovers of US targets in 2017 and 2018. In early 2019, CFIUS announced that it had forced three separate divestitures and had imposed a US$1 million fine, its first-ever civil penalty, for repeated violations of a 2016 mitigation agreement. Two of the forced divestitures related to concerns about the potential exploitation of sensitive data relating to US citizens, part of the expanded scope of CFIUS granted by FIRRMA.

In its proposal for the fiscal year 2020 budget, the Department of Justice requested additional resources to assist with reviewing CFIUS cases. Failure to obtain regulatory approvals can trigger break-up fees for acquirers, and the rise in CFIUS reviews could push more M&A parties to address it in termination fee provisions. In particular, Chinese buyers may have to offer a higher bid...
to overcome a perceived increased CFIUS risk. Parties may also want to consider carving off any sensitive portions of their US businesses, which recently has included, among other things, finance and technology.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In 2018, the leading industry sector in the US on the basis of announced deal value data provided by Thomson Reuters was the energy and power sector. Deal value in this sector reached US$407.5 billion in 2018, which was a 23.6 per cent market share. The technology sector fell from first to second place with US$324.8 billion (18.8 per cent of the market) and healthcare was again third with US$215.4 billion (12.5 per cent of the market). The top five deals signed in 2018 for a US target were Cigna Corp’s acquisition of Express Scripts Holding Co (US$68.5 billion), Energy Transfer Equity, LP’s acquisition of Energy Transfer Partners, LP (US$61.8 billion), T-Mobile US, Inc’s acquisition of Sprint Corp (US$58.7 billion), International Business Machines Corp’s acquisition of Red Hat, Inc (US$32.3 billion) and Marathon Petroleum Corp’s acquisition of Andeavor (US$31.3 billion).

i Shareholder activism and engagement

Like 2017, 2018 was a busy year for shareholder activists in the US, and shareholder activism is becoming increasingly concentrated among established activist players. In 2018, there were 268 total activist campaigns announced against US companies, compared to 254 in 2017. There were a total of 51 proxy fights in 2018, up 8.5 per cent from 47 in 2017. Activists invested approximately US$2.5 billion more dollars in new activist positions in 2018 than 2017, and won more board seats in 2018 than in 2017, mostly through settlements. While 2017 saw a focus by such activists on large-cap companies, in 2018 they reversed course and focused on fewer targets with market caps in excess of $50 billion.

In connection with US M&A, activists continue to play a key role by arguing for alternatives to proposed mergers or by demanding a higher price, undermining target shareholder approval of proposed transactions. Activism and M&A often overlap. When

99 Id.
100 Id.
103 Id.
105 Id.
Activist investors buy up company stock and engage in various campaigns, they produce disruption and uncertainty that acquirers can leverage to garner support for a transaction, as occurred at Campbell’s, Magellan Healthcare, Dell and Hyundai in 2018.\textsuperscript{107} Activists may also advocate in favour of a sale of a target company to benefit from short-term increases in value. Pro-M&A activism was prominent in 2018, with approximately 33 per cent of campaigns launched in 2018 being M&A-driven.\textsuperscript{108} As institutional investors continue to concentrate ownership, activist investors benefit from having to convince fewer of their fellow investors to pursue their agenda. As of December 2018, one of BlackRock, Vanguard or State Street was the largest shareholder in 438 of the S&P 500 companies, roughly 88 per cent, and collectively the three firms owned 18.7 per cent of all shares in the S&P 500,\textsuperscript{109} compared to 14.7 per cent in 2013, while retail holders now hold less than 30 per cent.\textsuperscript{110} With the rise in shareholder activism, companies have increased their level of shareholder engagement with both activists and institutional investors.\textsuperscript{111}

\textbf{ii}  
Shifts in merger litigation to federal courts and away from disclosure-only settlements

Increasing deference towards boards of directors, exemplified by the legal developments in appraisal and post-closing fiduciary duty actions for damages discussed in Section III, have in part led to a shift in litigation away from appraisal and fiduciary duty claims in Delaware in favour of challenges in federal courts through federal securities claims alleging proxy fraud under Rule 14a-9 under the Securities Act of 1933.\textsuperscript{112} In 2017, 73 per cent of deals valued over US$100 million were challenged by shareholders, down from 94 per cent in 2013, but 87 per cent of those lawsuits were filed in federal court compared to only 32 per cent in 2013.\textsuperscript{113} The number of M&A litigated in Delaware has dropped precipitously in recent years, declining 81 per cent from 37 in 2016 to seven in 2017.\textsuperscript{114}

Also fuelling the migration to federal courts has been Delaware’s disdain towards disclosure-only settlements. In 2014, 93 per cent of US M&A deals over US$100 million resulted in shareholder litigation, with the first lawsuit in a challenged deal being filed an average of 14 days after the announcement of the deal and 59 per cent of all such litigation being resolved before deal closing.\textsuperscript{115} Of the litigation resolved before closing,

\textsuperscript{107} Id.
\textsuperscript{109} ‘Review and Analysis of 2018 U.S. Shareholder Activism’, footnote 102.
\textsuperscript{110} Id.
\textsuperscript{111} ‘M&A Update: Highlights from 2015 and Implications for 2016’, footnote 35.
\textsuperscript{112} Securities Act of 1933, footnote 18; False or Misleading Statements, 17 CFR 240.14a-9 (2000).
close to 90 per cent settled, with the remainder being withdrawn or dismissed.\textsuperscript{116} Of the 78 settlements reached in 2014, only six settlements, or 8 per cent, provided monetary consideration to shareholders, nearly 80 per cent only provided disclosure and 9 per cent included changes to deal protection provisions in the merger agreements.\textsuperscript{117} However, after years of building criticism of routine disclosure-only settlements within the Delaware Court of Chancery, the Court was particularly critical in 2015, resulting in the rejection of two such proposed settlements in key cases: \textit{Acevedo v. Aeroflex Holding Corporation} and \textit{In re Aruba Networks, Inc Stockholder Litigation}.\textsuperscript{118} Similarly, in its January 2016 decision in \textit{In re Trulia, Inc Stockholder Litigation}, the Delaware Court of Chancery reaffirmed its disfavour of disclosure-only settlements in class action M&A litigation on the basis that such settlements fail to create meaningful value for the class while providing defendants with broad releases.\textsuperscript{119} Such rulings have led to fewer M&A challenges in Delaware and increasing challenges in federal courts under federal securities laws. However, after \textit{Trulia}, the Seventh Circuit Court of Appeals overturned a lower court order approving a disclosure-only settlement using the same rationale as \textit{Trulia}.\textsuperscript{120} Judge Posner’s endorsement of \textit{Trulia} is binding on all federal courts in the Seventh Circuit, and is likely to convince other federal courts outside the Seventh Circuit to apply \textit{Trulia} as well.\textsuperscript{121} A number of federal district court judges have also raised questions about these settlements in recent years.\textsuperscript{122} Additionally, the New York Supreme Court in New York County recently declined to approve what the court described as a ‘peppercorn and a fee’ disclosure-only settlement.\textsuperscript{123} It remains to be seen whether other federal circuits will follow suit, but this development does not bode well for litigants who wish to use forum shopping to find a court that will rubber stamp a disclosure-only settlement.

A recent US Supreme Court case has additional implications for forum selection in securities litigation. The Supreme Court held in March 2018 that plaintiffs may bring class actions under federal securities laws in state courts, even where such lawsuits are comprised entirely of federal securities law claims, and companies may not then remove such claims to federal courts.\textsuperscript{124} Some companies attempted to circumvent that outcome contractually. Some companies used forum selection clauses in their by-laws, selecting the federal district courts as the exclusive forum for asserting claims under the Securities Act. While Delaware companies happily subject themselves to state forums for substantive claims such as fiduciary challenges, in light of increasingly deferential outcomes described above, they have looked to the federal courts for relief from the harsh scrutiny towards disclosure-only settlements to

\begin{enumerate}
\item \textsuperscript{116} Id.
\item \textsuperscript{117} Id.
\item \textsuperscript{119} In re Trulia, Inc Stockholder Litig, 129 A.3d 884, 895 (Del. Ch. 22 January 2016).
\item \textsuperscript{120} The Seventh Circuit Court of Appeals is based in Chicago, Illinois. Its jurisdiction covers the states of Illinois, Indiana and Wisconsin. In re Walgreen Co. Stockholder Litigation, 832 F.3d 718 (2016).
\item \textsuperscript{123} City Trading Fund v. Nye, 2018 WL 792283 (N.Y. Sup. Ct., 8 February 2018).
\item \textsuperscript{124} ‘Supreme Court Clarifies State Court Jurisdiction for Securities Claims and Opens Door to Plaintiff Forum Shopping’ Lexology, 23 March 2018, https://www.lexology.com/library/detail.aspx?g=6de86471-6e96-4ca7-808d-ddabe1dace06.
\end{enumerate}
resolve Securities Act claims. In late December 2017, a class action complaint by stockholders of Blue Apron Holdings, Inc, Stitch Fix, Inc and Roku, Inc (three of several recent companies that included forum selection by-laws requiring that federal securities cases be heard in federal district court), was filed in the Delaware Court of Chancery challenging such provisions under the DGCL. In December 2018, the Delaware Court of Chancery held that Delaware law does not permit corporations to use charter provisions to require stockholders to litigate certain claims brought under the federal securities laws in a specific forum.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

In US financing markets, 2008 to 2010 were difficult years, plagued by tumult and recession. 2011 to 2015 were characterised by recovery and growth, with record-setting financing activity and ever-lower yields. However, 2016 marked a turning point as interest rates experienced a sustained rise after hitting record lows in the first half of the year. In 2017, investment-grade corporate bond deal values reached record highs for the sixth consecutive year. During the first three quarters of 2018, the strong credit market continued. Leveraged loan issuance in the first half of 2018 fell just short of its first-half 2017 record. High-yield bonds also performed well, with the spread between junk bonds and US treasuries touching a 10-year low. However, the market turned dramatically in the fourth quarter of 2018, particularly in December. There was zero dollars of new high-yield issuance in December, the first such month since 2008. Leveraged loan prices also fell significantly, and multiple loan syndications were aborted due to lack of demand.

Several notable deals demonstrated that borrowers were able to achieve successful results at various credit levels in 2018. Permanent financings and major financing commitments included T-Mobile's US$38.0 billion of financing commitments for its combination with Sprint; Cigna's US$26.7 billion of bridge commitments, US$20.0 billion of senior notes and US$6.3 billion of bank facilities to fund its acquisition of Express Scripts; Broadcom's US$20.3 billion of loan facilities for its acquisition of CA; and United Technologies' US$6.5 billion bridge and US$11.0 billion of notes to support its acquisition of Rockwell Collins. In light of shakier financial markets, one trend to watch for in 2019 will be potential downgrades of investment grade borrowers. Commentators note that bonds rated in the lowest investment grade tier (BBB) now constitute more than half of the US$5 trillion

125 Complaint, Matthew Sciabacucci v. Matthew B Salzberg, No. 2017-0931-JTL (Del. Ch. 29 December 2017).
127 Id.
128 Id.
129 Id.
130 Id.
131 Id.
132 Id.
133 Id.
134 Id.
US investment grade bond market, up from about one-third in 2008. This uptick in triple B debt suggests that if the economy were to fall into a recession, a ‘wave of downgrades could push many BBB companies (and hundreds of billions of dollars of debt) out of the investment grade club entirely and potentially swamp the high-yield debt markets’.

Overall, US-syndicated lending reached an all-time high of US$2.5 trillion in 2018, an increase of 6 per cent over 2017, due primarily to increased investment grade lending volume. US-leveraged lending in 2018 was US$1.4 trillion, down 6.9 per cent from 2017, largely attributable to a reduction in refinancing activity. Despite the decline, US M&A leveraged loan issuance was robust, increasing 22 per cent to US$381 billion, the highest level post-crisis. In 2018, there were 78 leveraged acquisitions of US reporting companies valued at US$100 million or more, compared to 80 in 2017 and 88 in 2016, but leveraged acquisitions as a percentage of overall M&A activity was steady at 46 and 47 per cent in 2017 and 2018, respectively. The second half of 2018 saw a significant decline in leveraged deals, dropping from 56 per cent in the first half to 38 per cent in the second half. Average debt to EBITDA multiples for large US leveraged buyout (LBO) transactions stayed at elevated levels in 2018, remaining at an average 6.2 times. While the average debt to EBITDA multiples remained stable, the number of highly leveraged deals grew. Of LBOs completed in 2018, almost 40 per cent were levered seven times or more, a return to levels not seen since 2007.

US tax reform has had a significant impact on M&A financing moving forward (see Section VIII). In particular, new Section 163(j) of the Code caps taxpayers’ net interest expenses at 30 per cent of the taxpayer’s ‘adjusted taxable income’, which approximates EBITDA for tax years beginning before 1 January 2022, and EBIT thereafter. As a result of the limitation, highly levered acquirers are more likely to shift acquisition debt from the US, where interest deductions may be limited, to other jurisdictions. Acquirers may also limit their debt financing of acquisitions altogether in favour of equity financing (the new 21 per cent corporate tax rate has this effect as well). Because the limitation applies even to existing debt, financing for past acquisitions may also be compromised. However, it remains to be seen how the TCJA’s various provisions will interact to impact acquisition finance dynamics going forward.
VII EMPLOYMENT LAW

At its best, executive compensation can incentivise corporate performance by aligning the interests of shareholders and management. At its worst, as seen in the bankruptcy of Enron Corporation, executives’ pay can come at the direct expense of a company’s shareholders and stakeholders. Executive compensation has come under increased scrutiny from all directions – from institutional and retail investors, proxy advisers, courts and legislators – in efforts to minimise the agency problem that arises when directors and management are permitted to set their own compensation. As certain management-friendly pay practices are phased out in response to shareholder activism and proxy adviser recommendations, companies are crafting increasingly complex pay-for-performance programmes to better respond to shareholder and institutional investor concerns.

i Shareholder engagement and institutional adviser influence

In 2018, shareholders continued to remain engaged with executive compensation issues through say-on-pay (SOP) advisory votes and the approval of both new and amended equity plans. Although SOP votes are non-binding, public companies are generally concerned with their outcomes given the ability of SOP votes to influence director elections. In 2018, 57 Russell 3000 companies failed SOP votes, which is the highest failure rate since 2015. The 2018 failure rate represents a marked increase from the number of failed SOP votes in 2017 and 2016, and is generally consistent with the number of failed SOP votes in the three years preceding 2016.

Proxy advisory services such as Institutional Shareholder Services (ISS) and Glass, Lewis & Co continue to play a role in the increasingly complex landscape of executive compensation and equity programmes. However, data suggests that the connection between an ‘against’ recommendation from ISS and the shareholder vote to approve a company’s compensation programme is tenuous. While just 2.6 per cent of companies failed SOP votes in 2018, ISS issued against recommendations on approximately 14 per cent of SOP votes in 2018, which is the highest observed rate of against recommendations issued by ISS since 2013. Approximately, 20 per cent of companies that received against recommendations

144 Jerry W Markham, A Financial History of Modern U.S. Corporate Scandals: From Enron to Reform 87–88 (Routeledge, 1st ed. 2006) (comparing the severance payments of Enron executives to those of non-executive employees).
147 ’2018 Say on Pay Results – End of Year Report’.
from ISS failed their SOP vote in 2018.\textsuperscript{149} By comparison, 14 and 12.5 per cent of companies that received against recommendations from ISS failed their SOP vote in 2016 and 2017 respectively.\textsuperscript{150}

Although the extent of ISS and other proxy advisers’ influence on the corporate governance landscape is unclear, data shows that ISS recommendations do carry some weight. In 2018, shareholder support was 31 per cent lower at companies that received an against SOP recommendation from ISS.\textsuperscript{151} However, proxy advisers’ influence is not absolute, and not all US publicly traded companies engage with proxy advisers. Many of the major institutional investors, including BlackRock and Vanguard, maintain in-house proxy analysis and governance groups to inform their own voting decisions in lieu of engaging proxy advisory firms.\textsuperscript{152}

Criticism of proxy advisers has also increased in recent years. Some critics have argued that proxy advisers serve a quasi-governmental role without the necessary regulatory safeguards.\textsuperscript{153} For example, lawmakers have argued that ISS is inherently conflicted because it provides both proxy voting recommendations to shareholders and also consulting services to public companies.\textsuperscript{154} As a result, in October 2017, HR 4015, the Corporate Governance Reform and Transparency Act of 2017, was introduced with the purpose of regulating proxy advisory firms.\textsuperscript{155} Under HR 4015, proxy advisers would be required to register with the SEC, disclose any potential or actual conflicts of interest relating to the provision of proxy advisory services and provide an opportunity for companies to comment on draft recommendations. HR 4015 passed the House of Representatives and was referred to the Senate on 21 December 2017, which has held a number of hearings on the bill.\textsuperscript{156}

\textsuperscript{149} Id.


\textsuperscript{154} Id.; see also ‘Examining the Market Power and Impact of Proxy Advisory Firms: Hearing Before the Subcomm. on Capital Mkts. & Gov’t Sponsored Enters. of the H. Comm. on Fin. Servs.’, 113th Cong. 2 (2013), https://www.govinfo.gov/content/pkg/CHRG-113hhrg81762/pdf/CHRG-113hhrg81762.pdf.


\textsuperscript{156} Id.
ii Golden parachutes and executive severance developments

ISS has singled out certain change in control (CIC) benefits historically provided to executives in connection with M&A transactions (such as single-trigger acceleration of equity-based awards and gross-ups of the excise tax imposed under Section 280G of the US Internal Revenue Code of 1986 (Code)) as problematic. ISS’s published policy guidance states that it is likely to render an against or withhold vote recommendation when single-trigger acceleration or a Section 280G gross-up is included in a new CIC agreement. In addition, ISS considers whether a company’s plans and agreements that were in place prior to a transaction contain excise tax gross-up and single-trigger equity acceleration provisions in determining its recommendation on say on golden parachute (SOGP) proposals.

Given the range of shareholder responses to SOGP proposals and pressure from proxy advisers to limit excessive compensation package strategies, it is likely that companies will continue to review and restructure CIC benefits and may shift increasingly towards a transaction-based gross-up model. Although many companies have eliminated Section 280G gross-ups from their CIC and employment agreements to avoid negative recommendations from proxy advisory firms, recent data suggests that companies are increasingly providing for Section 280G gross-ups in the context of acquisitions. Although shareholder dissatisfaction with outsized golden parachute payments has increased over the years to historically high levels, 2018 saw an increase in the failure rate compared with 2017, with 14.7 per cent of the 95 Russell 3000 companies conducting an SOGP vote in 2018 failing versus 19.5 per cent of the 123 Russell 3000 companies conducting an SOGP vote in 2017.

iii Director compensation

In recent years, director compensation has come under scrutiny after a series of shareholder lawsuits alleging excessive director pay. Until recently, the Delaware Court of Chancery reasoned that potential conflicts of interest that occur when directors set their own compensation are nonetheless subject to business judgment deference where stockholders approve a plan that contains ‘meaningful limits’ on director compensation.

However, the Delaware Supreme Court held in In re Investors Bancorp Stockholder Litigation in December 2017 that certain awards to directors are subject to an ‘entire fairness’ review rather than business judgment deference. Following Investors Bancorp, the business

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158 Id.
159 Id.
161 Id.
162 ‘2018 Say on Pay Results – End of Year Report’.
163 See, e.g., Calma v. Templeton, C.A. No. 9579-CB (Del. Ch. 30 April 2015); Seinfeld v. Slager, C.A. No. 6462-VCG (Del. Ch. 29 June 2012); In re 3COM Corp, C.A. No. 16721-VC (Del. Ch. 25 October 1999).
164 Seinfeld v. Slager, at *40.
165 In re Investors Bancorp Stockholder Litigation, C.A. No. 12327-VCS (Del. 19 December 2017).
Judgment rule will apply to judicial review of director compensation in Delaware only where directors submit specific compensation decisions for approval by fully informed and disinterested stockholders or where the stockholder-approved plan is self-executing and does not permit director discretion. Otherwise, directors must prove that their compensation is entirely fair to the company, which may require the support of peer-group data and analysis by independent consultants. However, where a shareholder-approved plan limit is reasonable, and where directors receive board approval to make grants to themselves within such limit, then it is possible that a board’s decision will continue to receive business judgment deference. Therefore, maintaining restrictive plan share limits that minimise director discretion will reduce the threat of shareholder litigation and maximise the chances of receiving business judgment review.

Notably, ISS has recently turned its focus to director compensation and revised its proxy voting guidelines to specifically address non-employee director compensation. Under ISS’s guidelines for 2019, ISS will make recommendations on a case-by-case basis and take into consideration qualitative factors such as the existence of a meaningful limit on director compensation and ownership as well as ownership and holding requirements for equity awards. Effective as of the 2020 proxy season, ISS has updated its methodology to identify pay outliers representing individual pay figures to directors above the top 2 to 3 per cent of all comparable directors within the same index or sector in both 2019 and 2020, followed by a qualitative evaluation of a company’s director pay practices. Relatedly, the number of proposals seeking shareholder ratification of director pay increased from one in 2017 to seven in 2018, with six such proposals receiving majority support.

**Looking ahead**

High levels of shareholder and proxy adviser involvement with SOP and SOGP votes indicate that boards of directors are increasingly restricted in their ability to set executives’ compensation. In addition, Delaware directors will now have their own compensation analysed under the more rigorous standard of *In re Investors Bancorp*, which aims to mitigate the conflicts of interest that arise when directors set their own pay, and will be subject to the

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166 Id. at 3.
169 Id.
172 Id.
increased focus of proxy advisory companies. Companies should continue to review their compensation and equity programmes (including those for directors) and carefully document compensation decisions, particularly in the context of acquisitions given the continuing impact of the SOP vote and the enhanced focus on director compensation.

Shareholders are also likely to continue exploring other avenues for influencing the pay practices of companies that are unresponsive to SOP votes and SOGP votes. Thus far, director reelection generally has been affected but not swayed by failed SOP votes, although shareholders increasingly express frustration over compensation practices by voting against reelection of directors, particularly those involved in compensation decisions.\(^{174}\) The practices identified as most troublesome by ISS and other proxy advisory firms will likely continue to disappear, and compensation, even with respect to perquisites and other fringe benefits, is expected to continue to shift away from cash-to-equity and performance-based awards under increasingly complex pay-for-performance programmes. It is unclear what effect the migration to equity and performance-based pay, coupled with the elimination of the performance-based compensation exception under Section 162(m) of the Code, will have on future M&A transactions. Given the market uncertainty surrounding recent changes in law and practice, investors should engage with management and boards of directors in the early stages of the acquisition process to maximise both executive retention and shareholder value.

VIII TAX LAW\(^{175}\)

Congress passed the TCJA at the end of 2017, and with it transformed the US tax system. The TCJA’s changes affect a significant number of rules that are relevant to US and cross-border M&A transactions, including those governing interest deductibility, bonus depreciation, net operating losses and the US international tax system.\(^{176}\) Notwithstanding the significance of the TCJA’s changes, however, the process behind it was rushed and chaotic, and left significant issues in the statute to be addressed by regulation. Throughout 2018 and early 2019, the Treasury Department released extensive regulatory guidance on topics related to the TCJA. We highlight two significant areas below.

i Tax on global intangible low-taxed income

One of the TCJA’s most significant changes is the introduction of a tax on global intangible low-taxed income (GILTI). Section 951A requires each US person (US shareholder) that owns at least 10 per cent of the stock of a controlled foreign corporation (CFC) to include in his or her income the US shareholder’s GILTI, which is calculated based on the income and loss of its CFCs. Mechanically, the calculation of a US shareholder’s GILTI inclusion is complex and can vary unexpectedly, because attributes of one CFC can interact with, and offset, the attributes of another CFC owned by the same US shareholder.


\(^{175}\) Section references in this part are to the Internal Revenue Code of 1986, as amended (Code), unless otherwise specified.

\(^{176}\) See, e.g., Section 163(j) (interest deductibility); Section 179 (bonus depreciation); Section 172 (net operating losses).
Because a US shareholder must include GILTI in income, it is taxed at the US shareholder’s regular tax rate. Corporate US shareholders, however, are entitled to a deduction that is intended to reduce GILTI’s effective rate to 10.5 per cent for taxable years prior to 2025, and 13.125 per cent thereafter. Corporate shareholders are also entitled to offset the inclusion by an 80 per cent credit for foreign taxes, subject to certain complicated limitations.

Given these complexities, what were once reasonably straightforward structuring decisions (e.g., making a Section 338 election) now frequently require considerable numerical analysis. Smart taxpayers will engage their tax advisers before making decisions that affect structure.

**Proposed regulations**

Notwithstanding the complexity of GILTI, the statute does not address many important questions about how the GILTI regime actually operates. In late 2018, the Treasury Department issued two sets of proposed regulations to address these questions, and we discuss certain issues raised by the proposed regulations below. Although these regulations remain in proposed form, they will apply retroactively if finalised.

**Net operating losses**

The GILTI rules permit losses from one CFC to offset the income of other CFCs held by the same US shareholder; generally, this ensures that a US shareholder will owe GILTI tax only if its CFCs are profitable overall. The statute, however, does not address whether those same losses can be carried forward to offset income in later tax years (or carried back to offset income from previous tax years). Practitioners generally believed that permitting some form of loss carry forward would be fair and consistent with the intent of the GILTI regime. Nevertheless, the proposed regulations provide that US shareholders cannot be carried back or forward for GILTI purposes.

**CFC basis reduction rule**

The proposed regulations add a new rule that requires US shareholders to reduce their basis in a CFC’s stock to the extent that the CFC had losses that offset the income of other CFCs held by the US shareholder. The calculation of this reduction is complicated but, critically, it occurs at the time the US shareholder disposes of its CFC stock. One consequence of this change is that US shareholders will frequently have more gain on the sale of a CFC than they thought, because their basis may be reduced unexpectedly as a result of this rule. The rule may also affect the desirability of certain US tax elections, including those under Section 338.

177 Section 250. The deduction may be carved back if the applicable US shareholder has net operating loss carry forwards.
178 Section 960; Section 904(d).
181 See NYSBA Tax Section Report No. 1394, at 34.
Consolidated groups

Another issue left open by the TCJA is the interaction of GILTI with the US consolidated group rules. Groups of commonly controlled US corporations can elect to file a consolidated federal tax return, which is intended to minimise the effect of the existence of the separate group entities on the group’s consolidated tax liability. Consistent with this rationale, commentators believed that the GILTI calculation should be performed at the consolidated group level, taking into account all of the CFCs held by group members.182 The proposed regulations adopt this approach, but also introduce complex rules that govern the basis consequences of offsetting income and loss for consolidated group members that own CFCs.

Partnerships

One implication of the GILTI rules is that foreign corporations held by US partnerships are treated as CFCs (and therefore create GILTI for the US partners of the partnership), even though the same entities would frequently not be CFCs if the partnership were foreign. This is a harsh result because partnerships are flow-through entities for US tax purposes: for this reason, commentators believed that it was inappropriate to have the application of the GILTI rules depend on whether the partnership was domestic or foreign. Indeed, the difference in treatment has led many taxpayers to convert US investment partnerships into foreign partnerships to avoid this result.

The proposed regulations do not resolve this issue, and instead further complicate the treatment of partnerships under the GILTI rules. On a high level, the new rules make the treatment of a partner dependent not only on whether a partnership is domestic or foreign, but also on whether the partner’s indirect ownership of the CFC is 10 per cent or more. Compliance with this approach may be very costly for domestic partnerships: in certain circumstances, the rules will require domestic partnerships to perform many individualised GILTI calculations for their US partners.

ii Dispositions of interests in partnerships with a US business

The TCJA made important changes to the taxation of foreign persons that dispose of an interest in a partnership that conducts business in the United States. Prior to the passage of the TCJA, it was settled law that, under the US rules governing effectively connected income (ECI), a foreign partner in a partnership conducting business in the United States would be taxed on its share of the ECI generated by the partnership’s activities. It was unclear, however, whether gain on the sale of an interest in that same partnership would also constitute ECI. The IRS position, set out in Revenue Ruling 91-32,183 was that a portion of the gain was ECI; this position ensured that the ECI consequences to a partner selling its partnership interest mirrored those of the partnership’s ordinary course business activities. Taxpayers frequently took the opposing view that the gain was not ECI, consistent with the general rule treating gain on the sale of a partnership interest as capital gain.184

The issue went unresolved until a taxpayer ultimately challenged the IRS’s position before the Tax Court in the 2017 case Grecian Magnesite, Mining, Industrial & Shipping Co.

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184 See Section 741.
In *Grecian Magnesite*, the Tax Court held that a foreign partner did not have ECI upon the redemption of its partnership interest, even though the taxpayer conceded that it would have been allocated ECI upon a sale of the partnership’s assets. In so holding, the Tax Court explicitly rejected Revenue Ruling 91-32, finding it so flawed that it ‘lack[ed] the power to persuade’.

The taxpayers’ victory in *Grecian Magnesite*, however, was short-lived. The TCJA overturned *Grecian Magnesite* by adopting Section 864(c)(8), which provides that gain on the sale of an interest in a partnership is ECI to the extent that the partner would have been allocated ECI on a deemed sale of the partnership’s assets. In addition, the TCJA introduced Section 1446(f), which imposes a new withholding tax in connection with the sale of a partnership interest if that sale results in ECI under the new Section 864(c)(8) rule. Notably, the withholding tax equals 10 per cent of the amount realised by the foreign partner (including the partner’s share of partnership liabilities). If the withholding tax applies, the transferee of the partnership interest is responsible for collecting it, although the partnership must also withhold on distributions to the transferee if the transferee fails to remit the tax.

**Proposed regulations**

Although the TCJA created a new withholding regime in adopting Section 1446(f), it offered taxpayers no guidance as to how to satisfy their withholding obligations. In May 2019, however, the Treasury Department released proposed regulations to flesh out new Section 1446(f). The regulations generally allow selling partners to avoid withholding if they provide an appropriate certification to the purchaser. The certification can take a number of different forms: for instance, it may address the seller’s status as a US person or the nature of the income and assets of the partnership. The proposed regulations also provide rules for collecting withholding tax on dispositions of interests in publicly traded partnerships.

**IX COMPETITION LAW**

In 2018, the Antitrust Division of the DOJ and the FTC (together, the agencies) carefully examined transactions in a variety of industries, including healthcare, entertainment and agriculture. The agencies continued to employ a rigorous approach to merger enforcement towards both proposed transactions and consummated mergers. Furthermore, the DOJ announced a number of new processes to streamline merger reviews.

Through both enforcement actions and statements from public officials, the agencies have continued to demonstrate a preference for structural remedies and a scepticism towards behavioural remedies. Agency officials have reasoned that structural remedies eliminate the

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185 149 T.C. 63 (2017).
186 Id.
187 The IRS did mitigate the disruption caused by the TCJA’s changes by suspending a portion of the new rules and allowing taxpayers to follow the related withholding rules under Section 1445 (pertaining to dispositions of interests in US real property) in the interim. See Notice 2018-08, 2018-7 I.R.B. 352 (29 December 2017); Notice 2018-29, 2018-16 I.R.B. 495 (2 April 2018).
188 See REG-105476-18, Federal Register Vol. 84, No. 92, 13 May 2019 at 21198-21225. The Treasury separately proposed regulations that address the calculation of the amount of ECI that is generated on the sale of a partnership interest under Section 864(c)(8). REG-113604-18, Federal Register Vol. 83, No. 247, 27 December 2018 at 66647-66655.
incentive and ability of merged companies to engage in harmful conduct while removing the necessity for monitoring of parties’ compliance with consent decrees. Of the 17 consent decrees entered into in 2018, the agencies required divestitures for 15 of the transactions. The remaining two consent decrees were issued by the FTC, and required behavioural remedies including implementing firewalls, instituting monitors and limiting the sharing of competitively sensitive information, among other conditions. As in previous years, the FTC increased the filing thresholds under the HSR Act. Under the new thresholds, the size of transaction test is satisfied for most transactions valued over US$90 million (increased from US$84.4 million).

In 2018, the agencies also took a few enforcement actions in connection with consent decrees that were entered in previous years. For example, in March 2018, the FTC modified its consent decree against CoreLogic, Inc concerning the company’s acquisition of DataQuick Information Systems, Inc in 2014. The FTC alleged that CoreLogic failed to adhere to the 2014 order’s condition that it provide all of the required data and information to the


divestiture buyer. Under the modified consent order, CoreLogic is required to provide bulk data to the divestiture buyer for an additional three years beyond the term of the original order and to adhere to certain quality metrics and service requirements. Similarly, in December 2018, the FTC approved an application by Teva Pharmaceuticals Industries Ltd to reopen and modify its decision and order concerning the merger of Watson Pharmaceuticals, Inc and Actavis, Inc in 2012. Under the previous decision and order, the merged company was required to divest a generic drug, supply it to Pfizer, Inc for no more than four years after the relaunch of the drug and assist with a technology transfer to a third party for manufacturing the drug. The drug was relaunched in 2015, and in 2016 Teva assumed the rights and obligations of Actavis through another acquisition. At Pfizer’s request, Teva sought to extend the supply agreement for an additional period since Pfizer had not yet completed the technology transfer.

The DOJ also announced and began the implementation of a number of processes to streamline the merger review process. In particular, in September 2018, Assistant Attorney General Makan Delrahim announced that the DOJ had set a goal to resolve most merger investigations within six months, provided that the parties to a merger promptly comply with DOJ requests throughout the review period. The DOJ has since published a model voluntary request letter, which seeks information from parties during the initial 30-day waiting period, and a revised model timing agreement, which governs the longer Second Request review process, on its website. The DOJ has stated that its model timing agreement is designed to speed the merger review process by providing for fewer custodians whose documents must be searched as part of the Second Request, fewer depositions and a shorter time period for the DOJ to complete its review following the parties’ certification of substantial compliance with a Second Request. In exchange, the DOJ expects parties to provide faster and earlier productions of documents, and for data and to be forthcoming and accurate about privilege issues in the parties’ document production.

Some recent, significant DOJ and FTC actions are described below.

194 Id.
195 Id.
197 Id.
198 Id.
199 Id.
202 Id.
203 Id.
i  **DOJ**

**Bayer/Monsanto**

In September 2016, Bayer AG (Bayer) announced that it would acquire Monsanto Company (Monsanto) in a transaction valued at US$66 billion. The DOJ approved the transaction in May 2018 subject to divestitures of certain businesses and assets totalling US$9 billion, the largest negotiated merger divestiture ever required by the agencies. The DOJ alleged that without the divestiture, the transaction, which combined two of the largest agricultural companies, would have resulted in higher prices for farmers, and by extension consumers, and would have stifled innovation in the industry. Under the consent decree, Bayer was required to divest its businesses that competed with Monsanto, including its cotton, soybean, canola, vegetable seed and herbicide businesses. The consent decree also required a number of other divestitures related to the parties’ seed treatment businesses, intellectual property and research capabilities, including pipeline R&D projects, and assets that would provide the divestiture buyer with similar innovation incentives, capabilities and scale.

**Disney/Fox**

In December 2017, The Walt Disney Company (Disney) announced it would acquire Twenty-First Century Fox, Inc (Fox); the parties subsequently announced they had signed an amended agreement valued at US$71.3 billion in June 2018, following a bidding war with Comcast for Fox. Shortly thereafter, the DOJ approved the transaction subject to divestitures, alleging the parties competed to sell cable sports programming licences to multichannel video programming distributors (MVPDs) in several local markets, and that as a result of the proposed transaction, MVPDs would face increased prices. Under the consent decree, Disney was required to divest Fox’s 22 regional sports networks. The transaction was completed in March 2019.

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206 Id.

207 Id.

208 Id.


210 Id.

211 Id.

CVS/Aetna

In December 2017, CVS Health announced it would acquire Aetna, Inc in a transaction valued at US$69 billion.\textsuperscript{213} In October 2018, the DOJ approved the transaction subject to Aetna’s divestiture of its Medicare Part D prescription drug plan for individuals business.\textsuperscript{214} The consent decree also required that Aetna assist the divestiture buyer with operating the plan during the transition period.\textsuperscript{215} The DOJ reasoned that without the divestiture, the combined company would result in increased prices, decreased innovation and decreased quality service in 16 Medicare Part D regions.\textsuperscript{216} The parties completed the transaction in November 2018.\textsuperscript{217}

\textbf{FTC}

Northrop Grumman/Orbital ATK

Despite the agencies’ stated preference for structural remedies, in June 2018, the FTC utilised behavioural remedies in its consent decree concerning Northrop Grumman Corp’s acquisition of Orbital ATK, Inc.\textsuperscript{218} The transaction, which was announced in September 2017, was valued at US$9.2 billion.\textsuperscript{219} The FTC reasoned that because the defence industry only has the one buyer, the Department of Defense (DoD), it would allow the acquisition subject to certain conditions. Specifically, the consent decree required Northrop Grumman to supply solid rocket motors to competitors on a non-discriminatory basis, separate its solid rocket motors business via a firewall and allow the DoD to monitor its compliance with the order.\textsuperscript{220} The parties completed the transaction in June 2018.\textsuperscript{221}


\textsuperscript{215} Id.

\textsuperscript{216} Id.


Tronox/Cristal
In February 2017, Tronox Limited announced it had reached a definite agreement to acquire Titanium Dioxide (TiO₂) business from Cristal in an acquisition valued at US$1.7 billion.²²² The FTC challenged the proposed transaction at the end of 2017 by filing an administrative complaint and then subsequently seeking a preliminary injunction in federal district court.²²³ The FTC alleged that the acquisition would substantially lessen competition in the North American market for chloride process TiO₂ and would increase the risk of both coordination among competitors and anticompetitive strategic output reductions by Tronox in the future.²²⁴ In September 2018, the court granted a preliminary injunction.²²⁵ Following this decision, in December 2018 an administrative law judge issued an initial decision upholding the complaint and requiring the parties to terminate the proposed transaction.²²⁶ Tronox ultimately reached a settlement agreement with the FTC in April 2019. Under the proposed consent decree, Tronox was required to divest Cristal's North American TiO₂ business to INEOS.²²⁷

Ottobock/FIH Group Holdings
In September 2017, Otto Bock HealthCare North America, Inc (Ottobock) acquired FIH Group Holdings, LLC, the owner of Freedom Innovations, in a transaction that was not reportable under the HSR Act.²²⁸ The FTC issued an administrative complaint against Ottobock in December 2017, alleging the transaction harmed competition in the US microprocessor prosthetic knees market by eliminating a significant competitor.²²⁹ While Ottobock had taken steps to integrate the Freedom Innovations business, it subsequently agreed to hold the business separate pending the FTC litigation.²³⁰ In April 2019, an

²²⁴ Id.
²²⁶ Id.
³º Id.
administrative law judge upheld the FTC’s administrative complaint. The judge also issued an order that requires Ottobock to divest FIH Group Holding to an approved buyer within 90 days of the order being final.

iii Conclusion

The DOJ and FTC have continued to engage in active enforcement, demonstrating a willingness to challenge both proposed and consummated transactions, engage in litigation where necessary and require significant remedies where they believe these are necessary to preserve competition.

X OUTLOOK

In 2018, US M&A activity increased in value, but decreased in volume, recovering from two years of declining deal values. Delaware courts continued to be deferential to corporate boards of directors, further reinforcing deal price as the starting point for fair value in appraisal actions. In terms of cross-border M&A, CFIUS review presented an increasingly significant obstacle, particularly for Chinese acquirers. Energy and power was the leading US M&A sector, driven in part by the increasing prevalence of combinations of technology companies with non-technology companies. Shareholder activism continued to exert significant influence, although the attacks on large-cap companies has subsided somewhat. As in 2017, all-cash transactions by strategic buyers were the norm, supported by robust financing opportunities. Antitrust enforcement continued to be aggressive. Finally, in light of the CFIUS developments, and the myriad of other dynamic forces that shape the US M&A landscape, it remains to be seen how M&A activity will progress for the remainder of 2019.


232 Id.
I OVERVIEW OF M&A ACTIVITY

During 2018, M&A activity in Venezuela was not very significant, apart from the very few implementations in Venezuela of international acquisitions between multinational conglomerates.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Although the Venezuelan Code of Commerce does not define mergers, Articles 343 to 346 provide the registration and publication requirements that must be complied with for a merger to become effective; specifically, each entity must notify the respective mercantile registry (attaching the merging entities’ balance sheets) to record the merger agreement. Additionally, the Code states that a merger will not become effective until a waiting period of 90 days has elapsed counted from the date of publication of the merger resolution and its registration data.

With respect to acquisitions, these can be divided into two kinds.

i Acquisition of shares

As per Article 296 of the Code of Commerce, the transfer of ownership of shares is accomplished by the execution of the respective transfer entry in the company’s share registry book by the transferor and the transferee. Moreover, a review of the articles of incorporation of the company whose shares are being transferred must be conducted, as the company may have preferential rights granted to other shareholders.

In addition to the Code of Commerce, there are certain statutes that are relevant to the acquisition of shares, such as the Security Markets Law and the rules issued by virtue of said Law for shares that are publicly traded. Additionally, the Law to Promote and Protect the Exercise of Free Competition is applicable in cases where, inter alia, the acquisition could produce an economic concentration.

With regards to acquisitions of shares in areas such as telecommunications and banking, previous authorisation or clearance may be needed, depending on the pertinent statute.

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1 Guillermo de la Rosa Stolk, Juan Domingo Alfonzo Paradisi and Valmy Díaz Ibarra are senior partners and Domingo Piscitelli Nevola is an associate at Torres, Plaz & Araujo.
ii Acquisition of assets
Depending on the type of assets, different requirements must be met:

Real estate
The provisions of the Venezuela Civil Code and the pertinent statute that establishes and organises the public registry system shall be applicable. Therefore, for a transfer of ownership of real estate to be effective before third parties, registration of the deed of transfer at the public registry office that has jurisdiction over the aforementioned property must be made.

Movable goods or chattel property
Requirements will depend on the type of good or asset.

If a transaction comprises the transfer of ownership of a business by the disposal of chattel property and the transferee wishes to avoid joint liability for the business obligations of the transferor, then the provisions of Articles 151 and 152 of the Code of Commerce shall be applicable; such provisions contain the obligation for three notifications to be published in a local newspaper announcing the disposal of the ownership of a business.

If the transaction involves intangible assets such as intellectual or industrial property, then registration at the competent registry office must be made for the transfer to become effective before third parties.

In general, all the aforementioned transactions could have tax consequences, which will be explained in Section VIII.

III FOREIGN INVOLVEMENT IN M&A TRANSACTIONS
According to governmental sources, investment was the product of strategic alliances between Venezuela and Argentina, Belarus, China, Cuba, Spain, France, Iran, Japan, Portugal and Vietnam. The economic sectors that were recipients of investment include manufacturing, telecommunications, automobiles, petroleum and infrastructure (construction). The aforementioned investments were the product of associations between entities from those foreign countries and the Venezuelan government, and also between non-governmental entities of the respective foreign country and Venezuela.

Additionally, the world economic crisis – together with the country’s risk factors – continue to have an impact on the investment and profitability levels of multinational entities operating in Venezuela, which have implemented budget cuts and reviewed their investment programmes.

IV SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES
In developing its policy to become the leader in the food industry and marketing chain, between 2002 and 2012 the government announced the acquisition of almost 1,200 companies. Most of those companies are still in the process of nationalisation.

2 The conveyance of property or goods must result in the cessation of the business activities of the transferor that were carried out within its premises.
V Financing of M&A: Main Sources and Developments

There have not been any new relevant ways of financing acquisitions made by the state; its primary source has been revenue from the sale of oil and from the placement of debt instruments.

VI Employment Law

In connection with the merger of companies in Venezuela and also with the acquisition of businesses, it is worth bearing in mind from a labour relations point of view that such negotiations will have several consequences for a company’s employees, as follows. In May 2012, a new Organic Labour and Employees Law was published that establishes the following.

i Employer substitution

Article 66 of the Organic Labour Law provides: ‘There will be an employer substitution when the property, ownership or the running operation of a company is transferred for any reason, from a natural or juridical person to another, and the operation of the company continues.’ In the same manner, Article 68 of the Law provides:

Substitution of the employer will not affect existing work relationships. The substituted employer will be jointly responsible, with the new employer, for obligations derived from the Law or from contracts in effect prior to the substitution and until expiration of the prescription period provided for in Article 61 of this Law.

Upon termination of this period, only the new employer’s responsibility will subsist, unless previous labour suits exist, in which case the final judgment shall be executed indistinctly against the substituted owner or against the substitute. The responsibility of the substituted employer will only subsist, in this case, for five years as of the date on which a definite sentence has been declared.

Article 32 of the Organic Labour Law Regulation states:

The transfer or assignment of the worker is verified when the employer agrees or requires the worker to render his services on a permanent basis under the dependency of and on account of another, with the consent of the latter. The worker transfer or assignment shall be subject to the employer substitution regime and will produce the same effects.

On the other hand, by motion of Justice Dr Omar Mora Díaz, the Social Court of Appeal of the Supreme Court of Justice, in his decision issued on 19 September 2001, in the lawsuit brought by R Cameron against Compañía Occidental de Hidrocarburos, Inc, published in Ramírez y Garay, Book CLXXX, September 2001, stated ‘[T]his Social Court of Appeal before deciding on the appropriateness of the accusation, wishes to make, in the first place, some considerations regarding the form known as employer substitution’.

In fact, Dr Rafael Alfonzo Guzmán, in his book *Estudio Analítico de la Ley del Trabajo Venezolana*, mentions the point in question with the following considerations:

There is a substitution of employer when the owner or holder of a company, establishment, running operation or work, transfers his rights to another natural or juridical person who continues the same economic activity or, at least, continues it without substantial changes.
Mario de la Cueva states that for the employer substitution to take effect, it is not enough to sell the products of the negotiation or part of the machinery, utensils or equipment: it is necessary to transfer them to the company as an economic–juridical unit or part of the company itself, which in turn constitutes an economic–juridical unit; in the first case, the employer's substitution is total. In the second case, it only works with respect to workers who provide their services in a branch or the transferred premises.

From the above, it is evident that there may exist two types of employer substitution as provided for in the Mexican doctrine, which has been influential on the Venezuelan Labour Law. These are on the one hand total substitution, which materialises when a company itself is transferred as an economic–juridical unit, and on the other, the company itself that in turn constitutes an economic unit.

In applying such criteria to the case under study, we may determine that what the defendant showed is that there was an employer substitution, which opinion was shared by the court, since, as can be seen from the records, on being transferred to Venezuela, the defendant continued to provide his services to a branch of the company domiciled in the United States, evidencing the continuity of the labour relationship.

By virtue of the foregoing, it is evident that when the transfer of an employee from one company takes place, because the company merges and the business continues to operate, there is what the law, the doctrine and the jurisprudence have defined an employer substitution.

ii Effects of an employer substitution

An employer substitution is intended to maintain stability for the workers. Therefore, the existing labour relations are not affected, and thus the workers are entitled to continue receiving all legal and contractual benefits that they were already receiving.

In fact, when an employer substitution takes effect and the existing labour contracts are not affected, the transferred workers shall enjoy the benefits and conditions that they were enjoying when they worked for the former company: that is, all the legal and contractual benefits to which they were entitled. In the same manner, the new employer shall be responsible for all the benefits, fringe benefits and indemnities that may be due to the workers who now provide their services to the substituted employer from the beginning of the labour relationship.

On the other hand, it is important to point out that pursuant to the provisions of Article 70 of the Organic Labour and Employees Law, assuming that workers receive some payment on account of fringe benefits or indemnities due to the employer substitution, and continue to provide their services, the payment received will be considered an advance of the payment to which they are entitled upon the termination of the labour relationship.

VII TAX LAW

i Income tax

Under the Venezuelan tax framework, particularly under the Decree with Rank, Value and Force of the Master Tax Code (MTC) and the Decree with Rank, Value and Force of Partial Reform of the Decree with Rank Value and Force of the Income Tax Law (ITL), in the scenario of a statutory merger, any outstanding benefits (attributes) or liabilities remain with the surviving company regardless of whether the merger is carried out as an incorporation or absorption merger.
According to Article 24 of the MTC\(^3\) and Paragraph 5, Article 16 of the ITL,\(^4\) for income tax purposes, the subsisting entity will assume all the liabilities and benefits of the merged entity, as well as future liabilities and benefits, including income tax credits (ITCs), which may arise after the merger becomes effective, all of which are based on activities carried out prior to such merger.

The surviving company would be in a position to use all the tax attributes that will be used in the absorbed entity, including, but not limited to, ITCs, net operating losses (NOLs) as applicable, other tax losses (i.e., losses resulting from the adjustment per inflation (API) system, where applicable), and other tax credits such as those resulting from excess withholding (i.e., taxes paid in excess in prior fiscal years), input VAT (tax credits) and VAT withholding.

In a merger by absorption, from a fiscal standpoint, the fixed assets and liabilities of the merged company maintain their tax cost basis (including revaluation for inflation where applicable), that is, tax basis carryover. In this regard, such assets and liabilities may be restated for inflation at the first fiscal year-end following the date on which the merger took place. Non-monetary items would be adjusted for inflation from the date of the merger as applicable. As a result, no major effect arises with regards to adjustment for fiscal inflation of fixed assets, as these maintain the same date of acquisition, historical costs and restated values they held in the books of the merged company.

A merger by absorption interrupts the current fiscal year and begins a new fiscal year for the combined operations of the merging companies. Therefore, the merged company must file its income tax return for the fiscal year in which it performed individual operations within the three months immediately following the cessation of its activities in accordance with Articles 146\(^5\) and 150\(^6\) of the ITL Regulations. This final year may be shorter than 12 months, and could further cut short the carryover term for attributes (i.e., three fiscal years for ITCs and NOLs and one year for losses pursuant to API, as applicable). The surviving entity must notify the Tax Administration of the transaction under Articles 35.4\(^7\) and 155.6 of the MTC.\(^8\)

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3 Article 24 MTC: ‘In the case of mergers, the company that subsists or that is created from the original one(s) will assume any tax benefit or responsibility that corresponds to the merged company(ies).’

4 Article 16 Paragraph 5 ITL: ‘For tax purposes, any tax benefit or liability corresponding to merged companies shall subsist for the company resulting from the merger, notwithstanding the rights and obligations of the merged companies.’

5 Article 146 ITL Regulations: ‘Definitive income tax return will be presented within the three (3) months following to the completion of the taxable period of the taxpayer without prejudice to the prorogations granted by the Tax Authorities.’

6 Article 150 ITL Regulations: ‘In case of legal entities or communities who ceased their business by sale, exchange, cession of their assets, business or commerce fund, merger or any other cause different from the dissolution, the tax period will be finished the day of cessation.’

7 Article 35 MTC: ‘The Taxpayers have the obligation to inform the Tax Administration, within a period not exceeding one (1) month, the following facts: [. . .] ’4 Cessation, suspension or paralysation of the Taxpayer’s regular economic activity. ‘

8 Article 145 MTC: ‘The Taxpayers, persons in charge and third persons are compelled to fulfil the formal duties related to the control tasks and investigation made by the Tax Authorities and especially, must: [. . .] ’6 Communicate any change in the situation that could originate on their tax responsibility, specially when the charge is related to the beginning or ending of activities of the taxpayer.’
ii Other taxes (stamp tax and real property tax)

The registration of acts and documents with the civil law registry office or the commercial registry office is subject to registration tax.

Real estate transfer taxes are due and payable by the transferring company upon the transfer of assets from the target company to the acquiring company. Normally, upon the registration of purchase–sale documents for real property and any other events, a 1 per cent fee on the value of the property must be paid.

In the case of a sale of real property to a third party, the 1 per cent payment would apply, in addition to a 0.5 per cent withholding prepayment, in either cash or credit form, for income tax determined on the sale price. This prepayment shall be credited to the income tax amount resulting from the final income tax return of the year.

iii Value added tax

The VAT Law provides that sales of tangible goods, including any part of their property rights as well as withdrawals or retirements of movable goods by taxpayers, are subject to VAT. However, sales of intangible goods, such as fiscal rights, stocks, bonds, mortgage bonds, mercantile effects, and other securities and personal goods in general that represent money, credit, or rights other than property rights over tangible goods, are not subject to VAT.

As a general rule, under the Venezuelan VAT legal framework, in the case of a merger, the property transferred (i.e., movable property) qualifies as a sale operation and constitutes a taxable event for VAT purposes under Article 3.1 of the VAT Law in accordance with Article 10.5 of the VAT Law’s Regulations.10

However, the VAT Law’s Regulations (Article 10.5) state that if the surviving company carries on with the same purpose or activities that the dissolving companies pursued, wholly or partially, it should not be deemed that there has been a transfer of ownership of corporate goods attributable to a sale for VAT purposes, and hence no taxes should be applicable.

Finally, the surviving company would be in a position to use all of the VAT tax credits that will be used in the absorbed entity, including those resulting from excess VAT withholding (i.e., taxes paid in excess in prior fiscal years) and input VAT (tax credits) under Article 41 of the VAT Law.11

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9 Article 3 VAT Law: ‘For the purposes hereof, the following activities, legal transactions or operations shall constitute taxable events: ‘Sale of tangible movable property, including aliquot parts on the property right on such property, and the retirement or disincorporation of movable goods by the taxpayer of this tax.’

10 Article 10 VAT Law’s Regulations: ‘For the purposes of this tax, sale is considered, among others, the following acts and contracts that deal with onerous transfers of real personal domain of an aliquot of property rights over them: [. . .] ‘5 Contributions or act to transferring rights to assets for the establishment, expansion, modification, merger, takeover or the other similar, with respect of companies or legal entities or economic. In any case, if the new companies emerged continue the same line of activities of the predecessor companies, whether in whole or in part, it should not be deemed that there had been an act, transaction or transfer of ownership of corporate goods attributable to a sale for purposes relating to the application of this tax, unless an increase in the capital take place through contributions of new movable property.’

11 Article 41 VAT: ‘The right to deduce the tax credit from the tax debits is individual for each ordinary taxpayer and it not be assigned to third parties, except for the case indicated in Article 43 or when it is a merger or take over of companies, in which case, the resulting partnership of said merger shall enjoy the remaining tax credit that corresponded to the companies that formed part of such fusion.’
iv Municipal tax (tax on industrial, commercial and services activities)
In Venezuela, a municipal tax is applicable to all industrial, commercial and service activities (except professional services) performed in the territory of a municipality. The taxable base is the turnover (gross proceeds) received by the taxpayer and arising from the activity performed in the locality. Tax rates vary from locality to locality and range from 0.5 to 5 per cent. It is usually paid and a return filed yearly.

Regarding municipal tax on industrial, commercial and services activities, an absorbed company must notify the relevant municipal tax authorities of the suspension (or termination) of its activities in the municipality where it conducted its activities in accordance with Articles 35.4 and 155.6 of the MTC, and pay any debt owed to the municipal tax authorities. Municipal tax rates vary depending on the municipality in which the business was conducted.

The surviving company shall request a business licence to incorporate new activities (if any) and to carry out the activities of the absorbed company within the jurisdiction of the municipality in which the surviving company operates.

v Science and technology contribution
A science and technology contribution is provided for in the recent amendment to the Organic Law of Science and Technology, which applies to entities defined in the law as large ventures (companies with a turnover of 100,000 tax units or more).

The contribution amounts to 2 per cent of turnover (gross proceeds) for entities engaged in the manufacturing or commercialisation of alcohol and spirits, as well as tobacco and tobacco products. Gambling activities are subject to a similar rate. Hydrocarbon and mining activities, when carried out by private parties, are taxed at a rate of 1 per cent on turnover. When these activities are carried out by entities in which capital is considered public capital (i.e., wholly or partially state-owned, but controlled by the state), then the same are taxed at a rate of 0.5 per cent of turnover; any other industry or commercial activities (i.e., general activities) are subject to the latter 0.5 per cent rate on their turnover.

Regarding the science and technology contribution, an absorbed company must notify the relevant tax authorities of the special science and technology fund, Fonacit, about the suspension (or termination) of its activities in accordance with Article 155.6 of the MTC, and pay any debt owed to Fonacit.

vi Anti-drug enforcement contribution
A contribution for the purposes of illegal drug enforcement and education is provided for, computed at a rate of 1 per cent on the net earnings of the relevant taxpayers engaged in commercial, industrial or services activities; for those taxpayers engaged in manufacturing spirits and liquor, and cigarettes and tobacco, a 2 per cent contribution on their net earnings applies. The tax basis is net earnings (accounting income before taxes) as per the Venezuelan generally accepted accounting principles (GAAP) and as per the regulations (Provisions 006-2011 and 007-2011 of March and May 2011).

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12 Article 155 MTC: ‘The taxpayers, person in charge and third persons are compelled to fulfil the formal duties related to the control and investigation made by the Tax Authorities and, especially, they must: [. . .] 6 Communicate any charge in the situation that could originate alterations on their tax responsibility, especially when the change is related to the beginning or ending of activities of the taxpayer.’
A new anti-drug enforcement law, the Organic Law of Drugs, was passed in November 2010 and covers the relevant contributions in Articles 32 and 34. These contributions are paid into a special fund, FONA, created for that purpose, and are used for projects identified in the law, which may include reinvestment (up to 40 per cent) in approved activities or projects regarding payors and payors’ employees (Provision 0001-2011).

Regarding the anti-drug enforcement contribution, an absorbed company must notify the relevant tax authorities of the FONA of the suspension (or termination) of its activities in accordance with Article 155.6 of the MTC, and pay any debt owed to FONA.

**vii  Sport contribution**

A contribution for the purposes of funding a special fund – the National Fund for the Development of Sport, Physical Activity and Physical Education – was established in the Sport Law passed in August 2011.

The contribution under the Sport Law arises upon the exercise in Venezuela of any commercial, industrial or services activity by any person (inter alia, individuals, companies, partnerships) resulting in net earnings in a given year in excess of 20,000 tax units, and is computed as 1 per cent of the net earnings of the relevant taxpayers.

The tax basis is net earnings (accounting income before taxes) as per Venezuelan GAAP, as identified in Regulation No. 1 of the Law. The contribution may be paid in cash in full, or part of the same may be used for projects identified in the Law and approved by the National Sports Institute, which may include reinvestment (up to 50 per cent) in approved activities or projects for payor and payor employees.\(^\text{13}\)

Regarding the sport contribution, an absorbed company must notify to the relevant tax authorities of the National Fund for the Development of Sport, Physical Activity and Physical Education of the suspension (or termination) of its activities in accordance with Article 155.6 of the MTC, and pay any debt owed to such authorities.

**VIII  COMPETITION LAW**

The Venezuelan legal framework in terms of economic concentrations (mergers and acquisitions) in the field of the analysis of competition is based on Article 113 of the Venezuelan Constitution, which establishes an express prohibition on monopolies. Specifically, any acts, activities, behaviours or agreements between private parties that are intended to establish monopolies are declared unconstitutional.

**i  Rules pertaining to economic concentrations in the field of antitrust laws**

From the viewpoint of competition, the following norms contain all regulation existing in Venezuela, starting with the Free Competition Promotion and Protection Law, published in Official Gazette No. 34,880, dated 13 January 1992, which was derogated by the Decree with Rank, Value and Force of Antitrust Law, published in Gazette Extraordinary No. 6,151, dated 18 November 2014.

To ensure the correct application of the Decree Law, the Superintendency of Antitrust was created as the public institution in charge of applying the law, with functional autonomy in the matters within its jurisdiction and administratively managed by the ministry with
jurisdiction over matters of internal commerce. All administrative proceedings culminate in decisions of the Superintendency. They may be appealed through judicial proceedings, at the contentious administrative courts at first instance, and through second instance appeals to the Supreme Court.

Under Chapter II of the Decree Law, the following are prohibited: all economic concentrations that produce or reinforce a dominant position in all or part of the market, that may cause adverse effects to effective competition, or that may cause democratisation in the production, distribution and marketing of goods and services. Nevertheless, small and medium-sized companies, and cooperatives that are covered by the system of communal economy are exempted. The procedures of evaluation and approval will be established by the regulation of this Decree Law. The Decree Law on Antitrust states that the procedures for the notification, evaluation and approval of economic concentrations shall be established in regulations that have not yet been published.

Furthermore, Instruction No. 3 regarding Economic Concentration Operations, published in Official Gazette No. 36,209 (Instruction No. 3), dated 20 May 1997, contains the information required by the Superintendency for the authorisation of an economic concentration operation. Prior notification of an economic concentration operation is not mandatory under the current laws: it is voluntary for those concerned. This does not preclude the Superintendency from opening an investigation once an operation is declared certain to determine whether it could have a negative impact on free competition. The Superintendency of Antitrust has up to one year to conduct such investigation, as of the date on which the economic concentration operation is actually closed.

Moreover, in Venezuela there are no exceptions regarding the economic activity or sector in which the economic agents are involved. Therefore, both profit and non-profit private and public economic agents engaged in economic activities inside the national territory or in operations with effects on the national market are subject to the regulations governing matters of economic concentrations.

A resolution by Procompetencia (which was the institution that was in charge of applying the law before the Superintendency of Antitrust) No. 2451, dated 11 July 1996, published in Official Gazette No. 36,000, dated 15 July 1996, establishes, based on Article 2 of Regulation No. 2 of the Free Competition Promotion and Protection Law (Regulation No. 2), the minimum limits that shall apply to economic concentration operations subject to antitrust laws. These include when the overall volume of the business of the companies involved in the economic concentration operation is greater than 120,000 tax units, and when the merging companies involve divisions from several companies where the overall volume of business of the divisions participating in the operation shall be taken into consideration.

Additionally, the Decree with Rank, Value and Force of Organic Law of Fair Prices (Organic Law of Fair Prices), published in Official Gazette No. 40,787 and dated 12 November 2015, establishes similar provisions to those established in the repealed Free Competition Promotion and Protection Law. Among those provisions, Article 53 provides for the crime known as boycotting in the following terms:

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14 At the time of writing, the value of the tax unit is 50 bolivares.
Those who jointly or separately develop or carry out actions, or incur in omissions that directly or indirectly prevent the production, import, storage, transportation, distribution, and commercialization of goods, as well as the rendering of services, shall be punished with prison of twelve (12) to fifteen (15) years. When said actions or omissions have been committed in detriment of the public patrimony, the assets shall also be subject to confiscation, in accordance with the provisions of the Constitution of the Bolivarian Republic of Venezuela.

Likewise, they will be sanctioned with the temporary occupation of the establishment up to one hundred and eighty (180) days extendable for a single time.

In addition to the above, Article 70 of the Organic Law of Fair Prices states that the National Superintendency for the Defence of Socioeconomic Rights (SUNDDE) may adopt and execute preventive measures if, during the inspection of any stage of the administrative procedure, there are indications of non-compliance with the obligations set forth in the Organic Law. Such measures may consist of:

a. the preventive seizure of goods;
b. the temporary occupation of establishments or essential goods for the development of an activity;
c. the temporary closure of an establishment;
d. the temporary suspension of licences, permits or authorisations issued by the SUNDDE;
e. the immediate adjustment of the prices of the goods to be marketed or services to be provided, in accordance with those established by the SUNDDE; or
f. all those measures that are necessary to protect the rights of citizens as under the Organic Law.

Moreover, the Organic Law provides that in cases where temporary occupation is dictated, such measure will last up to 180 days, and will ensure the operationality and use of such establishment or local vehicle by the SUNDDE.

Recently, the SUNDDE issued a temporary occupation preventive measure for 90 days for a site, administrative offices, and establishments and property owned by a renowned wood and chip-making company for allegedly committing the crime of boycotting. The SUNDDE also found that an estranged citizen had been appointed to the company as the head of the pro tempore administration board. Subsequently, this citizen, in his capacity as head of the pro tempore administration board, was named president in charge of the company, and proceeded to appoint a director of legal affairs and a finance director of the aforementioned board.

The case was brought to the Venezuelan courts, and on 12 December 2018, the First Contentious Administrative Court issued judgment No. 2018-0501, under which a claim for annulment made by the company against the measure of temporary occupation issued by the SUNDDE was provisionally admitted, and a precautionary amparo action was declared appropriate based on the violation of the constitutional economic rights of the company, since the preventive measure that materialised seemed more an administrative intervention rather than a temporary occupation, as stated in Article 70 of the Organic Law of Fair Prices. On 19 March 2019, a ratification and extension of the sentence handed down by the Court was obtained.15

15 The aforementioned case has been brought by Torres, Plaz & Araujo.
Economic concentration modalities according to Regulation No. 2

Mergers among independent companies include:

a. the incorporation of a company where the resulting company acts permanently as an independent company;

b. operations whereby one or more companies acquire control of one or more companies that were independent, or parts of those companies; and

c. acquisitions of production assets, going concerns, and any other act or contract whereby companies, divisions or parts of companies are concentrated.

In addition, Chapter II of Regulation No. 2 establishes the procedure for the prior evaluation of an economic concentration operation for its authorisation by the Superintendency. Considering that the prior notification system is voluntary, there are no limitations for making such notification, and there are no penalties in the event of such notification not being made. According to the provisions of Article 6 of Regulation No. 2 to the Law, the process for requesting a prior evaluation does not prevent an economic concentration operation from following its natural course and even taking place before a decision is obtained from the Superintendency, notwithstanding whatever is ultimately indicated.

Procedures

Prior authorisation procedures are governed by the provisions of Chapter I of Title III of the Organic Administrative Procedure Law as regards ordinary proceedings.

The penalty procedure is governed by the provisions of Title V, Chapter I, Articles 43 et seq. of the Decree with Rank, Value and Force of Antitrust Law when, once an economic concentration has taken place, it is presumed that it could have anticompetitive effects or create or strengthen a dominant position on the market.

Terms

The ordinary proceeding contained in the Organic Administrative Procedure Law establishes a term of four months from the time that the request for a prior evaluation is formally presented. This term may be extended for another two months if necessary, depending on the complexity of the study.

During this proceeding, the Superintendency receives all the information for its opening contained in Instruction No. 3 from each party involved in the proceeding. It may later send questionnaires to independent third parties, whether they are competitors or are located at another level of the chain, to complete the information required to determine the dynamics of the market.

If necessary, the evaluating agency may require additional information or clarification of information from the parties for its final decision.

The term established for the substantiation of the penalty procedure is 15 business days, which term is extendible for another 15 business days. The file then enters the decision stage, which lasts 30 business days with the possibility of being extended for an additional three days (in other words, the minimum term for the penalty procedure is 45 business days).
v Sectoral regulations

Public companies

Merger operations of capital market companies must be informed to, and gain the prior approval of, the National Exchange Superintendency. Likewise, economic concentration operations among companies participating in the capital markets are also subject to the Decree with Rank, Value and Force of Antitrust Law. Although a request for prior evaluation is voluntary, the Superintendency may investigate an operation when it suspects that it could have restrictive effects on competition or could create or strengthen a dominant position on the market.

Banking

Economic concentration operations in the banking sector require the prior approval of the Superintendency of Banks and Other Financial Institutions. Additionally, a request for the prior evaluation of this type of institution is voluntary in the area of antitrust law; once notified, such institution may be subject to investigation and penalties imposed by the Superintendency.

Insurance

Transfers of portfolios, mergers or split operations of insurance and reinsurance companies require the prior approval of the Superintendency of Insurance Activity once it has heard the Antitrust Superintendency's opinion, which has binding character.

Consequences and penalties

The Decree Law establishes that those who engage in prohibited practices or acts described in Chapter II shall be punished by the Superintendency with a fine of up to 10 per cent of the value of their gross annual revenue if there are mitigating circumstances. If aggravating circumstances attend an offender's conduct, that amount may be increased to 20 per cent. In cases of recidivism, the fine will be increased to 40 per cent as a general penalty. Furthermore, the Decree Law states that the notification, evaluation and approval procedures for economic concentrations shall be established in regulations that have not yet been published.

However, under Instruction No. 3 there are no penalties for not requesting a prior authorisation for economic concentration operations, as such request is voluntary.

In the case of prior evaluations, the Superintendency may recommend the modification of some of the conditions of the economic concentration operation to minimise any anticompetitive effect that could derive from the evaluation, or recommend divestment in part of the market.

If the parties do not accept the observations of the Superintendency, it may open, once the economic operation takes place, a penalty procedure for presumptive anticompetitive effects, which could include the following: full or partial divestment of the economic concentration operation; other orders of lesser magnitude, such as the modification of territories, exclusive rights in the distribution of products or in the purchase of inputs, or non-compete clauses; or a fine of up to 20 per cent of the aggregate gross sales of the parties involved in the operation.
Finally, the Superintendency of Antitrust has not issued any resolution about economic concentrations under the terms of this new Decree Law, and the procedures for evaluation and approval will be established by the regulation of this Decree Law, which is pending publication.

IX OUTLOOK
In view of the global and national economic crisis, it is expected that the Venezuelan economy will have somewhere between very moderate or no growth during 2019. Moreover, it is expected that if foreign private investments are made, they will be derived from bilateral cooperation agreements and mainly in the construction, oil, gas and mining sectors.
I OVERVIEW OF M&A ACTIVITY

According to the 2018 Annual Report of the Ministry of Planning and Investment,² there were a total of 6,496 acquisition and subscription deals by foreign investors registered nationwide with a total value of US$9.89 billion, which is a 59.8 per cent increase compared to 2017.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

M&A activity has developed in Vietnam during the past 12 years following the government’s issuance of a large number of new legal regimes, which was considered the government’s preparation for Vietnam’s official accession to the World Trade Organization (WTO) on 11 January 2007. However, there is no united legal platform for M&A activities, and investors need to consider the requirements, guidance and other information concerning the interpretation or practice regarding investments found in different pieces of legislation. The principal regulations for M&A activities may be classified under the following main categories:

a international treaties and agreements to which Vietnam is a contracting party include Vietnam’s commitments to the WTO applicable to foreign investment into Vietnam from other state party investors, and other mutual agreements between Vietnam and a specific country or countries;

b general regulations, including the Civil Code 2015, which is the key general law regulating the ‘legal status and standards for conduct of individuals and legal entities, the rights and obligations of individuals and legal entities in property and personal relations arising from relations established based on equality, freedom of will, independence of property and self-responsibility’. (Article 1 of the Civil Code 2015);

c the primary sources for regulating M&A activities are the Law on Enterprises 2014 (which governs the establishment, management, organisation and operation of enterprises) and the Law on Investment 2014 (which mainly focuses on investment activities within Vietnam);

d regulations on land, including the Law on Land 2013. Ownership of all land lies with the entire population, with the state acting as the representative owner. Therefore, no
enterprise, whether a domestic private enterprise, state-owned enterprise or foreign private enterprise, is the actual owner of the land. Investors may use land through a land use right;

e) regulations on specialised business areas, which specifically govern the relevant investment businesses of investors in, for instance, the areas of finance, education, distribution or restaurant services;

f) regulations applicable to public companies, including the Law on Securities 2006 (as amended in 2010) and its implementing decrees and circulars. In 2015, total foreign investment in a public company was relaxed by the government (see Section III. iii). According to Article 25 of the Law on Securities 2006, a public company is a joint-stock company that has already conducted the public offering of its shares, has its shares listed on the Stock Exchange or at the Securities Trading Centre, or has its shares owned by at least 100 investors, excluding professional securities investors, and has a contributed charter capital of 10 billion dong or more;

g) regulations on competition, including the Laws on Competition 2004 and 2018 and their implementing decrees and circulars (Section IX on the Law on Competition); and

h) regulations on other relevant matters, including foreign exchange management and labour.

Some parts of the above regulations are not sufficiently well developed, such as the overlapping and inconsistent regulations between the Law on Enterprises and the Law on Investment, as well as regulations on securities and on competition. In addition, similar to other new market economies, foreign restrictions still play an important part, and foreign investors should look at both domestic laws and international treaties, including bilateral and multilateral treaties, to understand the differences and decide the most appropriate type of M&A arrangement. In addition, if state-owned enterprises (SOEs) or state-owned capital are involved in the contemplated transactions, investors should also pay attention to the regulations applying to those SOEs or state-owned capital, which sometimes prolongs the closing of an M&A deal.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT


According to the old regime (before 1 July 2015), upon establishment, all companies, including domestic companies, had to be issued with a business registration certificate (or, after 1 June 2010, an enterprise registration certificate), except where foreign investors invested in Vietnam for the first time and were issued with investment certificates that concurrently acted as their business registration certificates.

The Law on Enterprises 2014 and the Law on Investment 2014, which have come into effect since 1 July 2015, introduced a new regime. Accordingly, an enterprise registration certificate will be required for the establishment of all companies with or without foreign capital; in addition, foreign investors have to apply for and obtain an investment registration certificate. Specifically, foreign investors (i.e., foreign individuals or foreign organisations incorporated under foreign laws) that wish to set up a new entity in Vietnam will first need to apply for investment approval from the investment licensing authorities (under the form of an investment registration certificate) for their investment projects in Vietnam. Upon issuance of the investment approval, the foreign investors will carry out the establishment procedure...
for the issuance of an enterprise registration certificate. These steps are also applicable if a company of which foreign shareholders together hold (directly and indirectly) 51 per cent or more of the total shares or equity wishes to set up its subsidiary in Vietnam.

In the case of a share acquisition or subscription in an existing Vietnamese company, foreign investors must register the proposed acquisition or subscription with the investment licensing authority if the target company engages in conditional business sectors, or the proposed transaction would result in 51 per cent or more of the total shares being held (directly or indirectly) by foreign investors. This registration step is not required in other acquisition or subscription situations. Upon completion of the registration, the target company shall carry out the procedure for the amendment of its enterprise registration certificate or enterprise registration details in accordance with the Law on Enterprises 2014, namely changes in the foreign shareholders of a joint-stock company or members of a limited liability company, or to the charter capital of a company, or both. This procedure is also applicable when the acquirer or subscriber is a foreign-invested company based in Vietnam of which 51 per cent or more of the total shares is held (directly and indirectly) by foreign shareholders.

In March 2019, the government introduced the draft law on amendments to the Law on Enterprises 2014 and Law on Investment 2014, which is expected to enhance the competitiveness of Vietnam’s business market. One notable point of the draft law is that foreign investors may not be required to register a proposed acquisition or subscription if such acquisition or subscription causes no increase in foreign shareholding in the target companies. In addition, the law reduces the requirements for the establishment and operation of a company.

ii The Law on Land 2013

For the first time, the Law on Land 2013 allows foreign-invested companies to use land in allocation form where foreign-invested companies develop a residential-house-for-sale or for-lease-sale project. Nevertheless, domestic entities still have more mechanisms and options to acquire a land use right than foreign-invested companies. Specifically, domestic economic organisations, households and individuals can obtain a land use right by:

- being allocated land from the state;
- leasing land from the state;
- receiving a transfer, donation or inheritance of land use rights;
- receiving land use rights as in-kind capital contribution from a lawful land user (applicable to economic organisations);
- recognition by the state of land use rights;
- leasing and subleasing land from a developer of an industrial zone, high-technology zone or economic zone;
- receiving the transfer of an ongoing project using land; or
- receiving land use rights in accordance with the result of a land dispute settlement.

Foreign-invested companies cannot acquire land under method (c) above.

Corporate real estate M&A in Vietnam are not commonly conducted in the form of an asset or land direct transfer, as asset or land direct transfers involve rather complicated processes, not to mention that where the transferee is a foreign-invested company, the land

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3 Article 55.3 of the Law on Land No. 45/2013/QH13.
must be returned to the government before being transferred to the transferee. In practice, corporate real estate M&A in Vietnam are normally structured in the form of a project or asset holding company M&A, as this will save the new owner from having to re-obtain the necessary licences for the real estate project’s development (if the permits and licences have already been obtained), as well as offering more options for tax planning.

If a project or asset holding company M&A changes the status of the target company from a domestic private company into a foreign-invested one, the target company can still retain the licences and permits and the rights of a land user over the target land or asset that were obtained as before the transaction.

Another key point under the Law on Land 2013 relates to the definition of offshore entity, under which it is clear that an offshore entity itself may not obtain a land use right. Additionally, with respect to a foreign-invested company being a land user in Vietnam, there is no difference whether it is a 1 or a 100 per cent foreign-invested company.

### iii The Law on Securities

Decree 60/2015/ND-CP, providing guidance on the Law on Securities, took effect on 1 September 2015, thereby relaxing the restrictions imposed on foreign investment in public companies. Foreign ownership in a public company is regulated as follows:

- if an international treaty to which Vietnam is a party has provisions governing the foreign ownership ratio, then such provisions apply;
- if a public company operates in a business investment line for which the law on investment and other relevant laws have provisions on foreign ownership ratio, then those provisions apply. If a public company operates in a business investment line with conditions applicable to foreign investors, but there is not yet any specific provision on the foreign ownership ratio, then the maximum foreign ownership ratio is 49 per cent;
- if a public company operates in several business lines with different provisions on the foreign ownership ratio, then the foreign ownership ratio shall not exceed the lowest ratio of the business lines (in which the company operates) wherein there are provisions on foreign ownership, unless otherwise provided in international treaties; and
- for public companies not falling into any of the above scenarios, foreign ownership is unrestricted, unless otherwise provided in the company charter.

A proposal for an amended Law on Securities as a replacement for the current Law on Securities (Report No. 97/TT-Tr-CP of the government) was submitted to the National Assembly’s Standing Committee on 22 March 2019, with key highlights on notable changes being as follows:

- the maximum foreign ownership ratio will be governed specifically by the government from time to time, and will not be specified in the Law on Security. In 2017 and late 2018, the Ministry of Finance kept introducing draft amendments to the Law on Securities to lift the maximum foreign ownership ratio to 100 per cent with respect to business investment lines not prescribed in Vietnam’s WTO commitments;
- the conditions for the first public offering of securities are as follows: an increased requirement on the offering company’s charter capital from 10 billion dong to 30 billion dong, and profitable business results from the previous one to two years;
- adding a new condition that the new share issuance’s par value must not be higher than the total par value of the issued shares;
the conditions for the public offering of bonds are as follows: an increased requirement on the offering company’s charter capital from 10 billion dong to 30 billion dong;

- supplementing the conditions on reliance ratings applicable to certain organisations that issue bonds;

- linking public offerings of securities with the listing and registration of transactions on the securities trading floor, accordingly requiring that companies that apply for their public offering of securities via the State Securities Committee must also apply for listing or registering transactions on a securities trading floor at the same time; and

- for private offerings of shares, specifying the entities eligible to take part in the private offering of shares or convertible bonds that include only strategic investors and professional security investors, and a restriction on the transfer of the shares or convertible bonds post-purchase lasting for a period of three years or one year, respectively.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

According to StoxPlus, investors from Thailand and Singapore have aggressively seized megadeals since 2017 and also lead in terms of deal value. Meanwhile, Japanese and Korean investors, although they have contributed the largest number of deals, usually conduct small and medium-sized deals.

The accumulated inbound M&A deal value entering Vietnam since 2013 amounts to US$26.89 billion from 535 transactions. The inbound deal value in 2017 increased by more than double compared with 2016. By the first half of 2018, US$2.83 billion from 40 transactions had already been recorded.

The shift in inbound M&A in 2017 and the first half of 2018 was to megadeals. In these agreements, foreign investors acquired a majority stake in leading Vietnam-domiciled enterprises, including leading brewery SABECO, real estate conglomerate Vinhomes and Vincom Retail, dairy corporation Vinamilk, Ho Chi Minh City Infrastructure Investment, Techcombank and Nam Long Investment Corp.4

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

M&A deals that focused on real estate, processing and manufacturing, wholesale and retail were the most attractive deals for investors in 2018.

The real estate sector continues to be one of the most active in M&A due to a high demand for real estate, policies on tightening capital flow to the real estate sector and State Bank Vietnam’s control over non-performing loans. The physical transfer of land, buildings and other types of real estate, however, is a problematic issue and can take a long time, especially if it is a transfer to a foreign investor. In particular, an offshore investor may need to set up its subsidiary in Vietnam, apply to the licensing authorities to implement projects in connection with the use of the real estate to be transferred and register the physical transfer of the real estate with the relevant authorities. Therefore, in practice, foreign entities often

consider acquiring vendors’ shares in the project company that owns the real estate. The procedure for share acquisition is much simpler, and offshore investors still own the real estate through the project company. Highlight transactions in 2018 included the following:

a. GIC Private Limited (a Singapore government fund) purchased 5.74 per cent of shares of Vinhomes Joint Stock Company for a value of approximately US$853 million. Vinhomes Joint Stock Company Vietnam is the biggest integrated real estate developer in Vietnam with a focus on residential and office property;

b. Singapore-based Frasers Property Limited acquired, through its subsidiaries Frasers Property Investments (Vietnam) 2 Pte Ltd and Frasers Property Investments (Vietnam) 1 Pte Ltd, 75 per cent of the shares of Phu An Dien Real Estate JSC (PAD) and Phu An Khang Real Estate JSC (PAK) for the respective prices of US$35.2 million and US$18 million. PAD and PAK are developers of the residential-cum-commercial projects in Thu Duc District and District 2 of Ho Chi Minh City;

c. Hanoi Hotel Tourism Development Limited Liability Company acquired 75 per cent of the shares in TPC Nghi Tam Village Ltd, which operates the international five-star hotel Intercontinental Hanoi West Lake Hotel in Hanoi, for about US$53.3 million; through its wholly owned subsidiary, CVH Nereus CapitaLand acquired 16.97 million shares, or 99.49 per cent of the charter capital, of Hien Duc Tay Ho Joint Stock Company for about US$29.7 million. Hien Duc Tay Ho Joint Stock Company, which changed its name to Capitaland - Hien Duc Joint Stock Company after the acquisition, is the developer of a real estate complex located on 0.9 hectares of land in the Tay Ho District in Hanoi; and


M&A activities in manufacturing and processing remain active in 2018. Notable deals include:

a. The Nawaplastic Industries (Saraburi) Co, Ltd additionally acquired 27,823,623 shares in Binh Minh Plastics Joint Stock Company for US$107 million to increase its shareholding to 54.39 per cent;

b. Sojitz Corporation acquired over 95 per cent of the shares in Saigon Paper Corporation for US$91.2 million;

c. Kyoei Steel additionally acquired more than 50 per cent of shares of Viet Italy Steel Company 2018; and
d. Itochu Textile Prominent (ASIA) Ltd, a subsidiary of ITOCHU Corporation, paid around US$47 million to additionally acquire 10 per cent of the shares in Vietnam National Textile and Garment Group (Vinatex), raising its shareholding in Vinatex to 15 per cent.

In the wholesale and retail sector, M&A activities were bolstered by local retailers, as they have the edge in expanding their reach via M&A amid fierce competition; specifically, they are closer to local consumers and not subject to the requirement of an economic needs test.
Vingroup continued its M&A activities in 2018, either directly or through its retail brand, to acquire various smaller companies and expand its retail chain, including:

a 23 supermarkets in the Fivimart chain;  
b 87 convenience stores in the Shop&Go chain;  
c the acquisition of mobile retail chain mobile Vien Thong A; and  
d becoming the exclusive distributor of the Chevrolet in Vietnam.

In early 2018, the Malaysia-based private equity firm Creador announced its acquisition of 35 per cent of the shares of Mobile World Investment JSC, which is one of Vietnam’s biggest retailers with over 2,200 retail shops in Vietnam, for US$43 million.

M&A deals in the banking and finance sector, consumer finance received attention thanks to strong growth in recent years, with the following being notable deals:

a Shinhan Card acquired a 100 per cent stake in Prudential Finance Vietnam for around US$150.8 million from Prudential Hoborn Life Limited;  
b Lotte Card Company Limited wholly acquired Technological and Commercial Finance Company Limited (Techcom Finance) from Techcombank for US$74.67 million; and  
c Southeast Asia Commercial Joint Stock Bank (SEABank) won an auction to wholly acquire Vietnam Posts and Telecommunications Group for 710 billion dong;  
d in March 2018, Techcombank announced that two legal entities managed by Warburg Pincus would invest over US$370 million into the bank, subject to appropriate regulatory approval, which was one of the most notable deals in banking that year.

The food and beverage sector also saw one of the biggest deals of the year when South Korean Group acquired 109.9 million Treasury shares, accounting for a 9.5 per cent stake in Masan Group Corporation for around US$470 million.

With respect to the sale of state-owned capital, the state equalised and sold shares to strategy shareholders in 30 enterprises in 2018 according to Government Notice No. 39/TB-VPCP dated 25 January 2019, which falls short of its target of 181 enterprises. The equalisation and divestment of state-owned capital continues to face obstacles due to many factors, such as a lack of accuracy in evaluating state-owned capital, foreign ownership limitations in several sectors, lack of transparency and consistency in the process, and a complicated procedure. The government’s goal, by 2020, is to retain only 150 state-owned enterprises in the following vital sectors:

a electricity transmission;  
b cartography related to national security and military operations;  
c railway infrastructure;  
d air traffic services;  
e postal services;  
f irrigation management;  
g lending for socioeconomic development;  
h banking safety; and  
i the lottery.

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VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Foreign investment is the main factor driving M&A in Vietnam, especially in the real estate sector. Foreign investors may mobilise capital from overseas countries and pour it into the domestic market. Regarding Japanese acquirers, they seem to prefer to finance their acquisitions of Vietnamese companies by using their existing equity capital and retained profits.

Local investors, by contrast, rarely disclose the source of their purchases’ financing. For example, in the largest M&A deal by a local investor in 2018, An Quy Hung Limited Company, with charter capital of 500 billion dong, succeeded in acquiring a 57.71% stake in Vietnam Construction and Import-Export JSC (Vinaconex), which is one of the largest conglomerates in construction, for 7.366 billion dong, but the financing of the deal is still unclear. Considering that there is a limit on the amount of credit that can be extended by banks and security companies for the acquisition of stakes, it is assumed that the acquisition was sourced by the acquirer’s partners, which are various real estate companies. Other domestic acquirers tried to mobilise capital from their shareholders and foreign investors to fund M&A deals in 2018, such as Saigon Thuong Tin Real Estate JSC, which sought the approval of the general shareholders’ meeting to issue and sell new shares to mobilise a total of US$90 million for M&A.

For the first time in three years, the State Bank of Vietnam (the central bank of Vietnam) has reduced its lending interest rate by 0.25 per cent, to 6.25 per cent, to boost economic growth. However, enterprises, especially small and medium-sized ones, continue to face difficulties in gaining financing from domestic banks because of high interest rates.

Vietnamese parties are familiar with the typical clauses applicable to offshore loan arrangements, such as financial covenants and security requirements. However, while an offshore creditor’s right to collect payment from debtors in the event of default is protected, enforceability of some terms may in practice be questionable. For instance, offshore creditors may face challenges if they wish to exercise the right to acquire secured shares in the event of default if a project company is operating in areas that are conditional or restricted for foreign investment. In addition, offshore creditors are not allowed to have collateral over a land use right in Vietnam.

According to foreign exchange management regulations, offshore loans with terms of more than one year are subject to registration with the State Bank of Vietnam. However, the loan registration requirement is just an administrative tool for the State Bank of Vietnam to manage and control the flow of foreign exchange currencies in Vietnam from time to time; it is not a confirmation or certification of the state that an agreement is legally recognised.

VII EMPLOYMENT LAW

The current Labour Code has been effective since 1 May 2013. According to Article 106, the number of overtime hours worked by employees must not exceed 50 per cent of the normal working hours in one day. In the case of working on a weekly basis, the total of the normal...
working hours plus overtime hours must not exceed 12 hours in one day, 30 hours in one
month, and 200 hours in one year. The previous law simply provided that the number of
overtime hours must not exceed four hours per day and 200 hours per year.

Key provisions of the current Labour Code also include:

- adding one more day off during the lunar new year period (Article 115);
- extending the maternity leave period for female employees from four to six months in
general (Article 157);
- extending the limitation period for dealing with breaches of labour discipline from
three to six months, or 12 months in some special cases (Article 124); and
- providing more details regarding cases in which foreign workers are exempted from
work permit requirements (Article 172). In particular, exemption cases include:
  - capital-contributing members or owners of limited liability companies;
  - members of the boards of directors of joint-stock companies;
  - chiefs of representative offices and directors of projects of international
    organisations or non-governmental organisations in Vietnam;
  - those who stay in Vietnam for less than three months to offer services for sale;
  - those who stay in Vietnam for less than three months to deal with complicated
    technical or technological problems that adversely affect or are at risk of adversely
    affecting production and business activities where these problems cannot be
    handled by Vietnamese and foreign experts who are currently in Vietnam;
  - foreign lawyers possessing a professional practice licence in Vietnam in accordance
    with the law on lawyers;
  - cases that are in accordance with a treaty to which Vietnam is a contracting party;
  - those who are studying and working in Vietnam, provided that their employer
    shall notify the provincial level state management agency of labour of their
    employment seven days in advance;
  - internal transfers within an enterprise and within the scope of the 11 services
    on the List of Commitment on Services of Vietnam with the WTO, namely,
    business, information, construction, distribution, education, environment,
    financial, medical health, tourism, culture and entertainment, and transportation;
  - entering Vietnam to provide expert technical consultancy services or to undertake
    other tasks servicing the work of research, formulation, evaluation, monitoring
    and assessment, management and implementation of a programme or project
    using official development assistance (ODA) in accordance with an international
    treaty on ODA signed by the competent authorities of both Vietnam and the
    foreign country; and
  - entering Vietnam to work as an expert, manager, executive director or technician
    for a working period of less than 30 days and for a total cumulative period not
    exceeding 90 days in any one year.

In 2017, the government introduced a draft of the new Labour Code to replace the existing
Labour Code, which is scheduled to be submitted for approval by the National Assembly in
October 2019. The second version of the new law was presented for the solicitation of the
public’s opinion from April to June 2019, and includes some notable changes as follows:

- the maximum overtime of employees in specific situations regulated by the government
  increases to 400 hours per year from the existing limit of 300 hours;
b the retirement ages, which are currently 60 for men and 55 for women, are proposed to be gradually raised to 62 and 60, respectively, from January 2021;
b the executive committees of trade unions at the directly superior level are no longer able to perform the rights and duties of trade unions in workplaces. In other words, there must be a trade union at workplaces to carry out certain procedures relating to labour matters, such as disciplinary procedures;
d probation for managerial positions may be extended to six months from the current limit of 60 days; and
e the term of work permits may not exceed two years, and may be extended once for a maximum term of two years.

VIII TAX LAW

The current Law on Tax Administration was enacted in 2006 and amended three times in 2012, 2014 and 2016, and is now proposed to be replaced by a new version. The draft Law on Tax Administration (amended) has been reviewed at the National Assembly of Vietnam (National Assembly) meeting in February 2019, and will be continuously updated as determined by the National Assembly in this meeting. The proposed changes are mainly based on technical aspects.

In 2017 and early 2018, the Ministry of Finance introduced its draft proposals for some amendments to certain tax laws. Nevertheless, there has been no update or any agenda for reviewing this draft in the National Assembly meeting schedule for 2019.

IX COMPETITION LAW

On 12 June 2018, an entirely new Law on Competition 2018 was adopted by the National Assembly, effective from 1 July 2019. Below is a summary of the merger control provisions introduced by this new Law.

Unlike its predecessor, which sets the trigger for a merger filing requirement based on the combined market share of the parties concerned, the new Law prescribes several general factors, one of which the government may use as a basis to set the thresholds for triggering an obligation of the parties concerned to keep the local competition authority notified of a deal. These factors are:
a the total assets in the Vietnam market of the parties to the M&A transaction;
b the total revenue in the Vietnam market of the parties to the M&A transaction;
c the value of the M&A transaction; and
d the combined market share in the relevant market of the parties to the M&A transaction.

If a notification is required, the parties involved in the M&A transaction will need to submit a number of documents to the National Competition Committee for the purpose of the notification. The Committee will then carry out a two-phase appraisal: a preliminary one, which may take up to 30 days, and an official one, which will take up to 90 or 150 days, depending on the complexity of the case.

A transaction may be carried out, but the parties concerned must undertake to conduct one or more of the following pre-closing or post-closing measures as a condition for the National Competition Committee to allow it:
An M&A transaction is prohibited if it significantly restricts or is capable of significantly restricting competition in the market. The significant competition-restraining impact or the ability to cause a significant competition-restraining impact will be assessed based on any or a combination of the following factors:

- the combined market share of the parties participating in the contemplated transaction;
- the extent of concentration in the relevant market before and after the contemplated transaction;
- the relationship of the parties participating in the contemplated transaction;
- the competitive advantages brought by the contemplated transaction in the relevant market;
- the ability of the company formed from the contemplated transaction to significantly increase prices or the rate of return on sales;
- the ability of the company formed from the contemplated transaction to exclude or hinder other businesses from entering or expanding the market; and
- special factors in the industry or sector in which the companies taking part in the contemplated transaction operate.

The Grab/Uber case

Grab’s acquisition of Uber’s business remains the most recent notable merger control case in Vietnam (it was handled under the Law on Competition 2004, which was replaced by the new Law on Competition 2018).

On 25 March 2018, Grab Inc announced its acquisition of all of Uber’s assets and operations in South East Asia. As a result, GrabTaxi Company Limited and Uber Vietnam Company Limited entered into an agreement under which Uber Vietnam Company Limited transferred to GrabTaxi Company Limited all of its assets, operations and interests in Vietnam. On 16 April 2018, the Vietnam Competition Authority (VCA) issued a decision to conduct a preliminary investigation into the acquisition. In an explanatory document submitted to the VCA, the parties claimed that as their combined market share in Vietnam was less than 30 per cent, they did not need to comply with the merger notification requirement. However, an official investigation was carried out from May 2018, and the investigation results were issued on 30 November 2018. Accord to these, the VCA found signs of violations of competition law, including failure to notify an economic concentration under Article 20 of the Law on Competition 2004 and falling into the prohibited category of economic concentration under Article 18 of the Law on Competition 2004. In addition, it was held that Grab and Uber had market power and competed directly with each other; therefore, Grab’s acquisition of Uber’s business in Vietnam would change the market structure, undermine competition, and potentially result in a powerful enterprise that may abuse its dominant market position.

The VCA delivered the investigation’s conclusion to the Competition Council, which subsequently established a council to deal with the case. By law, within 30 days from the receipt of the file, the Council is authorised to decide whether to conduct an investigative
hearing, to return the file for additional investigation or to suspend resolution of the case. After the discovery of new evidence, the file was returned and the investigation procedure extended.  

X  OUTLOOK

Vietnam experienced strong economic growth in 2018, with the gross domestic product (GDP) rate sitting at 7.08 per cent (exceeding its target of 6.7 per cent), the highest rate in the past 11 years. According to the Annual Report of the General Statistics Office, 9 foreign direct investment reached US$35.46 million 10 and Vietnam’s total import and export turnover reached over US$480 billion, 11 and Vietnam remains a very attractive place for investment in the private sector. Vietnam is expected to benefit greatly from the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, which it signed in March 2018; according to the World Bank, the Agreement is expected to increase Vietnam’s GDP from 1.1 to 3.5 per cent by 2030.

The banking sector could be more active than ever as the government works hard to reform the banking system. Foreign ownership limits relating to the restructuring of weak commercial banks may be relaxed by the Prime Minister on a case-by-case basis, allowing for greater participation by foreign investors under a restructuring plan approved by the State Bank of Vietnam.

Real estate will remain one of the most attractive sectors for foreign investors, given the speed of the country’s urbanisation with the rise of the middle-income class. In 2017, the National Assembly issued a resolution aimed at easing the procedures for enforcement of property mortgages by banks. This is also one of the key factors to facilitate M&A in the real estate sector, as banks will find it easier to sell mortgaged properties and real estate development projects.

Both foreign and domestic deal makers continue to seek to acquire pharmaceutical distribution chains. Given the existing stringent restrictions on foreign investments in this sector, foreign deal makers should structure their deals creatively.

Retail, energy, and fast-moving consumer goods will continue to lure foreign investments. There are also opportunities in renewable energy projects, high-tech agriculture and other high-tech industries.

The speeding up of the privatisation of state-owned companies offers foreign investors many more opportunities to enter the market through M&A. The government’s plan to further divest the following enterprises may draw the attention of foreign investors: Petrolimex,

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11 The 2018 Annual Report of the General Department of Vietnam Customs was published on 15 January 2019: https://www.customs.gov.vn/Lists/ThongKeHaiQuan/ViewDetails.aspx?ID=1559&Category=Ph%C3%A2n%20t%E1%BB%99nh%20k%E1%BB%B3&Group=Ph%C3%A2n%20t%E1%BB%B3&Group=Ph%C3%A2n%20t%E1%BB%B3.

According to Nikkei Asian Review, as efforts by manufacturers to establish a business in Vietnam have stabilised, infrastructure exports are creating a new wave of investment as Vietnam lures private sector funding in infrastructure development, with an anticipated need for US$400 billion in infrastructure spending over the next 10 years.
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A senior partner and member of the firm’s board of directors, Juan Domingo Alfonzo Paradisi graduated from the Universidad Católica Andrés Bello in 1987. In 1990, he obtained a postgraduate degree in administrative law from the same university. In 1992, he obtained a doctorate in administrative law from Universidad Complutense de Madrid, and a doctorate in superior studies in public administration from the National Public Administration Institute, graduating cum laude. From 1996 to 1999, he served as an alternate judge for the First Contentious Administrative Court.
Dr Alfonzo Paradisi is a board member of the Association of Graduates of the National Institute of Public Administration of Spain. He is also a member of the Venezuelan Tax Law Association, the Administrative Law Foundation, the Venezuelan Financial Law Association and the Venezuelan Law and Economy Association.

Dr Alfonzo Paradisi is the Vice President of the Venezuelan Chapter of ECSA-Andina (the European Community Studies Association). He is also a member of the board of directors of the European–Latin American Integration Institute (IELEPI).

He is a professor of the chair of protection of free competition for postgraduate courses and a coordinator of the postgraduate programme in economic law at the Universidad Católica Andrés Bello. At the Universidad Central de Venezuela, he is a professor of the chair in administrative and fiscal decentralisation for the postgraduate programme in tax law, administrative law and constitutional law for the Law School, and on administrative law for the School of Political Studies. He speaks Spanish and English.

LAWRENCE FUBARA ANGA
ÆLEX

L. Fubara Anga heads the banking, finance and transportation practice groups at ÆLEX.

He advises on M&A strategy, as well as on financial, corporate and commercial issues affecting projects and companies, especially in the oil, gas, electricity, aviation, maritime, banking and financial services sectors.

Mr Anga has been involved in project finance, banking and capital market transactions for several years. He is a former chair of the Capital Markets Solicitors Association.

He advised the government on the review of the Investment and Securities Act and was a member of the National Committee on the Review of Capital Market Structure and Processes.

He was invited to become a member of the Presidential Policy Advisory Committee; he was also a member of the subcommittee on finance and investment and authored the committee’s policy paper on foreign investment and privatisation. He is currently the chair of the board of trustees of the Investors Protection Fund of the Nigerian Stock Exchange. He was a member of the Securities and Exchange Commission’s (SEC) master plan committee and is currently a member of the rules and compliance subcommittee of the capital markets committee of the SEC.

Mr Anga was educated at Yale University and the University of Cambridge. He is admitted to practise law in Nigeria, England and Wales, and Ghana.

MIHÁLY BARCZA

Oppenheim Law Firm

Dr Barcza graduated from the József Attila University Szeged in 1994 and studied at University of Economics Budapest between 1995 and 1997. He was a trainee at the Budapest Stock Exchange and later was in-house counsel at CO-Nexus Investment House. He was a trainee, then attorney and later partner with a reputable Hungarian law firm, Réti Szegeő and Partners, from 1995 to 2004, spending seven months at Clifford Chance, London, on a scholarship. He was senior counsel and co-head of corporate with international law firm Freshfields Bruckhaus Deringer from 2004 to 2007. He is a founding partner of Oppenheim. He has been a member of the Money and Capital Market Arbitration Court since 2000.
MOHAMMED BASAMA  
*White & Case LLP*  
Mohammed is an associate in our corporate and M&A group, based in Doha. Mohammed advises clients on a range of matters including cross-border mergers and acquisitions, joint ventures, reorganisations and general corporate advice. Before joining White & Case, Mohammed worked for an international law firm in its London office.

OMAR S BASSIOUNY  
*Matouk Bassiouny & Hennawy*  
Omar S Bassiouny is the founding partner of Matouk Bassiouny & Hennawy and head of the corporate and M&A practice group. He is consistently ranked in top tiers and bands by legal periodicals in the areas of corporate law and M&A for his considerable expertise in setting up joint ventures and new projects in Egypt, as well as ensuring compliance with local laws and corporate governance.  
Omar is also the founding partner in Matouk Bassiouny’s Dubai office, where he heads the corporate and M&A work, along with Malack Habashi and Ahmed Ibrahim in association with Amal Advocates.

Cameron Belsher is the leader of McCarthy Tétrault’s M&A group. He focuses his practice on public and private M&A, corporate finance and private equity, frequently advising on international and cross-border deals. A senior member of the firm’s business law group, Cam is one of the most sought-after corporate lawyers in Canada and the relationship partner for some of McCarthy Tétrault’s key clients.

Cameron is a former member of the Toronto Stock Exchange (TSX) Listings Advisory Committee, which is composed of individuals representing legal, brokerage and securities-related industries, and provides feedback on TSX listings initiatives. He has lectured extensively on M&A and public corporation matters and is a former adjunct professor at the Faculty of Law, University of British Columbia. He received his LLB from Osgoode Hall Law School in 1987, and was called to the British Columbia Bar in 1988.

Cameron is ranked among Canada’s top business lawyers by a multitude of publications, including *Chambers and Partners, The Legal 500, Lexpert, Best Lawyers in Canada, Who’s Who Legal* and *IFLR1000*.

JUSTIN BHARUCHA  
*Bharucha & Partners*  
Justin is a partner at Bharucha & Partners and his practice focuses on M&A and finance. He advises on acquisitions by and from non-residents, especially in sectors where foreign investment is subject to restrictions, illustratively, real estate, defence and retail. Justin has also structured transactions and advised Indian clients acquiring companies offshore.
NICOLAS BIRKHÄUSER
Niederr Kraft Frey Ltd
Nicolas Birkhäuser specialises in merger control proceedings and cartel and abuse of dominance investigations, including multi-jurisdictional coordination, high-profile investigations and transactions, set-up of business (including cooperation, distribution, sourcing, research and development, dominance) and compliance. A particular focus of his practice lies on intellectual property-related aspects of competition law (including cooperation agreements, distribution systems and licensing).

MIGUEL BOLÍVAR TEJEDO
Uría Menéndez
Miguel Bolivar joined Uría Menéndez in 2010, and he has been a senior associate at the firm since 2018. From March 2016 to September 2016, he was seconded to the London office of Slaughter and May. Miguel practises as a lawyer in Uría Menéndez’s corporate department.

His main practice areas are commercial law in general, corporate law, M&A, and refinancing and restructuring of companies. He has advised on very diverse operations, including financing and debt restructuring operations, both bilateral and syndicated; buying and selling of companies; real estate transactions and the purchase and sale of asset portfolios; merger and restructuring operations of groups of companies; and contracting in general.

FRANCISCO BRITO E ABREU
Uría Menéndez – Proença de Carvalho
Francisco Brito e Abreu joined Uría Menéndez in 2001 after working as in-house counsel in the Portuguese subsidiary of a multinational corporation, a privately owned holding company and a listed Portuguese company, and as a lawyer in another prestigious Portuguese law firm. He was made a partner of Uría Menéndez in January 2005.

He focuses his practice on commercial and corporate law issues, and has extensive experience in corporate restructuring, M&A and private equity transactions.

He is recognised by major publications (Chambers Global, IFLR1000, PLC Which Lawyer?) for his work in M&A and private equity.

THOMAS BRÖNNIMANN
Niederr Kraft Frey Ltd
Thomas Brönnimann’s practice focuses on capital markets and private and public M&A transactions, with a particular focus on listed entities and other large enterprises. His M&A practice includes private transactions for both strategic and financial buyers and sellers, and public tender offers. He represents clients before the Swiss Takeover Board.

ADRIANO CASTELLO BRANCO
Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados
Adriano focuses his practice on a wide range of corporate matters, mergers and acquisitions and restructuring transactions, with an emphasis on listed companies and private equity investments. He is the Director of the Brazilian Institute of Business Law (Ibrademp) and has experience in law firms in Brazil and abroad, having worked as an international associate.
in the New York office of Davis Polk & Wardwell LLP. He has also held executive in-house positions and been a board member of listed domestic corporations. He is author of the book *The Board of Directors in Corporations* and several academic articles in collective works and law reviews.

**JOÃO MARCELINO CAVALCANTI JÚNIOR**

*Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados*

João counsels national and international companies (including listed companies), private equity funds and investors on corporate matters, including mergers, acquisitions, joint ventures and divestments. He is admitted to practise in Spain and Brazil. From 2007 to 2012, he gained international experience in Spain, where he practised at a Big Four firm, a multinational company and top-tier Spanish law firms. He holds a LLM degree in international business law from the ESADE Law and Business Schools and a LLM degree in taxation from University of Barcelona. He has also received a bachelor of laws degree from the Federal University of Pernambuco.

**HO KYUNG CHANG**

*Bae, Kim & Lee LLC*

Attorney Ho Kyung Chang is a partner in the corporate and M&A practice group of Bae, Kim & Lee LLC. He advises domestic and international clients in connection with a broad range of general corporate and transactional matters, including M&A, foreign investments, private equity investments, capital markets and corporate governance since he joined Bae, Kim & Lee LLC in 2009.

Mr Chang gained experience of working as a secondee in the foreign affairs and transactions team at LG Display Co, Ltd in 2011, and as a foreign attorney in the Washington, DC, office of Arnold & Porter LLP in 2014 and 2015. He was appointed by the Ministry of Justice of Korea as a member of the Legal Advisory Committee for International Investment Disputes in 2011.

Mr Chang received a bachelor of law degree from Seoul National University in 2005, completed the Judicial Research and Training Institute in 2009 and graduated from Georgetown University Law Center (LLM) in 2014. He was admitted to the Korea Bar in 2009 and the New York Bar in 2015.

**WEI (DAVID) CHEN**

*DeHeng Law Offices*

Mr Wei (David) Chen is a managing partner and head of cross-border transactions. His diversified practice includes advising state-backed investment funds, state-owned enterprises and private enterprises in outbound M&A, especially in semiconductors and mining. He was named in the March 2018 edition of *Asian Legal Business* magazine as one of the top 10 M&A lawyers in China. He advised JAC Capital in its US$2.5 billion acquisition of the Standard Products Unit of NXP Semiconductors. In mining mandates, Mr Chen has represented China Gold and other major miners as lead counsel in big ticket global deals. Mr Chen also has a long track record of representing foreign investors in their establishment and market entry in China and their negotiation of joint ventures with Chinese partners.
MARCUS CHOW

*Bird & Bird ATMD LLP*

Marcus is head of the corporate group at Bird & Bird ATMD LLP.

His transactional practice includes venture capital investments, private and public M&A, as well as private equity entries and exits. He has experience advising clients across a range of industries including manufacturing, retail, construction, real estate, food and beverage, banking and finance, airlines, mining, agriculture and technology.

Marcus graduated with an LLB from the National University of Singapore and an LLM from the University of Virginia. He also holds a certificate in governance as leadership from the Harvard Kennedy School of Government. Marcus is qualified to practise in Singapore and New York, USA.

VASSILIS S CONSTANTINIDIS

*Dryllerakis & Associates*

Vassilis S Constantinidis is active in the fields of M&A, employment law, commercial law, intellectual property, litigation and arbitration. He is specialised in employment law, having extensive experience in all HR issues (including code of conduct policies, data protection policies, employers’ handbooks, business-level collective labour agreements and individual employment contracts of any kind). He has worked for 18 years as an in-house lawyer and legal director in the holding company of Boutari Group and Myths Brewery SA (part of S&N and subsequently Carlsberg Group), and was also in charge of the HR and corporate affairs department, contributing to several international projects of Carlsberg Group.

He is a graduate of the Athens University Law School, and is a member of the Athens Bar. He is qualified to practise before all courts of all levels of jurisdiction. He speaks Greek, English and French.

ROGER A COOPER

*Cleary Gottlieb Steen & Hamilton LLP*

Roger Cooper is a partner at Cleary Gottlieb Steen & Hamilton LLP, based in New York.

Mr Cooper’s practice focuses on complex civil litigation, with an emphasis on disputes arising out of securities, M&A and derivative transactions, and on corporate governance issues.

Mr Cooper has been recognised as a leading lawyer by Chambers USA, Benchmark Litigation and The Legal 500 US and has written for numerous publications, including New York Law Journal: Complex Litigation, New York Law Journal Litigation, US Law Week, Derivatives, White Collar Crime and Derivatives Litigation in Business and Commercial Litigation in Federal Courts.

Mr Cooper joined the firm in 2003 and became a partner in 2011. He received a JD from Columbia University School of Law, a PhD in political philosophy from Duke University and an undergraduate degree from the University of Wisconsin. He also served as a law clerk to the Honourable B Avant Edenfield of the US District Court for the Southern District of Georgia.

Mr Cooper is a member of the Bar of New York, and is currently a member of the Committee on Securities Litigation of the Bar Association of the City of New York and of the Board of The Fund for Modern Courts.
SUZANNE CORREY
Maples Group

Suzanne Correy is a member of the Maples Group’s corporate and Latin American teams. She has extensive experience in all aspects of corporate work, including joint ventures, IPOs and M&A, and also advises on a wide variety of structured finance, capital markets and investment fund transactions. Suzanne maintains a strong focus on public company work, advising clients through all stages of their growth from start-up to IPO and beyond.

Through her Latin American practice, Suzanne advises clients both originating from and investing into the region. She has also advised telecommunications clients and hardware companies on Cayman Islands licensing and regulatory issues.

GUILLERMO DE LA ROSA STOLK
Torres, Plaz & Araujo

Guillermo de la Rosa Stolk has been a senior partner at Torres, Plaz & Araujo since 1992 and became a member of its board of directors in 1996. He joined the firm in 1984 and became a junior partner of the firm in 1988. Before joining Torres, Plaz & Araujo, he worked at Chadbourne, Parke, Whiteside & Wolf (currently Chadbourne & Parke LLC) in its New York office as a foreign associate (1983 to 1984).

He received his graduate degree from the Universidad Católica Andrés Bello (Caracas) in 1982. Furthermore, he completed postgraduate studies in comparative law at the Inter-American Law Institute, New York University School of Law (1983) and in financial law at the Universidad Católica Andrés Bello (1994).

He has devoted his practice not only to assisting the firm’s clients’ regular corporate needs, but has also been very active in numerous domestic and international transactions, including, but not limited to asset protection and cross-border structuring. He also advises on both federal and municipal taxes and estate planning. In his practice, Mr de la Rosa Stolk deals with domestic and international clients, the latter being from America, Europe and the Far East.

On the academic side, Mr de la Rosa Stolk has taught as a guest professor on the masters of economic law programme at the Pontificia Universidad Javeriana in Bogotá, and also on the specialisation in finance at the Instituto de Estudios Superiores de Administración in Caracas.

He is a member of the International Bar Association and the Inter-American Bar Association (Venezuelan Chapter), and represents Torres, Plaz & Araujo at the Capital Markets Committee of the Venezuelan-American Chamber of Commerce & Industry and at the Venezuelan-Colombian Economic Integration Chamber, of which he has been head of the legal committee and a member of its board of directors. Mr de la Rosa Stolk was a member of the board of directors of Mavesa SA, a former publicly traded large industrial food conglomerate, from 1994 to 2000. He speaks Spanish and English.

OLHA DEMIANIUK
Baker McKenzie

Olha Demianiuk is a partner in Baker McKenzie’s corporate M&A practice group and the head of the firm’s healthcare industry group in Kiev. Olha advises on private M&A, both cross-border and domestic, and cross-border equity capital market deals in various industries.
Olha also advises clients on the establishment of joint ventures and corporate restructuring. Olha is recognised by Chambers Europe, IFLR1000, The Legal 500 EMEA and Ukrainian law firm legal directories in M&A and healthcare practices in Ukraine.

**VALMY DIAZ IBARRA**

*Torres, Plaz & Araujo*

Valmy Diaz Ibarra is a graduate of the Universidad Católica Andrés Bello (2001), and has a postgraduate degree in tax law from the Universidad Central de Venezuela (UCV).

He joined the Torres Plaz & Araujo team in 2011 as a general partner. He has been involved in tax advice, litigation and planning for 18 years. As a litigator, he has represented local companies and multinationals before the superior tax courts and the Supreme Tribunal of Justice, challenging tax laws and regulations, as well as tax-deficiency memos issued by federal, state and municipal tax authorities.

He offers tax advice activities related to the application of tax rules, and the tax consequences in personal and corporate reorganisations and contracts.

He is currently an active member of the Venezuelan Tax Law Association (AVDT). He speaks Spanish and English.

**ROBERT DOOLEY**

*Bae, Kim & Lee LLC*

Robert Dooley is an Australian foreign attorney in the corporate group at Bae, Kim & Lee LLC. Robert advises public and private companies, multinationals and regulated entities on a wide variety of corporate and commercial matters, including M&A, joint ventures, corporate governance, commercial contracts, infrastructure investments and corporate restructures.

Before joining Bae, Kim & Lee LLC, Robert practised privately in Australia for nine years, including eight years with Norton Rose Fulbright.

**DENIS DURASHKIN**

*BGP Litigation*

Denis Durashkin is a senior associate at BGP Litigation. Denis is focused on M&A transactions and has more than 10 years of extensive M&A experience, which includes advising major Russian and international companies on complicated multinational deals.

**WILHELM EKLUND**

*Dittmar & Indrenius*

Wilhelm Eklund is a partner at Dittmar & Indrenius and co-head of the firm’s M&A and private equity practice. His work focuses on M&A as well as private equity, securities and corporate law. Mr Eklund has a law degree from University of Helsinki and an MSC (economics) degree in finance from Hanken School of Economics in Helsinki.
MAHA EL-MEIHY

*Maouk Bassiouny & Hennawy*

Maha El-Meihy is an associate at Maouk Bassiouny & Hennawy and a member of the corporate and M&A team.

Maha has worked on several due diligences, specifically corporate and commercial matters. Further, she has given advice on multiple daily matters in connection with the commercial law, the labour law relating to the termination and redundancy of employees as well as working on matters associated with the companies’ law, in particular to the establishment of corporate entities, giving advice on daily matters, organising and drafting the minutes of meetings, and drafting contracts including share and purchase agreements in addition to various contracts depending on the needs of the client.

RICHIE FALEK

*Winston & Strawn LLP*

Richie Falek, a partner in Winston’s New York office, has been lead antitrust counsel in hundreds of domestic and multinational transactions covering myriad industries including numerous multi-billion dollar transactions. He has closed transactions representing more than US$1 trillion in value. Richie’s primary goal is to get transactions closed with as little impact and distraction caused by the antitrust process as possible. He takes a holistic approach, overseeing all aspects of a transaction, beginning with the analysis of potential antitrust issues before the transaction is structured, through the negotiation of asset purchase or similar agreements, and then through the completion of the Hart-Scott-Rodino process and any other regulatory approvals. He has extensive experience with the Department of Justice, the Federal Trade Commission, and state and foreign regulators.

JÓZSEF BULCSÚ FENYVESI

*Oppenheim Law Firm*

Dr Fenyvesi graduated from the Janus Pannonius University of Pécs in 1998 and pursued postgraduate studies in EU law at the University of Pécs. He obtained an LLM in international economic law at the University of Warwick in 2004, and attended the University of Oxford as a Chevening scholar and received a *magister juris* degree in 2006. Mr Fenyvesi joined the Budapest office of Freshfields Bruckhaus Deringer in 2005. He became an associate of Oppenheim in 2007 and has been a partner at the firm since 2010. Mr Fenyvesi has been the head of the corporate practice of Oppenheim since 2014.

LAURA FERNÁNDEZ-PEIX PÉREZ

*Russin, Vecchi & Heredia Bonetti*

Laura Fernández-Peix Pérez is a senior associate at Russin, Vecchi & Heredia Bonetti. She provides legal assistance and consulting to firms and investment projects in all matters relating to their legal needs, particularly in areas related to contracts, commercial and corporate law. She has represented several companies in corporate reorganisation processes, such as mergers, spin-offs, acquisitions, dissolutions, corporate restructuring, tax planning, in-kind contributions, transfers of shares, transfers of assets, and the incorporation and registration of non-profit organisations.
SEOW HUI GOH

Bird & Bird ATMD LLP

Seow Hui leads the Bird & Bird Singapore employment practice, and her practice encompasses the full range of employment issues, including HR regulatory and compliance issues. She regularly advises corporate clients on employee issues arising from business restructuring needs, mergers and acquisitions, including employment due diligence, managing employee terminations, particularly complex exit negotiations, protection of employer trade secrets and confidential information, employment contracts, executive compensation and benefits, workplace policies, employee relations, workplace grievances and investigations, workplace ethics and compliance, workplace safety and health, work injury claims, industrial relations and collective bargaining, HR personal data protection, global mobility and immigration.

Seow Hui frequently represents companies in employment disputes, and clients value her methodical approach and pragmatic advice.

Her work covers Singapore and cross-border work into the region, with a particular focus on ASEAN. Seow Hui is also experienced in managing large-scale and complex regional restructuring and integration projects.

Seow Hui is an accredited mediator with the Singapore Mediation Centre and a member of the Association of Workplace Investigators.

EDUARDO GONZÁLEZ

Creel, García-Cuéllar, Aiza y Enríquez, SC

Eduardo González is a partner in the Mexico City office. His practice focuses on M&A, representing buyers, sellers, boards of directors and financial advisers in connection with complex transactions, including M&A, private equity deals, spin-offs, joint ventures, strategic alliances, minority investments and asset sales. Among other things, Mr González regularly advises large multinationals and global private equity investors and sponsors on acquisitions and investments in Mexico across multiple industries.

Mr Gonzalez has been repeatedly recognised as one of the country’s leading practitioners in M&A by specialised publications such as Chambers and Partners Latin America, Who’s Who Legal and The Legal 500.

Mr González has authored and co-authored several articles on M&A and private equity-related topics for prestigious publications including The Chambers Legal Practice Guide and The Private Equity Review.

MARK I GREENE

Cravath, Swaine & Moore LLP

Mark I Greene serves as the head of Cravath’s corporate department and as the leader of its international practice. His practice focuses on M&A, corporate governance and securities matters, including advising on cross-border transactions, private equity deals, complex restructuring transactions, proxy fights, takeover defences, hedge fund activism and global securities offerings.

Mr Greene has long been recognised as one of the world’s leading M&A practitioners by, among others, Chambers USA, Chambers Global, The Legal 500 United States, The Legal 500 Latin America and IFLR1000. In 2018, he was named the ‘Cross-Border Dealmaker of the Year’ by The Deal.
Mr Greene received a BA from Cornell University in 1989 and a JD from the University of Pennsylvania in 1993. After a clerkship with the Honourable Charles Legge of the US District Court for the Northern District of California, he joined Cravath in 1994 and became a partner in 2001.

RICHARD HALL
Cravath, Swaine & Moore LLP

Richard Hall is a partner in Cravath’s corporate department. His practice focuses on M&A, corporate governance advice and matters relating to activist defence. Mr Hall is the head of Cravath’s M&A practice for EMEA.

Mr Hall has been repeatedly cited as one of the country’s leading practitioners in M&A by, among others, Chambers USA, Chambers Global, The Legal 500 United States, The Legal 500 Latin America and IFLR1000. He was named a ‘Dealmaker of the Year’ by The American Lawyer in 2018.

Mr Hall received a B Com with honours in 1984, an LLB with honours in 1986 from the University of Melbourne and an LLM from Harvard University in 1988. He joined Cravath in 1988 and became a partner in 1996.

ROBERT HANSEN
McCarthy Tétrault LLP

Robert Hansen is a partner in McCarthy Tétrault’s business law group. His practice focuses on the purchase and sale of shares and assets of public and private companies, with additional experience in continuous disclosure and corporate governance matters. Recognised as a skilled dealmaker, Robert has acted as lead counsel in a range of complex transactions, providing strategic advice and innovative insight on some of Canada’s most high-profile deals while successfully pursuing his clients’ objectives.

Robert is on the faculty of the Directors College, Canada’s first university accredited corporate director development programme, founded by the Conference Board of Canada and the DeGroote School of Business at McMaster University. He also teaches an advanced securities law seminar at the University of Windsor and Western University. Robert received his LLB from Osgoode Hall Law School in 1997, and was called to the Ontario Bar in 1999.

Robert is recognised as a leader in corporate law, securities, M&A and private equity by Chambers and Partners, Lexpert and IFLR1000. In 2008, he was named a ‘Rising Star’ by Lexpert, an accolade given to Canada’s top 40 lawyers under 40.

TARO HIROSAWA
Nishimura & Asahi

Taro Hirosawa is a partner at Nishimura & Asahi and is admitted to the Japan Bar (2005) and the New York Bar (2014), and is registered as a foreign attorney in Vietnam (2013). He is a graduate of Tokyo University (LLB, 2004) and Duke University School of Law (LLM, 2013). Since August 2013, he has practised law at Nishimura & Asahi’s Vietnam office. He has varied experience in cross-border transactions between Japan and Vietnam, and in providing legal advice to foreign-invested companies in Vietnam.
CHRISTIAN HOEDL

_Uría Menéndez_

Christian Hoedl is a lawyer in the Madrid office of _Uría Menéndez_. He joined the firm in 1987 and became a partner in 1998. He was resident partner in the firm’s Bilbao office between 1999 and 2001.

Christian focuses his practice on M&A and private equity.

He heads the M&A and private equity practice area at _Uría Menéndez_. He has participated in a large number of private equity deals for national and international funds, with or without a presence in Spain, both in private and P2P deals. Christian has extensive experience in M&A and joint ventures, and has also advised on financing, directors’ bonuses and refinancing in private equity-owned companies. He acts as secretary to the board of several companies.

He is recognised as a leading lawyer by the main international legal directories (_Chambers & Partners_, _PLC_, _Who’s Who Legal_, etc.).

HANS HENNING HOFF

_Heuking Kühn Lüer Wojtek_

Hans Henning Hoff is qualified in both Germany and Iceland. He studied law, Scandinavian languages and history at the universities of Erlangen, Reykjavík and Bonn, and obtained his _Dr jur summa cum laude_ from the University of Munich with a thesis on the influence of Roman law on the oldest written Icelandic law.

Hans advises domestic and international corporate clients and financial institutions in Germany and in Iceland. His areas of practice are corporate and commercial law with a special focus on energy-related projects. Hans also has considerable experience in real estate transactions. Regarding corporate law, he advises his clients with regard to M&A transactions, corporate restructurings and joint ventures on an ongoing basis.

PHILIPPE HOSS

_Elvinger Hoss Prussen_

Philippe Hoss became a member of the Luxembourg Bar in 1987 and joined Elvinger Hoss Prussen in 1988, where he has been a partner since 1990.

Philippe holds a _maîtrise en droit_ and a postgraduate degree (DEA) in business law from the _Université Paris 1 Panthéon-Sorbonne_ (France).

He lectures on various business and financial matters at the University of Luxembourg, and on company law as part of the course for admission to the Luxembourg Bar.

He has been a member of the board of directors of the ILA (Luxemburg Institute of Directors) since 2010 and a member of the Capital Market Committee set up by the CSSF (Financial Sector Supervisory Commission).

Philippe’s principal fields of activity are M&A, capital markets, banking and finance, and securitisations.

Philippe authored the first published English translation of the law of 10 August 1915 on commercial companies and of all subsequent updates thereof.
MASAKAZU IWAKURA
TMI Associates

Masakazu Iwakura is a senior partner at TMI Associates. He obtained an LLB from the University of Tokyo in 1985 and a LLM from Harvard Law School in 1993, and is qualified to practise in Japan and the state of New York.

Mr Iwakura has handled a variety of large-scale and unprecedented M&As, inter alia, Japan Post’s acquisition of Toll Holdings, Idemitsu Kosan’s acquisition of Showa Shell Sekiyu shares from Royal Dutch Shell, the integration of UFJ Bank Group and Mitsubishi Tokyo Financial Group (MUFG), the acquisitions of AIG Edison Life Insurance and AIG Star Life Insurance by Prudential Financial, and the demutualisation and GPO of the Dai-ichi Mutual Life Insurance Company.

Mr Iwakura has lectured on corporate law, M&A law and other laws at various law schools and universities for more than 25 years. He was a visiting professor of law at Harvard Law School in 2007 and 2013 academic years and a lecturer at Kyoto University Law School from 2005 to 2007; furthermore, he has been professor of law at Hitotsubashi University, Graduate School of Law, Department of Business Law, since 2006.

THIERRY KAUFFMAN
Elvinger Hoss Prussen

Thierry Kauffman became a member of the Luxembourg Bar in 2009 and joined Elvinger Hoss Prussen the same year; he became a partner in 2018.

Thierry holds a maîtrise en droit from the Université Paris 1 Panthéon-Sorbonne (France) and a master’s degree in international private and business law from the Université Paris II Panthéon-Assas (France).

He was the president of the Luxembourg young bar association in 2018 and 2019.

Thierry’s principal fields of activity are M&A, capital markets, corporate and finance.

HEINRICH KNEPPER
Hengeler Mueller Partnerschaft von Rechtsanwälten mbB

Heinrich Knepper received his law degree after studying at the universities of Regensburg, Germany and Paris II Panthéon-Assas. He was admitted to the German Bar in 1996 and began his career at the Berlin office of Hengeler Mueller.

Mr Knepper has been a partner at Hengeler Mueller since 2001. From 2003 to 2006 he headed Hengeler Mueller’s London office, before returning to Frankfurt. He advises both German and international corporate and financial clients on private and public M&A and on debt financing, in particular acquisition finance with a focus on leveraged buyout transactions, as well as restructuring transactions.

MELTEM KONING-GUNGORMEZ
Kennedy Van der Laan

Meltem specialises in private equity and venture capital transactions, M&A, corporate governance and international restructurings. She advises private equity and venture capital investors, management teams and entrepreneurs on management buyouts and exits. Corporations often seek her advice on reorganisations, acquisitions and disposals. Meltem
works extensively with (mostly US or UK-based) international corporations who want to add the Netherlands to their geographical footprint, and advises foreign investors doing business in the Netherlands. She has a particular track record in the technology, media and retail sectors. Meltem helps her clients to achieve their goals by providing practical, stage-appropriate, business-oriented advice. Prior to Kennedy Van der Laan, Meltem advised high-profile clients on public and private M&A and private equity transactions in both Amsterdam and New York.

MEREDITH KOTLER
Cleary Gottlieb Steen & Hamilton LLP

Meredith Kotler is a partner at Cleary Gottlieb Steen & Hamilton LLP based in New York. Ms Kotler’s practice focuses on securities, M&A, general commercial and shareholder derivative litigation, in federal and state trial and appellate courts. She regularly represents clients in securities class actions and a host of corporate governance matters.

Ms Kotler has been recognised as a leading lawyer by Chambers USA, Benchmark Litigation and The Legal 500 US, and has spoken on securities issues and other topics before the Practising Law Institute, the SEC Institute and the Compliance, Governance and Oversight Council. Her writings on the latest developments in Delaware courts and deal litigation have been published in the Harvard Law School Forum on Corporate Governance and other outlets.

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After spending several years near the beginning of his career at McCarthy Tétrault, he joined the in-house legal team at the Canadian Imperial Bank of Commerce (CIBC) and CIBC World Markets Inc., where he managed the legal aspects of almost all of CIBC’s strategic transactions globally and led a large legal team that spanned across several continents. He served on the board of directors of CIBC’s Canadian and European investment banking subsidiaries, and was a member of most of CIBC’s key governance and deals committees. He returned to McCarthy Tétrault in 2018.

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He has been involved in a number of M&A transactions, including tender offers, residual tender offers and squeeze-outs. He has been counsel to financial advisers in connection with M&A and securities transactions. Mario Santa Maria was a member of the Italian desk based at Greenberg Traurig, New York and worked at another important US law firm. He is a Columbia University School of Law LLM graduate (Harlan Fiske Stone Scholar) and is admitted to practise both in Italy and in New York.
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He regularly advises foreign and Italian clients on commercial, banking and corporate matters, assisting them in the completion of corporate transactions, including joint ventures, commercial cooperation agreements and settlement negotiations. He worked at the New York offices of Greenberg Traurig LLP, and is a New York University LLM graduate admitted to practise in both Italy and New York.

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Sandra has spoken widely on contract, governance and competition issues. She is also the co-author of *Business Guide to Competition Law*, published by Sweet & Maxwell in 2011. She sits on the council and executive committees of industry associations such as the Sustainable Energy Association of Singapore, the Energy Studies Institute, SGBC and the Waste Management & Recycling Association of Singapore, and is a director of two local charities.

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Christian Thaler is a graduate of the Law School of Vienna University and, after graduation, spent several years as an assistant professor and lecturer in the civil law and business law departments of Vienna University and spent an Erasmus term at Université René Descartes – Paris V in France.

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Michiel is a corporate and M&A partner. Active in the region since 2009, Michiel has represented some of the leading state-owned and private sector companies in the Middle East on a range of M&A and corporate finance transactions. He led the team on the US$5.3 billion Barwa/Qatari Diar asset sale transaction, which was recognised as the ‘Domestic M&A Deal of the Year’ at the 2014 *IFLR* Middle East awards. *Chambers* has praised him as ‘an excellent lawyer on M&A transactions’.
Michiel’s experience is both extensive and truly global. He has advised on closed M&A transactions involving targets located in the United States, Brazil, Russia, Qatar, the United Arab Emirates, France, Germany, the Netherlands, Turkey, Spain, Italy, the United Kingdom, Greece and Japan.

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