Quarterly Update (June 2020)

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1. Public M&A: Key Precautionary Defenses in the COVID-19 Environment

- **Background.** Market valuations are currently depressed in sectors that have been adversely affected by the COVID-19 pandemic. As occurred during the 2008 financial crisis, some European-listed companies are examining defensive measures to seek protection against opportunistic unsolicited bidders or corporate raiders who may take advantage of current depressed share prices. Although the range of defensive measures could be extensive, in some European jurisdictions, issuers have recently focused on certain preventive actions, including (i) private investments in public equity, or "PIPE," transactions, (ii) rights plans (or "poison pills") and (iii) caps on voting rights exercisable at the general meeting. In addition, the recent strengthening of foreign investment screening regimes by several European governments may act as an effective shield against some non-domestic bidders and activist investors.

- **Trends.** While during the first few weeks of the COVID-19 outbreak issuers and PE firms were more focused on closing transactions that had already signed (or even terminating or renegotiating transactions), as well as on internal and operational/liquidity issues for existing businesses, it is now likely that potential bidders could begin looking at European targets that have become more affordable. Despite the market recovery during the last few weeks, market valuations of listed entities may currently still be attractive and PE firms continue to sit on considerable amounts of uninvested cash (or "dry powder"). For example, in 2019, Blackstone is reported to have raised $26 billion for its latest BCP VIII fund; Advent raised $17.5 billion for its GPE IX fund; Cinven raised €10 billion for its seventh fund; and KKR raised €5.8 billion for its biggest EU fund to date.

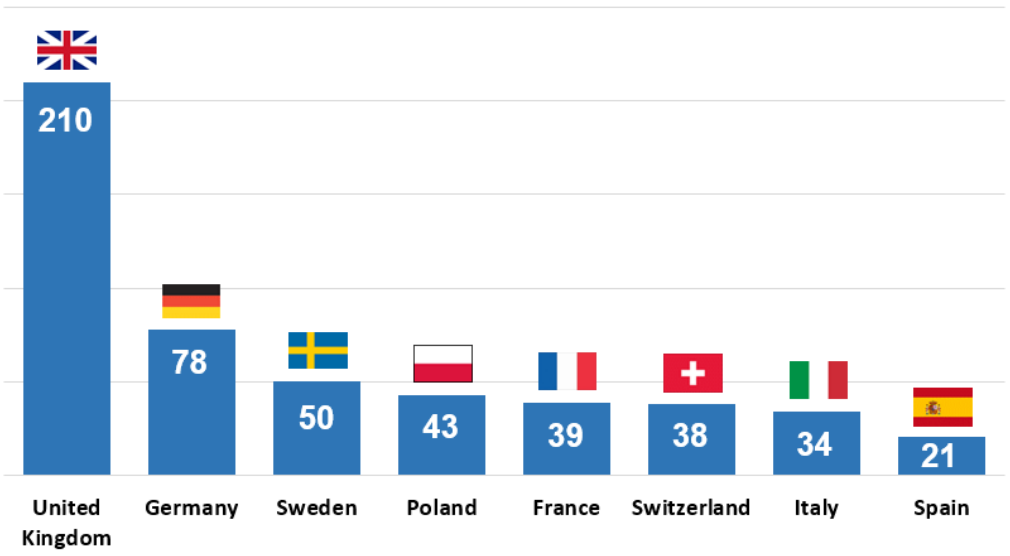
  "Purely" unsolicited takeover offers – where the board of the target does not recommend the offer for the duration of the offer – are still unusual in the European market. In France, for example, while 21 "purely" unsolicited tender offers were recorded before 2000, only 7 have been recorded since then (including Vivendi/Gameloft in 2016 and Foncière Paris France/PHRV in 2011). In Germany, unsolicited approaches are likewise the exception rather than the rule, although the number of situations in which listed targets have resisted takeover bids outright or opposed solicitations have increased (*e.g.*, then DAX-listed K+S against the takeover proposal by Canadian rival Potash (2015); MDAX-listed Uniper against Finnish competitor Fortum (2017); unsolicited takeover offer by Morgan Stanley Infrastructure for VTG in 2018 followed by a delisting offer in 2019). While the number of hostile takeovers has traditionally been higher in the UK than in other European countries, in recent years the number has trended downward.

Shareholder activism, by contrast, is a day-to-day topic that European companies are facing more frequently – and it is a phenomenon that has favored the occurrence of transactions that the listed target company opposed at the outset. For example, the recent fierce opposition between the activist hedge fund Amber Capital and the French media group Lagardère resulted in Vivendi acquiring a 13.36% stake in Lagardère; the campaign by AOC for Stada led to the bid by Bain/Cinven (2017); and Elliot Advisors also supported in 2019 the ultimately successful hostile offer by Melrose for GKN in the UK. In 2019, non-U.S. campaigns accounted for approximately 40% of total activist campaigns. The focus of shareholder activism on European public companies in particular has increased in recent years:

- between 2014 and 2018, activist campaigns in Europe increased by 99%; and
- during 2018, approximately 25% of the activist campaigns directed at companies with a market cap of more than $500 million were targeted at European companies.

With a sizeable portion of these campaigns launched in the context of event-based investing, shareholder activism can be expected to continue to act as a catalyst for M&A processes.

Number of companies publicly subjected to activist demands between Jan. 1, 2013 and Sep. 30, 2019
(by company HQ location)



Source: S&C, based on Activist Insight, Activist Investing in Europe, 2019

- **Selected Landmark Hostile Bids:**
  - **Vonovia/Deutsche Wohnen (Germany).** One of the most iconic takeover fights unfolded towards the end of 2015 amid rising prices in the German residential real estate sector when Deutsche Wohnen, the second largest player, signed an agreement to take over LEG Immobilien which holds the country's third-largest portfolio. DAX-listed Vonovia, which holds approx. twice the size of Deutsche Wohnen's portfolio, launched a EUR 14 billion hostile proposal to acquire Deutsche Wohnen and pushed it to let go of its signed LEG deal. Following the announcement of Vonovia's acquisition attempt, Deutsche Wohnen management used various defensive measures to foil the unwelcome bid, including the expansion of its own portfolio through M&A, the indication of willingness to cash-settle outstanding convertible loans and direct communication with Vonovia shareholders disputing the merits of the deal. In January 2016, despite reducing the minimum

acceptance threshold, Vonovia's offer failed due to a lack of support by Deutsche Wohnen shareholders.

– **Wavecom/Gemalto (France).** Although more recent hostile bids exist, the 2008 Wavecom/Gemalto takeover battle appears particularly pertinent in the context of the COVID-19 crisis. At a time of unprecedented financial market turmoil on the back of the 2008 financial crisis, the Dutch world leader in digital security Gemalto filed in October 2008 an unsolicited takeover bid for Wavecom, a leading provider of embedded wireless technology for M2M (machine-to-machine) communication listed both in France and in the U.S. Gemalto's offer was perceived as highly opportunistic by Wavecom's boards of directors and therefore rejected. While seeking a "white knight" through Sierra Wireless Inc., a Canadian wireless modem maker, Wavecom convened a shareholders' general meeting in December 2008 to approve a rights plan and thereafter issued to its existing shareholders free equity warrants having a substantial dilutive effect. In light of these defensive actions, Gemalto withdrew and terminated its tender offer in France and in the U.S. on January 9, 2009.

– **Teva/Mylan (The Netherlands).** In 2015, the takeover fight between Israel's Teva Pharmaceutical Industries Ltd. and its rival generic drugmaker Mylan NV highlighted the powerful "*stichting*" Dutch-law defensive instrument. In order to fend off Teva's $40 billion hostile bid, the Dutch-domiciled company entered into an agreement in April 2015 with an independent foundation (a "*stichting*") that provided for the issuance of preferred shares to the latter upon exercise of a call option, allowing it to buy 50 percent of the company's total issued and outstanding capital. The foundation exercised its call option in July 2015, arguing that a Teva takeover would likely lead to redundancies at Mylan and reduce access to cheap generic medicines in emerging markets. A few days later, Teva abandoned its hostile takeover bid for Mylan, opting instead to acquire Allergan Plc's generic-drug business in a $40.5 billion deal.

- **Focus on Certain Defenses in the COVID-19 Environment:**

– **PIPE Transactions.** As occurred during the 2008 financial crisis, many European-listed companies are raising capital for liquidity reasons, but some European issuers are also seeking "anchor investors." Such investors may help protect against opportunistic unsolicited bidders and corporate raiders. Although no two crises are ever quite the same, private investments in public equity, or "PIPE," transactions may be an appropriate solution for some European companies under pressure in the context of the COVID-19 pandemic. However, for such companies, it is prudent to choose the proposed investors carefully.

For capital raisings in sectors adversely affected by the Covid-19 pandemic, the risk premiums and therefore discounts over share prices that institutional investors would typically request may be discouraging issuers from going out into the market. However, some investors, such as strategic buyers, large family offices or private equity funds may have special insights into certain sectors and may therefore be willing to move forward at acceptable prices or to enter into broader transactions, which may include cooperation arrangements and the like.

In companies that are the hardest hit by the economic turmoil, private placements may not be feasible at attractive prices, requiring issuers to resort to more broad based measures, such as rights offerings. While these can secure a company's financial position, they do not give the same degree of defense against unsolicited takeovers.

Governance rights, anti-dilution protections and conversion and redemption rights are generally the key terms investors focus on in significant PIPE transactions, beyond pricing.

On governance, the rights negotiated often depend on the expected depth and duration of the relationship between the issuer and PIPE investors. The larger the equity stake, the more robust the governance rights. Usually, these rights include, *inter alia*: (i) board rights (meaning the right to appoint a specified number of directors to the board/committees); (ii) voting and consent rights (which may include veto rights over key corporate actions taken by the issuer); and (iii) where relevant, registration rights (to provide for future liquidity of the stock to be issued if a PIPE investor subscribes for an instrument). Issuers may also seek to negotiate standstill provisions or lockup agreements. Depending on the jurisdictions, PIPE transactions will often involve subscription for an instrument other than shares, but which can convert into shares. Protective features inherent to the instrument itself include dilution protection, conversion measures and optional or mandatory redemption.

- **The French Perspective.** In France, PIPE transactions would generally consist of the issuance of new shares or instruments – such as equity warrants ("*bons de souscription d'actions*" or "*BSA*") or convertible bonds – for the sole benefit of PIPE investors, allowing them in the latter case to freely contribute to the capital of the company (*i.e*., similar to an equity line). A specially-called general meeting of the shareholders would however need to be convened to decide upon the issuance of such instrument to pre-identified PIPE investors. Yet, the PIPE investor would be able to exercise/convert its instrument over a period of time, and, as a result, subscribe to newly issued ordinary shares of the company without having to hold a new shareholders' meeting.

  The issuance would require a special resolution of the shareholders passed by two-thirds of the votes cast (the PIPE investors benefiting from the reserved offering being prevented from voting) whereby the shareholders waive their statutory preferential/pre-emptive rights ("*droit préférentiel de souscription*") over the new shares or instruments and, in the latter case, the new shares to be issued upon the exercise/conversion of the instruments. In addition, for the issuance of an instrument, the general meeting of the shareholders would need to determine *ab initio* (i) the issuance and strike price/conversion ratio of the instrument (which could be a formula) and (ii) the period of time during which the instrument may be exercised/converted. As PIPEs often represent less than 20% of the share capital of the issuer, no prospectus approved by the French financial markets authority – the *Autorité des marchés financiers* (the "AMF") – would be required.

  PIPE investors will need to be cautious not to trigger the obligation to file a mandatory tender offer for all the issuer's equity securities as a result of the PIPE transaction. Under French law, a mandatory bid could be triggered if the investor, acting alone or in concert, comes to hold directly or indirectly more than 30% of the issuer's share capital or voting rights or, if it already holds between 30% and 50% thereof, increases such holding by at least 1% of the issuer's share capital or voting rights within a period of less than 12 consecutive months in France. A waiver from the AMF could however be granted if the following cumulative conditions are met: (1) the issuer is facing "obvious financial difficulties" and (2) the PIPE transaction has been specifically approved by the shareholders' general meeting. This exemption has been relied upon many times since the 2008 financial crisis, although not in the context of PIPE transactions – *e.g.*, Marie Brizard in 2019, Groupe Flo in 2017, Solocal Group in 2016 and Belvédère in 2013.

- **The German Perspective.** In Germany, PIPE transactions come in various forms and are typically bespoke agreements to accommodate the parties' interests. Unlike in other jurisdictions such as the United States, the issuance of "naked warrants" is generally impermissible and achieving similar economics requires sophisticated structuring to comply with the restrictions German law poses – a PIPE transaction against a cash consideration is typically restricted to 10% of a company's shares and often conducted on the basis of a pre-approval by the company's shareholders' meeting. One alternative is the issuance of convertible bonds to an investor: the shares underlying the convertible are issued under the issuer's "conditional capital", the creation of which, as well as the authorization to issue the bonds, typically requires a 75% majority. One prominent example includes SoftBank's approx. EUR 900 million 2019 investment in Wirecard which was accompanied by a cooperation agreement. In the context of the COVID-19 crisis, the German government has come to the rescue of Lufthansa; the investment package reportedly includes a 5% convertible bond (besides a 20% direct investment) that the government would only seek to turn into shares under the aegis of a hostile proposal.

In Germany's most prominent PIPE investment in the midst of a disputed takeover process, Hochtief AG issued new shares to Qatar Holding and prominently welcomed the new approx. 10% shareholder. The move was interpreted by the market as a "white squire" defense tactic against the pending advances by Spanish competitor ACS. PIPE investments up to 10% may be conducted on the basis of a pre-authorization by the shareholders' meeting if the new shares are issued against a cash contribution and carry no significant discount over prevailing market levels.

- **The UK Perspective.** The UK Code on Takeovers and Mergers (the "Code"), which governs the conduct of takeover offers for many UK-listed companies, operates on the basis that it is the company's members who should evaluate the merits or otherwise of an offer, even a hostile offer, and that the target board should not take action to hinder its shareholders' ability to make their own decision on the merits of an offer. As such, the Code contains specific provisions which ensure target shareholders' consent must be obtained if the target board wants to take most forms of defensive actions, such as an issue of new shares or warrants (under a rights plan or otherwise) or take any step intended to (or which may) frustrate an offer or prevent target shareholders from deciding on the merits of an offer, when a target board believes a takeover offer is imminent.

  In any event, in recent years, especially since the takeover of Cadbury by Kraft in 2010, which led to a number of target-friendly amendments to the Code, hostile offers have become increasingly difficult to effect. Given the provisions and operation of the Code, it would therefore be unusual for a UK-listed company to adopt a specific strategy of seeking out a strategic investor to create a defensive block against an opportunistic bidder (other than, occasionally, as a white knight during an active offer situation) or to adopt a rights plan, as described below, to attempt to thwart a hostile bidder.

  While in other jurisdictions, directors can point to the need to protect shareholders in taking defensive actions, in the UK such a justification would not generally be sufficient given the provisions of the Code. That being said, placings to raise funds from new investors do take place in the UK, though these are generally effected more for liquidity or financing reasons than defensive ones. There are limitations on the amount of shares that can be issued during such fundraisings without shareholder approval, though most companies will have a standing annual authority to issue shares on a non- pre-emptive basis for up to 5% of the issued share capital with an upper limit of no more than 7.5% over a rolling three-year period. These limits on non- pre-emptive offers come from guidelines issued by the Pre-emption Group. As a result of many listed companies seeking emergency funding in the context of the Covid-19 pandemic, the Pre-emption Group recently advised that for a temporary period until the end of September 2020 it would advise its members to vote in favor of general disapplication of pre-emption rights sought at general meetings of up to 20%. Various mechanisms can be adopted, such as a cash box placing, to circumvent the need to obtain shareholders' consent to disapply pre-emption rights, though some have questioned the legality of such mechanisms. As in France though, the PIPE transaction may trigger the obligation to file a mandatory tender offer for all the issuer's equity securities. Only a vote of a simple majority of independent shareholders could avoid the need for a mandatory offer.

Of course, a target board can, and indeed should, put up a defense, if it doesn't believe the offer provides sufficient value to its shareholders. However, these defenses should be argumentative, and set out in a defense document made available to the shareholders, rather than actions which remove the ability of shareholders to make a decision. Other permitted defensive actions include finding an alternative and preferred "white knight" bidder to make a counter offer, issuing new financial and other information favorable to the target, obtaining expert valuations of key assets to try to demonstrate that the bidder's offer is too low, attacking the deliverability or timetable of the bidder's offer – particularly the obtaining of regulatory clearances – and making strong representations to regulators to refuse to grant approval to the offer.

– **Rights Plans.** Traditional takeover defense rights plans may also be suitable for companies under pressure in the COVID-19 context, although they are not available in every EU jurisdiction.

  Conceptually, takeover defense rights plans can be kept "on the shelf" by the issuer until they are needed in the context of an unsolicited takeover or activist approach. When implemented and triggered, they result in an automatic and substantial dilution of the unsolicited bidder's investment in the company by permitting the other shareholders to acquire additional shares at a significant discount to market prices.

  When seeking to adopt a rights plan, it is critical that the board of directors clearly communicate the rationale for adopting such a poison pill to the shareholders and the market. Institutional investors such as Vanguard and BlackRock and proxy advisory firms such as ISS and Glass Lewis continue to have policies that could result in them taking negative action against a board of directors that adopts a rights plan. Companies should therefore attempt to anticipate their reactions. However, in the context of the COVID-19 crisis, ISS has been more open to takeover defense rights plans to the extent they are appropriately tailored (*e.g.*, poison pill with a duration of less than a year, relevant reasons for adopting the pill (such as imminent threats), commitment to put renewals of the pill to a shareholder vote, etc.). As such, ISS has encouraged boards to provide detailed disclosure about their choice of duration of the rights plan.

  - **The French Perspective.** Under French law, the board of directors of the target company has the right to take any measure to frustrate an unsolicited tender offer, to the extent such actions fall within the corporate interest of the company. Subject to this general principle, rights plans may be used in France as a takeover defense measure. The French *Code de commerce* has specifically designed the framework of takeover defense rights plans: they take the form of equity warrants ("*bons de souscription d'actions*" or "*bons d'offre*") that are granted during the offer period to the existing shareholders of the company, allowing them to subscribe for newly issued shares of the company for a discounted price. Upon exercise of the warrants after the offer period, the shareholding of the unsolicited bidder in the target company would be massively diluted. The pill could therefore be a strong deterrent and encourage potential bidders to negotiate the terms of the transaction with the target board of directors. The target company could convene a shareholders' meeting either during the offer period to decide upon the issuance of the equity warrants at a simple majority of the votes cast or, to be on the safe side and benefit from the deterrent effect of the "ready-to-go" poison pill, before the company is put into play. In doing so, the shareholders would delegate their powers to the board of directors to issue the defensive equity warrants for a 12- or 18-month period following the vote, thus allowing the board to move quickly when time is of the essence, but also requiring issuers to renew their authorizations on a yearly basis.

To date, Bouygues is the only issuer of the CAC40 index that has renewed its takeover defense rights plan in 2020. Accor and PSA are expected to follow shortly – they have put a resolution in this respect to the agenda of their annual general meetings scheduled for the end of June 2020. As of the date of this publication, no further issuer of the CAC40 index has announced its intent to call for a shareholder vote on a preventive rights plan.

- **The German Perspective.** German law does not provide for "poison pills."
- **The UK Perspective.** The Listing Rules, which regulate the listings of companies listed on the Main Market of the London Stock Exchange, prohibit most forms of rights plans as one of the fundamental rules for Premium listed companies is that all shareholders must be treated equally. A plan which discriminates against one shareholder would fall foul of this rule. Standard listed issuers are not subject to such a restriction. However, rights plans are not a normal part of a UK-listed company's capital structure, even for Standard listed companies.

– **Cap on Voting Rights.** Unless the relevant corporate law prohibits a cap on the total number of voting rights per shareholder in a listed company (which is the case in Germany and the UK), another useful protection for issuers consists in capping the voting rights of their shareholders at the general meeting, irrespective of the date on which the shares have been purchased. In doing so, the influence and nuisance powers of new unsolicited shareholders could be greatly limited. A disabling threshold to this cap could also be provided if a shareholder comes to hold more than a certain level of share capital or voting rights (*e.g.*, 50.01% or 66.67%) of the issuer following a tender offer.

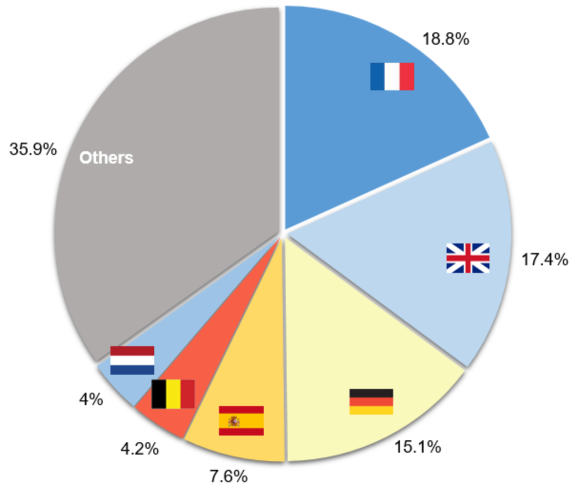
- **The French Perspective.** In France, issuers would need to convene a general meeting to amend their articles of associations – at a two-thirds majority of the votes cast – in order to provide for a cap which would then apply to all shareholders of the issuer, at any general meeting held after the amendment to the by-laws.

  A few companies of the CAC40 index have already provided for caps on voting rights in their articles of associations, including Danone (6% cap and, in case of double voting rights, 12%), EssilorLuxottica (31% cap), Pernod Ricard (30% cap), Safran (30% cap), Schneider Electric (10% cap and, in case of double voting rights, 15%), Société Générale (15% cap) and Total (10% cap and, in case of double voting rights, 20%).

– **Increased Scrutiny of Foreign Investments in Europe.** Although the EU has indicated that it wishes to remain an open market that is attractive to foreign investments, there has been an accelerated policy shift towards increased scrutiny of foreign investments to prevent a sell-off of Europe's strategic assets, including by protecting companies with market valuations well below their "true value" in the COVID-19 environment.

At times of unprecedented financial market turmoil, the European Commission issued a guidance paper on March 25, 2020, urging Member States to use existing foreign investment screening mechanisms or any other tools they may have to ensure the "continued critical capacity of EU industry" in and beyond the healthcare sector. Read more about the European Commission guidelines in S&C's previously released client memo **here**.

Foreign Direct Investments in Europe - Share of project numbers in 2019



Source: S&C, based on EY Attractiveness Survey Europe, May 2020

In this context, France, Germany, Italy and Spain (but not yet the UK) have strengthened their foreign investment regimes which may serve as effective shields against opportunistic unsolicited bidders and activist investors:

- **France.** The government implemented successive reforms to extend the level of control over foreign investments. Following the entry into force of a new set of screening rules on April 1, 2020, the government adopted specific measures in view of the continuing impact of the COVID-19 outbreak on financial markets and issuers' business activities. As of April 30, 2020, the biotech industry has been added to the list of the strategic sectors covered by the foreign investment screening mechanism. The Minister for Economic Affairs also announced it would temporarily lower from 25% to 10% in voting rights the threshold requiring its approval for investments made by non-EU investors in French-listed entities. The underlying decree should be published within the coming weeks and be in force until the end of 2020. Read more about the 2019 reform entered into force on April 1, 2020 in S&C's previously released client memo **here**.

- **Germany.** On April 8, 2020, the government approved a bill from the Federal Ministry of Economics and Energy to amend the Foreign Trade and Payments Act, which will likely result in a higher intervention risk due to a lower standard of review – from an "actual and sufficiently severe threat that affects a fundamental interest of society" to "likely to affect" national public order or security. Further, the addition of new critical sectors in the cross-sectoral review process, resulting in mandatory notifications from non-EU investors when they acquire 10% of the voting rights of German entities operating in artificial intelligence, robotics, semi-conductors, biotech, quantum and satellite technologies can be expected. The legislative proposal had already been initiated before the COVID-19 pandemic in January 2020. Protectionist tendencies have reframed public discussions in Germany regarding inbound transactions since the acquisition of industrial robot manufacturer KUKA by Chinese household appliances manufacturer MIDEA in 2016 and, more recently, the alleged U.S. attempt to acquire CureVac, a German biotech company developing a vaccine against COVID-19, has captured headlines. Read more about the bill approved on April 8, 2020, by the German government in S&C's previously released client memo **here**.

- **Italy.** On April 8, 2020, the government approved a Law Decree widening the scope of the Italian foreign investment regulation. In line with the European Regulation no. 452/2019, the scope of the regime has been extended to cover additional critical sectors, such as the whole banking and insurance sector, as well as the health and food industry. The Law Decree also introduced new temporary thresholds triggering the screening mechanism for investments made in Italian entities holding strategic assets: (1) the acquisition by non-EU investors of 10% of the entity's share capital or voting rights (where the overall investment value is equal to or higher than EUR 1 million) and any subsequent investment therein resulting in crossing upwards the 15%, 20%, 25% and 50% thresholds in share capital or voting rights of such entity; and (2) the acquisition by EU investors of a "controlling interest" thereof. However, these new thresholds are only applicable up until December 31, 2020.

- **Spain.** The government approved two Royal Decrees on March 17 and 31, 2020, to temporarily strengthen the Spanish foreign investment screening mechanism. While before such amendments, the existing regulation only required prior approval for foreign investments related directly to the national defense, the regime has been significantly strengthened and now covers investments from non-EU entities in Spanish targets operating in certain sensitive sectors, where the investor would (i) acquire a stake of at least 10% in the share capital of the Spanish entity or (ii) effectively participate in the management or control thereof. In line with the European Regulation no. 452/2019, critical sectors have also been widened to include, *inter alia*, critical infrastructures, technologies and sectors with access to sensitive information (such as personal data). In addition, the Spanish government would now have a say in any investments made by a foreign state-owned investor in Spain.

- **UK.** As mentioned in our previous European M&A and Corporate Governance Hot Topics issue (available **here**) following the UK general election last year, the new UK government confirmed its plans to introduce a National Security and Investment Bill to strengthen the government's powers to review takeovers on national security grounds. Since then, no bill has been published but a draft bill is expected to be published soon and will be subject to UK Parliamentary approval. However, as a corollary to increasing government powers to intervene in mergers on national security and other grounds not linked to competition issues, the UK's Competitions and Markets Authority has been asserting its jurisdiction in a more muscular way even where there is only a tenuous link to the UK or its markets. This is discussed in section 3 below.

Conversely, 13 Member States (out of 27) still have no such foreign investment screening mechanism, including Belgium and Luxembourg.

2. The Boards' Duties in a Hostile Takeover in Germany

- **Special Obligations.** Following the (binding) announcement of a takeover offer by a bidder, an issuer's management board faces a set of statutory fiduciary duties commonly referred to as the "duty of neutrality." At such time, management is prohibited from adopting any measures that may "jeopardize the success of the offer." A management continues to be free to take any such actions that (i) a "diligent businessperson would have enacted in the absence of an offer," (ii) involve the search for a competing bid and (iii) have been consented by a company's supervisory board.

  There are numerous uncertainties and very few precedent cases regarding the scope of these obligations. In practice, certain key themes have emerged upon which management boards typically rely once they are confronted with the prospect of a (potential) unsolicited advance that they view unfavorably:

  - **Early Adoption of (Revised) Strategy.** Unless the issuer has a shareholder whose participation exceeds 30%, a target's management board is not typically uninformed about a public bid announcement (as has been the case for Deutsche Wohnen in relation to Vonovia's hostile offer) since an acquirer will typically seek to evaluate a consensual transaction. Any strategy adopted during such time of coordination and ahead of the announcement may be continued even if it may impede the bid which is about to be launched. The target may also use any negotiation time with a potential bidder to pursue defensive measures in parallel as the statutory duty of neutrality has not yet set in. Such strategy may include the continued pursuit of M&A plans that could make the launch of an unsolicited bid impractical, including for antitrust reasons. Finally, typical components of a defense strategy include the examination of the target company's financing arrangements and the impact of change-of-control clauses ("poison debt").

  - **Value Defense and Communication.** One key tool for a management board to voice its concerns relating to an unsolicited bid is the communication that would typically start immediately after announcement and may take the form of a communication campaign – often times making the case that the proposal undervalues the company. Such communication has in practice proved critical and reluctant management boards have sought active communication with their shareholder base (including by individualized letters), solicited policy support and used it as their key "defense tool" (*e.g.*, K+S in fending off rival Potash, Uniper in the Fortum transaction and initially KUKA to enter into a favorable investment agreement with Chinese Midea). The stance the target company's boards adopt tends to carry significant weight for the outcome of the offer and their position may result in a de facto "gatekeeper" function. Further, the German Takeover Code provides for the opportunity of the boards to (jointly) issue a so-called "reasoned statement." The document is published during the acceptance period of the offer and gives the boards the opportunity to lay out their position vis-à-vis the offer in detail, and, in particular, to recommend to shareholders whether they should accept.

  - **Regulatory Requirements.** Besides leveraging the increasingly stringent foreign investment regime or antitrust concerns, significant transactions provide for a host of regulatory clearance requirements in respect of which the target company's collaboration or even support may be required. As an example, Uniper's management has not divested its majority holdings in a Russian subsidiary considered of critical importance for the

Russian state, which has effectively capped Fortum (which is majority-owned by the Republic of Finland) at 49.9%. Similarly, a target company may use its existing business activities that would interfere with OFAC requirements to shield itself from a certain set of bidders that are subject to these U.S. regulations (see offer condition in MorganStanley Infrastructures' bid for VTG).

- **"Technical" Defenses.** Target companies' boards have also used certain "technical" defenses after the examination of all tools at their disposal. Deutsche Wohnen announced it would cash-settle its outstanding convertible bonds while hostile bidder Vonovia was relying on the shares underlying the convertibles to be tendered into its offer. Luxembourg-incorporated Braas Monier issued 10% bonus shares to existing shareholders for no contribution which effectively led to an increase of the offer consideration by 10%. Target company Pfeiffer Vacuum examined the offer conditions in the hostile proposal by Busch Group and found that publishing an EGM convention would be sufficient to have an offer condition fail (preempting any potential waiver) due to the structure of the offer's closing condition. However, numerous other typical U.S.-style defense measures such as a "Pac Man" defense, a crown jewel sell-off or golden parachutes are limited in their significance under German law as the boards' fiduciary duties and other corporate law restrictions apply.

3. UK Competition and Markets Authority Asserts Jurisdiction Over – and Prohibits – Mergers with No Real Link to the UK

- **Introduction.** The UK Competition and Markets Authority ("CMA") has continued stretching the boundaries of the "share of supply test" under the Enterprise Act 2002 to assert jurisdiction over acquisitions with no obvious jurisdictional link to the UK. Under the Enterprise Act 2002, the CMA generally has jurisdiction to review mergers if the target's UK turnover exceeds £70 million. If this threshold is not met, then the CMA can assert jurisdiction if the parties have overlapping activities in the UK, and have a combined "share of supply" in the UK (or in a substantial part of the UK) of 25% or more in the supply or acquisition of goods or services of any description (the "share of supply test").

  Notably, recently the CMA's review has resulted in the parties abandoning the merger in two recent transactions, while ultimately in a third review the transaction was cleared. These are summarized below.

- **Recent CMA Merger Reviews based on the Share of Supply Test:**

  - ***Roche/Spark.*** The CMA's review of the acquisition by Roche of Spark Therapeutics, Inc., which it subsequently cleared on December 16, 2019, is one of the most striking examples of the CMA's creative approach to the share of supply test. The CMA considered that it had jurisdiction to review the acquisition, which was reviewed in parallel by the Federal Trade Commission ("FTC") in the U.S., on the basis that Spark would increase Roche's share of supply in gene and non-gene treatments of Hemophilia A in the UK based on the number of UK employees in R&D and the number of UK patents Spark had registered in the UK – notwithstanding that Spark had yet to commercialize any of its (early-stage) pipeline products and that it had zero sales or revenue in the UK. Read more about this transaction in S&C's previously released client memo here.

  - ***Illumina/Pacific Biosciences.*** In its review of the proposed acquisition by Illumina, Inc. of Pacific Biosciences of California, Inc., which was reviewed in parallel by the FTC in the US, the CMA asserted jurisdiction solely on the basis of the miniscule increment of share of supply of DNA sequencing systems that Illumina would gain as a result of its acquisition of

Pacific Biosciences (0%-5%). This demonstrates that the CMA is willing to assert jurisdiction even in a case where the target has little to no turnover in the UK, provided that the acquiring company has a significant market presence in the UK. The CMA's provisional findings, which effectively amounted to a provisional prohibition, ultimately led the parties to abandon the merger on January 2, 2020. Read more about this transaction in S&C's previously released client memo **here**.

1. ***Sabre/Farelogix*****.** The CMA's review of Sabre Corporation's acquisition of Farelogix, Inc. is perhaps the starkest, as well as most recent, example of the CMA asserting jurisdiction on a questionable basis. The decision is also remarkable in light of a federal US court judgment dismissing a lawsuit brought by the Antitrust Division of the Department of Justice in the US to block the merger only two days before the CMA proceeded to block the transaction in its entirety. Highlighting its *"broad discretion"* in applying the share of supply test in a "*flexible and purposive way*," the CMA found the share of supply test to be satisfied merely on the basis of Farelogix' sales to a *single* customer in the US (American Airlines) which had an interline arrangement with UK-based British Airways – notwithstanding the fact that Farelogix had no direct customers in the UK. Although the parties have since announced the termination of the merger, Sabre has lodged an appeal against the CMA's decision to the UK Competition Appeal Tribunal. Read more about this transaction in S&C's previously released client memo **here**.

- **What does this mean for the future merger clearance in the UK?** The CMA's liberal assertion of jurisdiction over mergers is likely to continue. It is the CMA's clear objective to position itself as a prominent competition authority following Brexit. Its bold and creative application of the share of supply test, and its adverse decisions in Illumina/Pacific Biosciences, Sabre/Farelogix, and most recently the (now-abandoned) acquisition of the book publisher Cengage by McGraw-Hill, clearly demonstrate the CMA's ambitions to become a global antitrust authority that is to be taken seriously.

- **What impact will this have on transactions?** The CMA's more muscular assertion of jurisdiction is likely to have onerous consequences for merging parties. Although there is no obligation to pre-notify mergers to the CMA, the resulting uncertainty may cause parties to engage with the CMA on a voluntary basis early on for comfort. Merging parties will need to recognise and carefully manage the impact of a potential CMA merger inquiry. The CMA review process is frequently lengthy and burdensome, requiring special attention and adherence to UK-specific rules, and may cause significant delays to closing. In addition, the CMA's initial enforcement orders can be damaging for acquirers, allowing closing but requiring that the acquiror and the target be held separate and integration be frozen until the CMA clears the transaction. Lastly, the CMA has, and uses, its enforcement powers, including forcing the unscrambling of completed mergers if it concludes that a less drastic remedy will be ineffective, or if the completed merger would prejudice its review.

4. French AMF Proposes New Measures Concerning Shareholder Activism

- **Background.** On January 8, 2020, Mr. Robert Ophèle, Chairman of the AMF, stated in his New Year's greetings that the regulator intended to clarify its approach regarding shareholder activism by the end of Q1 2020. These proposals were published on April 27, 2020, and are in line with several recommendations published by various French institutions, organizations and think tanks since October 2019.

  While acknowledging the role of shareholder activism in improving corporate governance and defending the interests of minority shareholders, the AMF considers that strengthened supervisory measures should be put in place to mitigate or prevent "excessive" activist behaviors that could destabilize issuers, adversely affect the proper functioning of financial markets and, potentially, place investors at a disadvantage. As indicated in the AMF's press release, "*the challenge […] is not how to prevent activism, but how to set limits and make sure that it is able to control excesses*" ("*la problématique n'est […] pas d'empêcher l'activisme mais d'en fixer les limites et de se donner la capacité à en maîtriser les excès*").

- **Key Measures:**

  – **Transparency and Threshold Crossing.** The AMF proposes to enhance transparency on stake-building by lowering the 5% mandatory reporting threshold to, most likely, 3% – the AMF has not adopted a clear position – and making public any crossing of an additional threshold set forth in the company's articles of association. The calculation methodology for testing whether a shareholder has exceeded statutory thresholds is also likely to be harmonized.

Thresholds for notification of major holdings in Europe

Austria	3% if the articles of association have stipulated this and if the FMA has been notified of the threshold (it then becomes the legal threshold) or, by default, 4%, 5%, 10%, etc.
Ireland	3% for Irish issuers, then 4%, 5%, etc.
Germany	3% for voting rights, otherwise 5%
Netherlands	3% of the capital or voting rights
Italy	3% of effective holdings except for SMEs. Otherwise 5%, with the CONSOB being granted flexibility to lower this threshold for non-controlled large-cap companies; the latter criterion was lifted temporarily on 10 April and the thresholds are currently 1% for 104 companies and 3% for the others with a statement of intent to be made at the 5% threshold (instead of 10%)
Spain	3% of voting rights
United Kingdom	3% of voting rights for UK issuers, otherwise 5%
Portugal	3% of voting rights for Portuguese companies

Source: S&C, based on Report by the AMF on shareholder activism, April 2020

  – **Short-Selling and Securities Lending.** The AMF suggests supplementing the reporting on net short positions regarding share capital with information on (i) debt instruments held by the investor (*e.g.*, bonds and credit default swaps) and (ii) the legal entity identifier of the investor. The AMF will therefore support EU proposals in this respect, as it is not competent to directly amend the applicable EU regulatory framework. As regards securities lending, the AMF intends to reiterate, in a recommendation, that it is good practice for fund managers to repatriate loaned securities and effectively exercise their voting right.

  – **Fair and Open Dialogue Among Issuers and Shareholders.** The AMF announced that its guidance on inside information will be revised to include developments and recommendations on shareholder dialogue. In particular, the AMF will revise its recommendation on so-called "quiet periods" to clarify that issuers may provide useful or necessary information to the market, even during a "quiet period," in response to public allegations from activist investors. In addition, the AMF will recommend that investors launching an activist campaign communicate without delay to the relevant issuer any substantial information shared with other shareholders (*e.g.*, white papers). The AMF acknowledges that activist campaigns raise the question of whether public statements made by activist investors should comply with the rules applicable to investment recommendations and will therefore engage with the European Securities and Markets Authority and the European Commission in order to solicit interpretative guidance in this respect. The AMF also announced that it supports the development of shareholder dialogue platforms by issuers.

– **AMF Repressive Actions.** The AMF suggested it be allowed to impose monetary penalties in respect of administrative injunctions and to order investors with a financial exposure to the financial instruments of an issuer to make corrective or supplementary publications, if errors or omissions have been identified in investors' public statements. In addition, the AMF will engage with ESMA to suggest the publication of a "white list" of activist behaviors, which would set out behaviors that may not, in and of themselves, lead to a conclusion that shareholders are acting in concert.

Read more about the new measures proposed by the AMF concerning shareholder activism in S&C's previously released client memo **here**.

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