Bloomberg Law Reports® Mergers & Acquisitions

Cross-Border Mergers & Acquisitions: A Study in Convergence and Cross-Fertilization

Frank Aquila and Brian Hamilton, Sullivan & Cromwell LLP

The increasing level of cross-border transactional activity in the past two decades, particularly between the U.S. and Western Europe, has been accompanied by harmonization of corporate and transactional laws and regulations, as well as cross-fertilization of "deal technology." As demonstrated by the actions of regulators and lawmakers during the global financial crisis of the last few years, rulemakers are influenced by policies of their peers in other jurisdictions and they often are willing to adopt rules that are quite similar to, or sometimes broadly based upon, rules that have been implemented in other countries. Similarly, lawyers, bankers and other advisors have come to move seamlessly across borders and have brought with them and adapted countless deal structuring ideas, innovations and techniques. This type of cross-fertilization contributes to an active transactional environment by allowing the best ideas and practices to develop and take hold, regardless of the market in which they began.

Legal and Regulatory Convergence

An early example of the influence of U.K. corporate law on lawmakers in the United States was evident in the adoption of the Williams Act in 1968. Acting in response to several hostile bid situations in the 1950s (and fearful that legislation would be enacted if it did not act to pre-empt it), the U.K. financial community first provided guidance on the conduct of takeover bids in the late 1950s and early 1960s, which stressed that shareholders should be given relevant information about a bidder before deciding whether to tender into an offer.[1] The rules governing the conduct of tender offers in the U.S. under Sections 14(d) and (e) of the Securities Exchange Act of 1934, first implemented in the Williams Act (which also was enacted in response to hostile deal activity), expanded on this idea so that bidders for listed companies would need to satisfy detailed disclosure requirements and adhere to procedural formalities all meant to level the playing field for shareholders. Since then, virtually every developed market has implemented rules regulating the conduct of, and disclosure regarding, tender offers for the shares of listed companies.[2]

Disclosure of stakebuilding in the shares of listed companies also was first regulated nationally in the U.S. with the adoption of Section 13(d) of the Exchange Act as part of the Williams Act. By forcing shareholders (or groups of shareholders acting together) that have a stake of five percent or more of a listed class of equity to disclose their positions upon crossing the five percent threshold, together with their plans, purposes and proposals with respect to the issuer, including any control intent, Section 13(d) and the related rules are meant to ensure that shareholders cannot be surprised by creeping acquisitions of control, even if the purchases of shares themselves are not made in a manner that would trigger the operation of the tender offer rules. Many European countries have implemented similar early disclosure and "concert party" rules, often triggered at thresholds lower than five percent, although the rules also tend to go one step further by requiring that a shareholder launch a mandatory tender offer for all of the outstanding shares of a company if it crosses a certain threshold. In the U.K., for example, the initial disclosure threshold is three percent, and the mandatory offer threshold is 30 percent, of the outstanding shares.

In the U.S., the Securities and Exchange Commission (the SEC) has implemented a number of rule changes since the late 1990s that have been intended to further cross-border harmonization. In particular, the cross-border rules that it adopted in 1999 and amended in 2008[3] were meant to encourage U.S. shareholder participation in cross-border transactions, particularly where a non-U.S. target did not have a relatively large number of U.S. shareholders. Because U.S. shareholders were routinely excluded from tender offers where the number of shares held by U.S. holders was not enough to be meaningful to the deal (most typically because a squeeze-out threshold could be achieved without the participation of the U.S. shareholders), the SEC recognized that the best way to get more offers open to U.S. shareholders would be to make compliance with U.S. rules easier (provided the SEC's primary goal of investor protection was maintained). The Tier I exemptions from most requirements of the Exchange Act and the Securities Act of 1933, in particular, allow bidders to extend offers into the U.S. without complying with detailed disclosure requirements and most tender offer rules and without needing to register any securities being offered in the deal, on the theory that information provided to shareholders based on home-country disclosure requirements should be sufficient in these situations.[4] Tier II exemptions limit the applicability of certain U.S. tender offer rules,[5] in deference to home-country procedural requirements.[6] Similarly, the SEC has adopted rules, and is considering further changes, to allow financial statements to be prepared and presented in International Financial Reporting Standards,[7] which is a big step toward harmonizing U.S. accounting standards with the standards that are in effect in Europe and elsewhere.

There are many other examples of rules convergence. Corporate governance practices are influenced a great deal by elements that have been introduced successfully in many places. For public companies, a majority of independent directors and a system of board of director committees that are comprised of expert and independent directors (most notably the audit committee) have become standard in the U.S. and Europe. Similarly, the dominant U.K. practice of having a separate chairman and chief executive officer is growing in influence in the U.S. Legislation governing Dutch B.V.s, or private companies with limited liability, is very consciously seeking to adopt the contractual flexibility of Delaware limited liability companies, including allowing for a single board of directors rather than the traditional two-tiered board structure that is common in Europe outside the U.K. The E.U. has implemented a cross-border merger regime that is forcing the introduction of the merger structure for the first time in many countries (which are obliged to adopt implementing legislation). In the U.K., schemes of arrangement (which allow a compulsory squeeze-out if a majority in number representing at least 75 percent by value of the outstanding shares approve the transaction, rather than at 90 percent of the shares to which the offer relates for a tender offer[8]) have become the default transaction form for friendly acquisitions of listed companies in much the same way that mergers are the default form for friendly deals in the U.S.

Transactional Cross-Fertilization

In 1997, Grand Metropolitan plc and Guinness plc merged in a friendly £23 billion transaction, which was structured as a scheme of arrangement under English law. Grand Met's U.S. lawyers[9] insisted that the deal be memorialized in a transaction agreement with representations, warranties and covenants of the type that would be present in a U.S. merger agreement. This approach had not been commonly taken in the U.K. prior to that time. Following that transaction, having this type of central agreement in place with the target at the time of announcement is now standard in the U.K., even when the deal is structured as a friendly tender offer.

"Certain funds" financing, meaning that a bidder cannot subject an offer to a financing contingency and must have unconditional financing in place at the time an offer is made (subject to narrow exceptions), which is required in offers for listed U.K. companies, was a foreign concept for U.S. deals prior to the acquisition of Anheuser-Busch Companies, Inc. by InBev NV in 2008. Because that transaction began on a hostile basis, InBev knew it would be critical to have secure financing in place so that Anheuser-Busch could not attack the offer as being subject to too much uncertainty due to the financing environment, which was very difficult at that time. Although InBev's legal and financial advisors were American,[10] a number of them had experience with U.K. practice and recommended the "certain funds" approach. InBev therefore lined up a syndicate of banks and demanded that they provide financing for the deal on a certain funds basis exactly as they would for a U.K. deal. This aspect of the bid was critical to getting the deal done and it was a key factor in causing the hostile deal to quickly turn friendly.

The private equity boom years that ended in 2007 provide two striking examples of deal cross-fertilization. First, in Europe, companies were sold (particularly in heated auctions) with no representations and warranties from the selling shareholders regarding the business to be acquired. This practice became the exception rather than the rule in Europe, and it remained in place until the bottom fell out of the leveraged finance market. It began to creep into auctions in the U.S. as well, but the private equity market collapsed before it took hold to any significant degree. Now, based on recent experience in Europe, many deals have moved back to the U.S. standard, where the party selling a company stands behind representations and warranties about the target's business. Second, following the acquisition of SunGard Data Systems Inc. by a consortium of private equity investors, reverse break-up fees (which originated in real estate deals in the U.S.) quickly became the model in private equity deals in the U.S. and also became commonplace in Europe.

A final example of deal cross-fertilization is the rise of shareholder activism in Europe. Prior to the agreement by IMS Health Incorporated and VNU NV to merge in 2005,[11] activist shareholders of the type that had been operating for some time in the U.S. were virtually unheard of in Europe. In fact, institutional investors tended to go along passively with transactions that were recommended by the companies in which they invested, whether they were targets or acquirors in any given situation. In the IMS/VNU transaction, a shareholder with a holding of less than 5 percent of the outstanding shares of IMS was able to very publicly create a groundswell of opposition to the agreed deal. This opposition ultimately caused the deal to collapse. A similar dynamic was at play very recently when institutional shareholder opposition killed Prudential PLC's agreed deal to purchase American International Group Inc's main Asia unit, AIA.

Conclusion

We expect that rules and transactional features and structures will continue to converge across jurisdictions as regulators learn from the successes and failures of their colleagues in other nations, advisors continue to operate in multiple jurisdictions and corporate clients increasingly function across the globe, regardless of the country in which parties are organized or have their headquarters. This harmonization will go hand-in-hand with increased cross-border deal activity and will help provide a common framework to facilitate transaction execution.

Frank Aquila (aquilaf@sullcrom.com) is a partner in the Sullivan & Cromwell LLP Mergers & Acquisitions Group, resident in the firm's New York office. His practice focuses on mergers, acquisitions, strategic alliances and corporate governance matters for large multinational corporations. Mr. Aquila was an American Lawyer "Dealmaker of the Year" in 2009 and is the 2010 recipient of the Atlas Award as the "Global M&A Lawyer of the Year." Mr. Aquila is a featured columnist for BusinessWeek.com and has received Burton Awards for Legal Achievement in 2005 and 2010. He is also a member of the Council on Foreign Relations and the Leadership Council on Legal Diversity.

Brian Hamilton (hamiltonb@sullcrom.com) is a partner in the Sullivan & Cromwell LLP Mergers & Acquisitions and Private Equity Groups, resident in the firm's London office. Mr. Hamilton advises on public and private mergers and acquisitions and private equity transactions, both in and outside the United States and in a variety of industries. Most recently, he advised the Silver Lake Partners-led consortium in its $2.025 billion acquisition of a 65 percent interest in Skype Technologies S.A. from eBay Inc. and Barclays Bank plc in its $13.5 billion sale of Barclays Global Investors.

[1] *See* John Armour and David A. Skeel, Jr., *Who Writes the Rules for Hostile Takeovers, and Why?—The Peculiar Divergence of U.S. and U.K. Takeover Regulation*, 95 Geo. L.J. 1727 (2007).

[2] Of course, the specific rules governing tender offers vary widely from country to country, even if the underlying goal is the same (i.e. ensuring that shareholders are able to make an informed decision about whether to tender into an offer).

[3] *See Cross-Border Tender and Exchange Offers, Business Combinations and Rights Offerings*, SEC Release Nos. 33-7759 and 34-42054 (Oct. 22, 1999), 64 FR 61382 (Nov. 10, 1999); and *Commission Guidance and Revisions to the Cross-Border Tender Offer, Exchange Offer, Rights Offerings, and Business Combination Rules and Beneficial Ownership Reporting Rules for Certain Foreign Institutions*, SEC Release Nos. 33-8957 and 34-58597 (Sept. 19, 2008), 73 FR 60049 (Oct. 9, 2008).

[4] *See* Exchange Act Rule 14d-1(c) and Securities Act Rules 800 and 802.

[5] *See* Exchange Act Rule 14d-1(d).

[6] The Tier I exemptions apply if a target has 10 percent or less of its shareholders in the U.S. The Tier II exemptions apply if a target has 40 percent or less of its shareholders in the U.S.

[7] *See Acceptance from Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards Without Reconciliation to U.S. GAAP*, SEC Release Nos. 33-8879 and 34-57026 (Dec. 21, 2007), 73 FR 986 (Jan. 4, 2008); and *Concept Release on Allowing U.S. Issuers to Prepare Financial Statements in Accordance with International Financial Reporting Standards*, SEC Release Nos. 33-8831 and 34-56217 (Aug. 7, 2007, corrected Sept. 13, 2007), 72 FR 45600 (Aug. 14, 2007).

[8] *See* Companies Act 2006, Part 26 Section 899 and Part 28 Section 979.

[9] Sullivan & Cromwell LLP and Mr. Aquila represented Grand Met in connection with its combination with Guinness.

[10] Sullivan & Cromwell LLP and Mr. Aquila represented InBev in connection with its successful bid for Anheuser-Busch.

[11] Sullivan & Cromwell LLP represented IMS Health in connection with its agreed deal with VNU.