The New Draft Proposal for a Directive on Takeovers - the German Perspective

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I. General remarks

The previous proposal for a company law directive on takeovers in 1990[1] was rejected in Germany almost unanimously for several different reasons.[2] The new "slimmed down" draft proposal, in the light of the subsidiarity principle, takes the different approaches to investor-protection in the various member states better into account. Notably, the most controversial principle of the previous draft, viz. the mandatory bid rule as the only means of investor-protection in case of a change of control, has been given up. Therefore a much higher degree of acceptance seems likely. The Bundesrat[3] (upper house) and the industry associations[4] have already expressed their consent; the Bundestag (Federal Parliament) will deal with the proposal shortly. The technique of a "frame directive" leaves ample leeway for the member states. That will shift the discussion back to the national level and there will lead to the question as to how to make use of this leeway (cf. II, III, below) rather than to a debate about principles as in the past. It seems likely that criticism will confine itself to more technical questions (cf. IV, below).

II. Public takeover bids

The current draft deals - as did its antecedents - with two different issues which will be treated separately in the following: the regulation of public takeover bids and the protection of outside shareholders in case of a change of control over a company.

1. The current regulation

Public takeover bids do not currently play a practical rôle in Germany.[5] There is no explicit statutory regulation of public takeovers. The Ministry of Finance's Stock Exchange Experts Commission has however developed rules concerning public takeover bids. The previous

"Guiding Principles" of 1979 consisted of few non-binding recommendations. In July 1995 the Commission published a new, comparatively comprehensive takeover code.[6] It will be implemented through contractual recognition by potential offerers, target companies and companies engaged in share dealing. So far it has been recognized by 229 of the 674 listed companies (numbers as of end of April, 1996).

2. Adaptation or replacement of the current regulation?

The question is whether, and with what corrections this new voluntary takeover code could continue to exist, or whether it would have to be replaced completely should the EU proposal become binding. The following remarks will be confined to two main problems and not deal with every point where an adaptation or change of the current regulation seems necessary.

a) According to arts. 1, 11 of the EU proposal, the member states will not have to implement the rules of the directive by statute or administrative acts. Other regulations or prodecures of implementation will be admitted provided that these will ensure compliance with the rules of the directive (art. 11). The technique of voluntary contractual recognition adopted by the German Takeover Code does however, not meet this requirement.[7] Even if all domestic listed companies and financial advisors signed the Code, it would not encompass all potential bidders, and in particular not foreign bidders. There are no enforceable sanctions against those who have not signed the Code for not complying with it. Compliance with the Code could thus not be ensured.[8] That means that at least the current technique of implementation through contractual recognition would have to be replaced by normative (statutory) rules.

b) Similar considerations apply to the supervisory organ which has to be put in place according to art. 4 of the proposal. Art. 4 admits that associations or private institutions may serve as supervisory organs. The German Takeover Code provides that a "Takeover Commission" will ensure compliance with the Code. The powers of this commission rest however, on the contract signed by the parties thereto and are hence clearly limited. Powers in respect of third parties would require a statutory provision.[9]

Both points (a] and b] supra) make it likely that a statutory regulation would have to substitute the new Takeover Code.[10] The (opposition) Social Democrats have anticipated that and tabled a bill last year which contained, inter alia, a takeover regulation.[11]

III. Change of control and shareholder protection

The most controversial provision in the previous drafts was the mandatory bid rule as the only means of shareholder protection in case of a change of control. Due to the fierce resistance of some member states, namely Germany and The Netherlands, other equivalent measures may now be taken (art. 3).

1. Limited focus of art. 3

The current proposal still does not fit well, at least in respect of the German approach in cases of a change of control in a public limited company. A mandatory bid rule will protect the interests of the present shareholders only. It does not take care of the interests of the future shareholders of a dependent company, including those of the present shareholders who are not, for whatever reason, willing to accept the tender offer. Nor are the interests of the creditors and employees of the company addressed. Art. 3 picks out only one out of a whole raft of questions connected with changes of control and then requires an assessment of whether the existing national regulation is equivalent to a mandatory bid. The following remarks will hence, following this narrow focus of art. 3, be confined to the question of how the present shareholders are currently protected in case of a change of control.

2. The statutory regulation

The traditional approach of German statute law so far has been the ex-post protection of outside shareholders, in particular by specific provisions in the law on groups of companies (§§ 317 ff. Stock Corporation Act). German company law provides for an obligatory takeover of all outstanding shares only in case of specific inter-company agreements (§§ 305, 320 b Stock Corporation Act).

The question whether this statutory ex-post protection is at least equivalent to the ex-ante protection provided by a mandatory bid rule is not easy to answer. On the one hand, it is claimed that the ex-post protection provided for by §§ 311 ff. Stock Corporation Code is not a very effective one.[12] On the other hand, if the ex-ante protection afforded by a mandatory bid rule were not combined with ex-post shareholder protection rules, it is hard to assess what regime outside shareholders would prefer, given that art. 10 of the EU proposal will also allow partial mandatory bids. Outside shareholders would definitely most welcome a combination of both approaches. That is exactly what the new German Takeover Code tries to achieve (cf. 3, below), but it seems clear that art. 3 of the proposal does not require such a combination.

3. The new Takeover Code

The new Takeover Code[13] provides for a mandatory takeover bid (art. 16 of the Code). Although the details of the regulation of the Code in this respect are hardly convincing[14] one has always to keep in mind that the regulations of the Code supplement the statutory shareholder protection rules in cases of a change of control.[15] Together with these they certainly meet the standard of art. 3 of the EU proposal,[16] even though they might not be convincing in every detail. But an enactment in national law of an EU-takeover directive would give rise to further discussion and perhaps to an improvement of the provisions of the Takeover Code.[17]

IV. Amendments to the proposal

a) The German industry associations have proposed in their comment that the wording of art. 3 be more specific. A takeover directive should in their opinion make it clear that indirect holdings do not constitute "control" of a company. Further exemptions should be made for various cases in which continuous control is not intended. In my opinion such a specification does not seem necessary. It is perfectly sufficient that the proposal (art. 2 sec. 2) leaves it to the member states to define in which cases "control" will be found.

b) The rule in art. 3 sec. 2 should be reconsidered. According to German private international law, for instance, the consequences of a change of control for the outside shareholders

(mandatory bid? other remedies and protective rules?) depend to the law applicable to the target company itself.[18] According to art. 3 sec. 2 however, the question of whether "control" has been acquired would have to be judged separately, according to the law applicable where the supervisory organ is located.[19]

c) The wording of art. 8 a) seems too narrow. The shareholders' consent may be difficult to obtain because of the comparatively short offer period.[20] The directive should instead rely on the liability of directors, should they intentionally and without justification thwart the possibility of tendering the shares.

d) If in the case of a partial bid, more shares are offered than the bidder is asking for (cf. art. 10 sec. 2), the quota for the offering shareholders should be derived from the total of all offered shares rather than from the total of all shares in the company.[21]

[1] ABlEG Nr. C 240 (Sept. 26, 1990) at 7 ff.

[2] Cf. *Neye* ZIP - Zeitschrift für Wirtschaftsrecht 1995, 1564, 1466 footn. 14 ff.; *Baums*, in: Rengeling (ed.), Europäisierung des Rechts (1996); both with further references.

[3] BR-Drucksache (Bundesrat, printed matter) 162/96.

[4] Cf. *Neye* Der Betrieb 1996, 1121, 1123.

[5] For a detailed analysis see *Lutter/Lammers* in: Maeijer/Geens (eds.), Defensive Measures against Hostile Takeovers in the Common Market (1990), at 113 ff.; *Baums* in: Prentice/Holland (eds.), Contemporary Issues in Corporate Governance (1992), at 151, 154 f.; *Hopt* in: Hopt/Wymeersch (eds.), European Takeovers - Law and Practice (1992), at 167 ff.

[6] *Börsensachverständigenkommission* beim Bundesministerium der Finanzen, Übernahmekodex (Frankfurt, July 14, 1995); published, inter alia, in: Die Aktiengesellschaft 1995, 563 ff.; *Kallmeyer*, Die Aktiengesellschaft 1996, 169 ff.; *Thoma*, Der neue Übernahmekodex der Börsensachverständigenkommission. Working Paper (Universität Osnabrück) 9/1996.

[7] *Krause* Die Aktiengesellschaft 1996, 209; *Neye* (footn. 4, supra), 1124 f.

[8] *Thoma* (footn. 6, supra), at p. 12.

[9] *Neye* (footn. 4), 1125.

[10] See also *Neye*, op.cit., at p. 1124 f.

[11] Bundestag-Drucksache 13/367 (Jan. 30, 1995), at p. 8 ff.

[12] *Koppensteiner*, Kölner Kommentar zum Aktiengesetz, Vol. 6, 2nd. ed. (1987), Vorb. § 291 n. 57 ff. with further references.

[13] Cf. thereto II 1, supra.

[14] It provides, inter alia, a mandatory bid should an investor acquire more than 50% of all voting shares. This threshold disregards that a "controlling" or "dominating" (majority) position will - in publicly held companies with widely distributed shares - typically be given at much lower thresholds (cf. the statistical data in *Baums/Fraune* Die Aktiengesellschaft 1995, 97, 102). A further criticism refers to the price which the bidder has to offer (detailed criticism in *Thoma* [footn.6, supra], at 12 ff., 15 ff. with further references).

[15] Cf. 2, supra.

[16] Also see *Krause* (supra footn. 7), 212.

[17] Cf. also the proposal of the (opposition) Social Democrats in Bundestag-Drucksache 13/367 (Jan. 30, 1995), at pp. 8, 11 (§§ 32, 40): mandatory bid and decision of a shareholders' meeting if the threshold of 25% of shares is surmounted.

[18] *Assmann*, in: Aktiengesetz, Großkommentar. 4. ed. Vol. 1 (1992) Einleitung n. 713 with further references.

[19] Cf. also *Neye* (supra footn. 4), 1123.

[20] According to art. 6 nr. 3 the offer period may not last less than 4 weeks and not more than 10 weeks. The calling of a shareholders' meeting would take at least 4 weeks according to § 123 (1) Stock Corporation Code.

[21] Also see *Neye* (supra footn. 4), 1123.