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M&A transactions and framework

Alexander Vogel, Christoph Heiz and Andrea Sieber of meyerlustenberger analyse the recently amended M&A framework in Switzerland

Private M&A transactions are primarily governed by the Swiss Code of Obligations, and, to the extent acquisition structures include mergers, demergers, asset transfers or bulk sales transactions, by the Swiss Merger Act which provides detailed rules for each of these procedures. The acquisitions of interests in listed companies are further governed by the Swiss Act on Stock Exchanges and Securities Trading (Sesta), which contains the applicable rules for both friendly and hostile public offers.

In addition, the Swiss Antitrust Statute needs to be taken into consideration if the turnover of each of the parties involved in the transaction is significant (that is, if at least two of the involved parties achieved in the preceding business year a turnover on a standalone basis exceeding SFr100 million ($110 million) and a combined turnover in Switzerland exceeding SFr500 million (or on a worldwide basis exceeding SFr2 billion). The latter Act provides for a preventive merger control procedure led by the Swiss Merger Control Commission for transactions exceeding certain minimal thresholds.

To the extent an acquisition is financed by the issuance of securities or the transaction structure otherwise provides for additional securities to be issued, the relevant provisions of Swiss Code of Obligations have to be complied with. If the issuer is listed on a Swiss stock exchange, the listing rules of such stock exchange will also apply.

The first two quarters of 2010 showed a fragile stabilisation of the sharp decline in M&A transactions experienced in 2008 and mainly in 2009, with the number of transactions remaining flat as compared to 2009, but with deal volumes still considerably dropping. The third and fourth quarters brightened up the picture significantly showing clear signs of improvement of market confidence. This trend was underpinned by a relatively strong fourth quarter.

The reversal of the negative trend dominating the two previous years can be interpreted as a sign of a slow recovery of the markets and reflects on one side the increased confidence of industrial buyers in their own projections and those of their targets as well as in the stability of the economy as a whole, and on the other side the (perceived) improved availability of financing even for large acquisitions which also prompted financial buyers to play a more active role in the market place again.

With regard to cross-border transactions, the further strengthening of the Swiss Franc continues to make acquisitions by foreign acquirers in Switzerland expensive while Switzerland based companies that are heavily dependent on exports and thus more exposed to a strong Swiss Franc are increasingly looking to expand their sourcing and/or production base to countries in the Euro-zone or to US dollar-dominated areas in Asia. Even though the strong Swiss Franc is likely to take a toll on the export-oriented segments of the Swiss economy, the solid domestic demand is expected to mitigate such negative impact and thus sustain the positive trend for M&A activity within Switzerland (although the levels experienced before the crisis still seem to be far out of reach).

2010 saw several significant cross-border takeovers by Swiss companies, including the $3.7 billion acquisition of the North American pizza business of Kraft Foods by Néstle.

The few transactions relating to Swiss listed target companies included Swiss equipment supplier Meyer Burger's acquisition by way of merger of the smaller listed equipment manufacturer 3S Industries AG for approximately CHF 345 mio. which was implemented in the first quarter 2010, the public offers of Adobe Systems on Swiss listed company Day Software for USD 260 mio., of 3M (Schweiz) AG for Winterthur Technologie Ltd, a leading international provider of complex abrasive technology, and the public offer to the shareholders of Datacolor, the product of an earlier spin off of former brewery group Eichhof's colour management solutions activities, by its main shareholder who held before the offer already a stake of 33.25%, which were both announced in

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December 2010. Further European ICT distributor Actebis and Switzerland-based listed ICT distributor ALSO Holding agreed in August 2010 to combine their businesses by means of contribution of the Actebis business by way of an ordinary share capital increase of ALSO for the benefit of the former Actebis shareholders, while the subscription rights of the public shareholders and of Schindler Holding Ltd., the former majority shareholder of ALSO being excluded. Since the articles of incorporation of ALSO provide for an "opting-out"-clause, the fact that the former Actebis shareholders hold slightly more than 50% of the combined company after completion of the transaction did not trigger an obligation to submit a public offer to the existing shareholders of ALSO.

Public takeovers

Specific regulations

Public tender offers on issuers listed on an exchange in Switzerland are governed by Sesta. In certain instances, mainly in the case of a listed issuer spin-off of a non-listed company, an offer on the latter's shares is nevertheless subject to the provisions of Sesta (see, for example, the Hammer Retex transaction in 2009 or the earlier Eichhof or Mövenpick/Clair Finanz Holding transactions). Conversely, pure merger transactions are not subject to the provisions of Sesta, but to those of the Swiss Merger Act.

An exception applies if one of the merging companies acquires before the effective date of the merger a controlling stake of the other merging company, thereby triggering the obligation to submit a public offer according to Sesta.

> **"In case of a mandatory offer, the offeror is required to offer cash consideration as an alternative in addition to the shares offered"**

However, in that case the Takeover Board, while requesting compliance of the merger documentation and to the extent applicable, the terms of the merger, with the requirements provided for in Sesta and the ordinance on public takeovers, allows the acquirer to postpone the offer and instead complete the merger with the consequence that the obligation to submit a public offer lapses due to the absorption of (usually) the target company, provided however, that if the merger fails, the acquirer will be obliged by the Takeover Board to follow through with its public offer.

Sesta defines when a purchaser is required to make a mandatory offer for all outstanding equity securities of a target which is the case if an acquirer directly or indirectly controls more than 33.3% of the company's voting rights whether exercisable or not. Exceptions apply if the target had increased this threshold in its articles of incorporation to up to 49% (opting up) or if the latter contain an opting out-clause.

Furthermore, once a public offer has been pre-announced, the board of the target is no longer permitted to take any defensive measures that could have the effect of significantly altering the assets or liabilities of the target but has to submit such measures to the shareholders' meeting for approval.

Compliance with the rules provided for in Sesta is supervised by the Takeover Board which issues binding administrative orders in the form of binding decrees. Any decision of the Takeover Board can be brought to Finma

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for review. Against decisions of Finma any party can make an appeal to the Federal Administrative Court whose decisions are final.

Impact of recent legislative changes

The Swiss legislator enacted the Financial Market Supervision Act (Finmasa) providing for a new regulatory framework that entered into force as of January 1 2009. Such regulatory framework is supervised by Finma. Together with Finmasa, several changes to Sesta relating to public offers and the applicable procedural rules were enacted which also took effect as of January 1 2009.

In view of these changes in the legislation, Finma and the Takeover Board undertook a general overhaul of the stock exchange ordinance of Finma (Sesta-Finma) and the ordinance on public takeovers (TOO). The amendments to Sesta, Sesta-Finma and TOO introduced some important changes to the applicable rules for public takeovers and codified to a certain extent the Takeover Board's decision practice since the enactment of Sesta in 1997.

The rules provide for a stronger position of the Takeover Board. While in the past it could only issue recommendations which could be accepted or rejected by the parties involved, as of this year its decisions are handed down in the form of a decree. Further, the procedure in front of the Takeover Board is – with a few exceptions – governed by the applicable procedural rules for administrative procedures.

The exceptions take into account that a takeover procedure needs to be speedy. Today, shareholders holding 2% or more of the voting rights of the target company, have the possibility, whether exercisable or not, to request the status of a party in the proceedings before the Takeover Board. This innovation changes the practical steps, particularly also in a friendly transaction, considerably.

In the past, the offeror and the target company could agree on the terms and conditions of a public offer and have those terms as well as all relevant documents relating to the offer approved by the Takeover Board before the publication of the pre-announcement of the offer or the offer itself. The Takeover Board then issued simultaneously with the publication its recommendation which could not be appealed by the shareholders. Here, the only potential threat to the success of a friendly offer was a competing offer by a third party offeror. In such a case, the original offeror had the option either to fight and increase its original offer or to withdraw its offer and leave the scene.

Under the revised rules, certain shareholders can request to participate in the proceedings before the Takeover Board and submit objections or requests to the latter and/or appeal against a decree issued by the Takeover Board. In view of these rights granted to qualified shareholders, the offeror has to comply with a mandatory cooling-off period of usually 10 stock exchange days. Further, due to the possibility of an appeal, the terms of the offer and the offer documents will be – even though reviewed by the Takeover Board – published with only a preliminary approval of the Takeover Board.

By making use of their procedural rights, qualifying shareholders have the possibility to considerably delay a friendly takeover. Such delays may considerably increase the transaction risks of both the offeror and the target company. The threat of extended litigation with a minority shareholder may thus well force the offeror to the negotiation table, trading better offer terms in exchange for withdrawing the legal challenges.

On the other hand, such delays may have considerable disadvantages for the target company, since itself, its management and workforce, customers and suppliers do not know for an extended period whether the intended transaction will be completed as planned or if an uninvited third party will enter the scene and launch a competing (hostile) offer, trying to profit from the fact that the target has put itself in play.

Put up or shut up rule

In order to prevent thepotential offeror publicly communicating that they are considering launching a public offer on a specific target company without publishing a pre-announcement in compliance with the Sesta rules, the Takeover Board can now force such potential offeror(s) to either submit a public offer within a certain deadline or publicly declare that it will not launch any offer in the following six months, provided, however, that in case of a third-party offer such temporary ban can be lifted by the Takeover Board.

Competing offers

A competing bid can be launched until the last day of the preceding (initial) offer by publishing an offer prospectus or at least a pre-announcement. In the latter case, the offer prospectus must be published within five exchange business days. In addition, due to the now mandatory cooling-off period, a potential competing offeror will in most cases have at least 10 more exchange business days available to prepare a competing offer.

A competing offer also affects the offer period of the previously published (initial) offer: the offer period of the initial offer is extended so that its offer period expires at the same date as the competing offer. Further, contrary to the former rules, the offeror of the initial offer is not able to withdraw its offer in case a competing offer is launched. The initial offeror can, however, amend its offer up to the fifth exchange business day before the expiration of the adjusted offer period.

Changes relating to defensive measures

As indicated above, once a public offer has been pre-announced (or announced), the board of the target company may no longer take defensive measures which have a significant impact on the target company, provided however, that it can submit such measures to the shareholders for approval.

TOO provides for a detailed blacklist containing such disallowed defensive measures. TOO provides, among other things, that assets generating more than 10% of the target company's consolidated earning power may not be sold or acquired and that the target company cannot purchase or sell its own shares, shares offered in exchange or related financial instruments, or write or grant any rights to acquire its equity securities, in particular conversion or option rights.

Rules relating to the offered consideration

Pursuant to the rules of Sesta-Finma regarding the consideration offered, the offer price may be paid in the form of a cash consideration or by offering securities in exchange. However, according to the applicable rules of Sesta-Finma, in case of a manda-

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tory offer, the offeror is required to offer cash consideration as an alternative in addition to the shares offered in exchange to the remaining shareholders of the target.

Until the Takeover Board published its Communication 4 in 2009, the consequences of this article were unclear and heavily criticised. The criticism focused on the fact that the obligation to offer a cash consideration as a mandatory alternative – if necessary at all – was not limited to an offer of illiquid equity securities (to securities that have not been traded on at least 30 of a period of 60 exchange business days before publication of the offer or pre-announcement).

If the offered equity securities are illiquid, the cash alternative to be provided enables the remaining shareholders of a target effectively to exit the target at a fair price. On the other hand, a mere offer of equity securities that are illiquid would leave the shareholders with the option either to: (i) remain a shareholder of the target with a minority stake and therefore enjoy limited shareholders' rights; or (ii) become the owner of equity securities that are not liquid and therefore not easily marketable.

However, from a potential offeror's perspective, this rule has a significant financial impact. The offeror is obliged to provide evidence of its ability to finance the public tender offer. In the past, in case of an exchange offer, the offeror had to prove the availability of the securities to be exchanged at the time the offer was scheduled to settle. As a consequence of the revised rule, the potential offeror now must not only prove the latter, but also make arrangements for the cash consideration to be offered alternatively to the remaining shareholders. The offeror must also prove the availability of such funds.

In its Communication 4, the Takeover Board stated that the obligation to offer a cash consideration as a mandatory alternative to an exchange offer does not apply to voluntary tender offers, even though as a general rule the minimum price rules for mandatory offers are also applicable for voluntary offers aiming more than 33.3% (or such applicable higher threshold in case of an opting-up) of the shares of a target. However, according to the amended language of Sesto-Finma, the rule in any case applies to mandatory offers, regardless of whether the offered equity securities are liquid or not.

In other words, the offeror whose holding in the target exceeds the relevant threshold of voting rights and thus triggers the duty to submit a mandatory offer will not have a choice as to how to fulfil such obligation and is not only bound by the minimum price rule and best price rule. To the contrary, even if the offeror wishes to offer securities that are liquid – and therefore can easily be sold by the offeree – it will be obliged to offer a cash consideration as an alternative and must prove the availability of such (additional) financing.

The Takeover Board stated in its Communication 4, however, that the value of the offered securities and the value of the cash consideration need not be equal. Therefore, the offeror may offer a premium on the offered security consideration compared to the cash consideration and, therefore, the offeror is allowed to provide an incentive to accept the exchange offer. However, both the value of the offered securities and the cash consideration must fulfil and comply with the minimum price rule.

"In the case of a voluntary tender offer, the offeror is free to offer equity securities for which no liquid market exists or which are not listed"

The last revision of Sesta has not changed the possibility to pay a so-called control premium in the case of a public offer: the price offered to the minority shareholders may be lower than the share price agreed before the offer with the principal shareholders. However, the Swiss Takeover Board recently proposed to abolish such possibility in the course of the next revision of Sesta now under way, as it is contrary to the principle of equal treatment of shareholders and is unusual in the European context.

Voluntary offers

As mentioned above, in its Communication 4 the Takeover Board further confirmed its interpretation that the obligation to offer a cash consideration as a mandatory alternative to an exchange offer does not apply to voluntary tender offers. This applies particularly to voluntary tender offers made for a number of equity securities the acquisition of which would reach the applicable threshold triggering a mandatory offer. Furthermore, the Takeover Board confirmed that a successful offeror (where the offeror holds a majority stake in the target exceeding the triggering threshold after the public tender offer is completed) has no obligation to submit an additional public tender offer (against cash consideration) to the remaining shareholders.

Nevertheless, the exemption for voluntary offers does not apply if the offeror acquires equity securities of the target against a cash consideration after the exchange offer is launched. Under such circumstances, the Takeover Board requires that the terms and conditions of the exchange offer be modified to ensure equal treatment of all shareholders of the target.

In particular, the recipients of the offer must have the choice whether to accept the initially offered securities or a cash consideration – as paid after the exchange offer was launched. Furthermore, shareholders that have already tendered their shares can change their election and request to receive the cash consideration rather than the previously accepted securities. However, a shareholder is not entitled to withdraw its tender (in other words decide to accept neither the offered securities nor the cash consideration) if it has already accepted the (initial) exchange offer.

On the other hand, the duty of equal treatment does not prevent the offeror from acquiring securities of the target against cash consideration, where the purchase has been effected before the pre-announcement or publication of the offer. However, such consideration needs to be taken into account when determining the minimum price of the offer.

Furthermore, in the case of a voluntary tender offer, the offeror is free to offer equity securities for which no liquid market exists or which are not listed. In such case the offeror will be required to provide a valuation by an accredited audit firm or investment bank.

The Takeover Board argued that in such case the shareholders of the target may, simply by refusing the tender offer, avoid the negative consequences of having to choose between becoming a minority stakeholder (thus limiting the shareholder's rights), and becoming the owner of equity securities that are not liquid and consequently not easily marketable. This is because, unlike in the case of a mandatory offer, the recipients receiving a voluntary offer have the option to reject the offer and thus prevent the offeror from acquiring a controlling stake.