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 CLIENT

INFORMATION

New German disclosure requirements for significant shareholdings apply as of 1 February 2012

On 1 February 2012, new regulatory disclosure requirements for shareholdings in German¹ listed companies will enter into force. The new disclosure requirements form part of the Bill on the Strengthening of Investor Protection and the Improvement of Financial Markets (*Gesetz zur Stärkung des Anlegerschutzes und zur Verbesserung der Funktionsfähigkeit des Kapitalmarkts – “AnSFuG”*) which was adopted by the German parliament in early 2011. The main objective of the new legislation is to capture arrangements which so far escaped the existing disclosure requirements even though they may be (and in fact have been) used to build up positions in a German listed company. Regulatory guidance on selected aspects of the new law has recently been published by the German Federal Financial Services Supervisory Authority (“BaFin”) in the form of a FAQ list. The FAQ list is available under the following link (as of the date thereof only in German):

http://www.bafin.de/eln_228/nn_724100/SharedDocs/FAQ/DE/Unternehmen/BoersennotierteUnternehmen/meldepflichten__25__wphg/faq__25awphg__00.html

Please note that the new disclosure requirements will also be relevant for holdings acquired before and still held when the new law enters into force. A party holding instruments making it possible to acquire five percent or more (taking into account the aggregation rules) of the voting shares of a German listed company on 1 February 2012 must disclose such holding without undue delay but at the latest within 30 trading days in Germany, i.e. by (and including) 13 March 2012. Existing structures should therefore be carefully reviewed.

¹ Under particular circumstances, the German disclosure requirements may also apply to non-German company whose shares are listed on a German stock exchange. The term “German listed company” is used in this memorandum to describe all companies whose shares are subject to the German disclosure rules for significant shareholdings.

I. Existing German Notification Requirements

The German provisions on the disclosure of significant shareholdings conferring voting rights are set forth in the German Securities Trading Act (*Wertpapierhandelsgesetz – “WpHG”*). Based on the European Transparency Directive (Directive 2004/109/EG), the WpHG requires owners of shares in German listed companies to disclose their voting rights by notification to the issuer and BaFin if certain thresholds (3%, 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75%) are reached or crossed. The disclosure requirements applicable to owners of shares are complemented by provisions on the attribution of voting shares owned by certain other shareholders (e.g. shares owned by subsidiaries, shares held by a third party for the account of the notifying party, acting-in-concert).

In 2007, the German disclosure requirements were extended to include financial instruments (as defined in the WpHG) which entitle the holder to acquire voting shares, such as call options. Following a further amendment, effective as from 1 March 2009, voting shares which can be acquired under such financial instruments must be aggregated with direct or attributed voting share ownership. These disclosure requirements, however, do not capture arrangements (such as certain securities lending transactions and repos) which do not fall within the ambit of the “financial instruments” definition. Furthermore, pursuant to the prevailing opinion shared by BaFin, these provisions only relate to instruments giving their holder a right to acquire already issued voting shares. Cash settled instruments are not captured, regardless of how likely it is that the holder will factually be in a position to take voting shares in lieu of cash.

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II. Overview of main Amendments by the AnsFuG

The following key changes to the German disclosure rules for significant shareholdings will be introduced:

1. The existing disclosure requirements for "financial instruments" are extended to include "other instruments" (which do not qualify as financial instruments) granting the right to acquire voting shares.
2. New disclosure requirements are introduced for instruments which do not grant an enforceable right to acquire voting shares but still make such acquisition (at least economically) possible.

There will, consequently, in future be three disclosure regimes, *i.e.* (i) for voting shares, (ii) instruments granting the holder an enforceable right to acquire voting shares, and (iii) instruments which do not grant an enforceable right to acquire voting shares but make such acquisition possible. These disclosure regimes are distinct, but interlinked by provisions on the aggregation of positions held in each of the different categories.

1. Other Instruments Granting a Right to Acquire Voting Shares (§ 25 WpHG)

The disclosure requirements for financial instruments are amended to include "other instruments" granting their holder the right to acquire voting shares.

As a consequence, the following instruments may, for example, be relevant for purposes of this disclosure requirement:

- **Rights for the delivery of voting shares under a share purchase agreement** (or other agreement such as a shareholders agreement) with deferred delivery or subject to conditions precedent under the exclusive control of the purchaser (*e.g.*, approval of corporate bodies of purchaser)
- **Rights for the redelivery of voting shares under a securities lending agreement or repurchase agreement**

2. Instruments making it possible to acquire voting shares (§ 25a WpHG)

New disclosure requirements are introduced for instruments which "make it possible" to acquire voting shares. In contrast to the already existing disclosure requirements applicable to instruments granting a right to acquire voting shares, the instruments captured by the new provision do not grant a legally enforceable right to acquire shares. However, due to their particular economic features or their underlying business logic, they may bring about the opportunity for the holder to acquire voting shares. Furthermore, it will be sufficient if a third party rather than the holder of the instrument is entitled to acquire voting shares (*e.g.* by way of a contractual agreement for the benefit of third parties / *Vertrag zugunsten Dritter*).

This broad and somewhat imprecise new rule is complemented by two statutory provisions exemplifying circumstances under which arrangements are deemed to make the acquisition of voting shares possible:

- The counterparty could hedge its risks arising under the instrument in whole or in part by holding voting shares; for the disclosure requirements in a given case it is, however, irrelevant whether such hedging actually takes place.
- The instrument provides for the right or the obligation to acquire voting shares.

a) Possibility of hedging through the holding of voting shares

The requirements of lit. a (possibility of hedging through the holding of voting shares) will, for example, be met in a cash settled transaction which confers the economic benefit and burden arising out of voting shares upon the holder of the instrument. Thus, for the new disclosure requirements it is not decisive whether an instrument provides for a cash settlement or the physical delivery of the underlying shares.

As a consequence, the following cash-settled instruments may, *inter alia*, be relevant for purposes lit. a:

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- **total return equity swaps** (from the perspective of the counterparty exposed to the economic risks and benefits of the underlying shares)
- **cash-settled call options** (from the perspective of the option holder)

b) Right or obligation to acquire voting shares

As far as lit. b (right or obligation to acquire voting shares) is concerned, an instrument may be regarded as making the acquisition of voting shares possible within the meaning of the new law even if the initiative for the acquisition of the shares must come from the other party to the transaction. Further, the new provision also captures instruments granting the right to acquire voting shares only subject to conditions whose fulfillment is not under the exclusive control of its holder. Currently, instruments (even in the form of financial instruments) are generally not captured by the existing disclosure requirements if such conditions are agreed.

Contrary to requests raised during an expert hearing on the new law and in the legal literature, neither the new law nor the legislative materials thereto contain any specific exemption for agreements under corporate law (share purchase agreements, shareholders' agreements, articles of association), which make it possible to acquire voting shares. While some voices in the legal literature argue against application of the new disclosure requirements to such agreements, the recently published BaFin FAQ list makes it clear that in the opinion of the regulator any type of (conditional) rights to acquire shares in such instruments falls within the ambit of the new disclosure rules, except for purchase agreements with immediate settlement (t+2).

As a consequence, the following instruments may, *inter alia*, be relevant for purposes lit. b:

- **Rights for the delivery of voting shares under a share purchase agreement** (or other agreement) which are subject to conditions precedent not under the exclusive control of the purchaser (*e.g.*, merger control clearance, approval of corporate bodies of seller)
- **Put options on voting shares with physical delivery** (from the perspective of the option writer) unless the bond

may exclusively be covered by newly issued shares; this may, *inter alia*, include the put right of the issuer under a mandatory convertible bond (*Pflichtwandelanleihe*)

- **Rights for the delivery of voting shares under a stock option plan** subject to certain vesting conditions

3. Instruments referring to Baskets or Indices

A disclosure requirement only arises if an instrument relates to voting shares in German listed companies. There is no requirement, however, for the instrument to relate exclusively to such shares. The new disclosure requirements also cover financial instruments referring to baskets or indices. The new law does not require any minimum weight of a particular share within a basket or index in order for the underlying instrument to be relevant for disclosure purposes. It is expected that the German Ministry of Finance will exempt diversified instruments from the new disclosure requirements by executive ordinance if voting shares of a relevant issuer account for not more than 20% of the basket or index but so far the executive ordinance has not been promulgated.

4. Disclosure Requirement, Relevant Thresholds and Aggregation Rules

Notifications of significant holdings in relevant instruments are subject to the same publication requirements as notifications of significant shareholdings. This means, in particular, that the relevant issuer must publish information on such holdings received from an instrument holder without undue delay but at the latest within three business days after receipt of the notification.

Whereas the lowest threshold for the disclosure of voting shares held or attributed to the notifying party is 3 percent under German law, financial and other instruments relating to voting shares must only be disclosed if they relate to 5 percent or more of the voting shares of the listed company. The new law does not provide for a netting of long and short positions for purposes of the disclosure requirements applicable to significant shareholdings.

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In order to determine whether a threshold for the disclosure requirements applicable to financial and other instruments making it possible to acquire voting shares has been reached or crossed, own or attributed shares, instruments granting a right to acquire voting shares and instruments making it possible to acquire voting shares must be aggregated. Besides specifying the aggregate number of voting shares, the relevant notification must, however, differentiate between own and attributed voting shares, instruments granting a right to acquire voting shares and instruments making it possible to acquire voting shares.

The number of voting rights to be disclosed in relation to financial and other instruments is generally determined by the number of shares which can be acquired under the instrument. If the instrument does not relate to a specific number of shares, the number of voting rights must be determined by the amount of shares which the other party would require for a full hedge of its position under the instrument. In respect of instruments referencing a basket or index the pro rata amount of the underlying share in the basket or index must be considered.

5. Sanctions

Non-compliance with the disclosure requirements for voting shares may lead to the loss of rights arising under such shares, including dividend rights and voting rights. The same may apply to attributed voting shares depending on which attribution rule has been violated. Furthermore, such non-compliance may be fined by BaFin.

Non-compliance with the disclosure requirements applicable to financial and other instruments generally does not lead to a loss of rights under the underlying shares even after they have actually been acquired. BaFin may, however, fine such non-compliance. The maximum fine will be increased to EUR 1,000,000 per violation by the AnsFuG.

This memorandum constitutes a summary of selected aspects and is not, and does not purport to be, a comprehensive analysis of the subject matter. Please note that so far neither case law nor regulatory guidance exists with regard to the new disclosure rules. Competent courts and BaFin may come to conclusions differing from those presented in this memorandum. This memorandum does not constitute legal advice on which any party may rely with respect to, or in connection with, any specific transaction. Additional implications may need to be examined and analyzed more closely, and preliminary conclusions arrived at herein may have to be re-examined depending upon the circumstances of each individual case.

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