# European Takeovers

## The Art of Acquisition

Euromoney Books

Author and Editor: Jeremy Grant

# Contents

Chapter 24

# Spain

Alejandro Fernández de Araoz
*Araoz & Rueda, Madrid*

Spanish takeover rules are embodied in mandatory statutory instruments. Unlike in the United Kingdom, there are no self-regulatory bodies or voluntary codes adopted by market participants. The mandatory rules are interpreted and applied by the Spanish National Securities Market Commission (CNMV), which has broad supervisory and enforcement powers, including the ability to impose substantial fines in the event the rules are breached.

The key statutory instrument in Spain's takeover regime is Royal Decree 432/2003 (RD 432/2003), which became effective on 12 April 2003. It modified Royal Decree 1197/1991 (RD 1197/1991), which contained Spain's existing takeover regulation for public companies. The new legislation has the objectives of protecting the interests of minority shareholders in the event of a change of control, and of improving market efficiency and transparency. The new rules were also intended to tackle the issues raised by a number of controversial takeovers that took place in 2002. They involved acquisitions of equity stakes below 25 per cent (the Spanish mandatory bid threshold) and were structured precisely to avoid having to launch a mandatory bid. Although it was widely perceived that control had changed hands in these cases, minority shareholders were nevertheless denied the benefit of a control premium, which was received only by the controlling shareholders who had sold their stakes to the acquirers. These transactions generated sufficient investor concern to instigate legislative reform.

RD 432/2003 modifies the existing Spanish takeover regime in four fundamental ways: by introducing additional situations requiring mandatory offers, modifying the exceptions to the requirement to make an offer, allowing new types of conditional offers, and modifying the regime applicable to competing bids.

## The mandatory bid rule

The Spanish takeover regime, contained in RD 1197/1991 as amended by RD 423/2003, is based on three fundamental principles:

- a 'mandatory bid rule' (MBR) requires that anyone seeking to acquire, in a single transaction or a series of successive transactions, a 'significant participation' *(participación significativa)* in a listed company must do so by means of a public takeover bid *(oferta pública de adquisición* or *OPA*). The key test therefore lies in the concept of a significant participation or stake in the target company. However, an acquirer may be legally obliged

to launch a takeover bid, even if it does not reach the statutory thresholds, when such a stake gives it the ability to appoint a number of directors to the target company's board;
- Spain's MBR is gradual in its effect to the extent that, depending on the percentage of shares the bidder wishes to acquire in the target company, the obligation to extend the bid to a certain percentage of shareholders varies;
- the MBR is applied on an *ex ante* basis: the takeover has to be launched as a prior condition to acquiring shares in the target company, not as a result of such an acquisition.

The Spanish MBR system establishes the basic criteria that trigger the legal obligation to launch a bid. One of these criteria is the acquisition of a certain shareholding percentage in the target company that reaches or crosses the mandatory bid rule threshold. The three different scenarios covered by the concept of a 'significant participation' are as follows:

- the acquisition of 25 per cent or more of the share capital of a company requires an offer for at least 10 per cent of the share capital of the company;
- an acquirer holding between 25 per cent and 50 per cent of the share capital of a company, and intending to acquire 6 per cent or more of the share capital of the company within a 12-month period, is required to make an offer for at least 10 per cent of the share capital of the company. This means that one can acquire up to 5.9 per cent within a year and repeat such a process every subsequent year up to 49.9 per cent; and
- the acquisition of 50 per cent or more of the share capital of a company requires making an offer for 100 per cent of the share capital of the company.

RD 432/2003 has introduced two additional scenarios requiring mandatory offers that are triggered, not solely by the acquisition of a predetermined percentage of a company's shares, but rather by the bidder's ability to appoint a certain number of the target company's board of directors. The new situations requiring mandatory offers are the following:

- the acquisition of more than 5 per cent, but less than 25 per cent, of the share capital of a company, with the power to appoint more than a third of the directors, or, if less than 5 per cent, giving it the right to appoint such a number of directors jointly with those already appointed by the bidder, now requires a mandatory offer for at least 10 per cent of the share capital of the company; and
- the acquisition of more than 5 per cent, but less than 50 per cent, of the share capital of the company, with the power to appoint more than half of the directors, or, if less than 5 per cent, giving it the right to appoint such a number of directors jointly with those already appointed by the bidder, now requires an offer for 100 per cent of the share capital of the company.

In order to determine the percentage of directors representing the interests of the bidder, the rules contain a rebuttable presumption that the following relationships establish a director's appointment by the bidder:

- nomination by the bidder or a related company;
- service as an officer, employee, director or consultant to the bidder or a related company;
- service by the bidder or a related party as a director of the target company;

- nomination with favourable votes from the bidder or a related company; or
- formal recognition in corporate or public documents that the director has been designated by the bidder.

In addition, a public bid must be launched if any of the following events occur:

- a single person becomes the owner of a significant stake as a result of converting convertible bonds, warrants or other securities that entitle their owners to acquire shares, and after all the shareholders have exercised their rights to acquire shares;
- an underwriting agreement is entered into between a public company and a financial institution in the context of a securities offering, as a result of which a significant stake is acquired by a financial entity;
- a public company's by-laws are significantly modified, where the modification is proposed by a shareholder holding more than 50 per cent of the share capital for the first time since it acquired such a stake in the company.

Beyond these criteria, Spanish takeover regulations also cover traditional concepts such as 'acting in concert' and 'group purchases', in which different purchasers are 'consolidated' for purposes of application of the MBR.

It is submitted that linking the MBR to objective thresholds and criteria, instead of to a more elusive and vague concept of 'control', provides a greater degree of legal certainty and predictability to private parties.

## Procedural aspects and timetable

### Preliminary steps

Provided that a potential bidder keeps its intentions confidential, no official announcements are required until the bidder formally notifies the bid to the CNMV. All bids must be notified to the CNMV for formal clearance. A prospectus explaining the offer and any other relevant documentation should be attached to the formal takeover filing. If the bid is hostile, pre-bid discussions may not have taken place between the bidder and the target, and the target will not be informed of the bid until the CNMV is notified. The target shareholders will first learn about the bid through the press announcement, unless they have been approached before the bid by the bidder to negotiate their support for the bid and to eventually grant irrevocable selling commitments.

Once the bid has been formally notified to the CNMV, the regulator orders a trading suspension of the target's shares until the information has been publicly disclosed and the market has knowledge of it. From this time onwards, the target's directors are obliged to manage the target in the ordinary course of business.

Next, the CNMV issues a resolution clearing or prohibiting the offer, and notifies the bidder and the target of its decision. The bidder must then publish a press announcement in the following publications:

- the *Official Gazette* of the Mercantile Registry;
- the *Stock Exchange Listing Bulletin*; and
- at least two newspapers, including one national newspaper and one widely distributed in the region where the target company has its registered offices.

The press announcement must contain the essential terms and conditions of the offer as stated in the prospectus, as well as the address of the place at which the prospectus and other ancillary documentation are available for inspection.

## Mandatory documentation

Once a bid has been authorised by the CNMV, the bidder must announce the offer and immediately afterwards make available to the target's shareholders both the prospectus and certain ancillary documentation.

The prospectus should include, among other things, the following information:

- the bidder's identity and details;
- details of the bidder's group structure (the entities which are part of the same group of companies);
- a list of the target company's shares that are already directly or indirectly held by the bidder, by the bidder's group of companies, or by other persons acting on the bidder's behalf or instruction;
- information on the bidder's activities and financial situation;
- the specific number and class of shares at which the bid is aimed;
- guarantees given by the bidder that it will pay the agreed price to the shareholders who accept the bid;
- the terms for acceptance of the offer; and
- the aim of the bid, expressly stating the intentions of the bidder in relation to the future activities of the target.

The ancillary documentation should include the following information:

- a mandatory bank guarantee, which means that the bid has to be funded ('money good') from the outset;
- any relevant administrative authorisations (clearance from any relevant regulatory or competition authorities as required);
- a draft of the advertisement that announced the offer in the *Official Gazette* and the press; and
- the relevant corporate documentation of the bidder, including the resolution approving the bid, certificates of good standing and audited accounts.

## Timetable

The following timetable typically applies:

- the bidder notifies the bid to the CNMV for clearance;
- the CNMV has 15 working days from notification to issue a resolution clearing or prohibiting the bid, although this can be extended if the CNMV requires additional information. In practice, this process will take between four and eight weeks;
- the CNMV orders the suspension of trading in the target's stock immediately after receiving notification from the bidder;

- the bidder has a maximum of five working days after clearance to announce the bid in the *Official Gazette*, the *Stock Exchange Listing Bulletin* and at least two newspapers;
- the bidder needs to make certain information available to the target's shareholders when it makes its offer;
- on notification of CNMV clearance, the target's directors must issue a report on the bid within 10 calendar days;
- the bidder must establish an acceptance period ranging from one to two months from the publication date of the first announcement of the bid;
- if the bid is conditional, the CNMV can extend the above deadlines to allow the target time to hold a general shareholders' meeting. Here, the board can inform the shareholders about the relevant conditions of the bid and any resolutions they need to pass;
- the terms and conditions of the offer can be altered within seven business days before the offer expires. If the terms are altered, the initial time frame is extended by a further seven calendar days; and
- when the period allotted for acceptance has expired, the CNMV must be notified of the result within five calendar days. If the minimum amount of shares stated in the offer has been reached, this is communicated by the CNMV within the following three calendar days from when the CNMV is notified and published in the *Stock Exchange Listing Bulletin* (see Exhibits 24.1 and 24.2).

Finally, it should be mentioned that if the takeover bid fails because the bidder does not achieve the minimum take-up percentage upon which it based the effectiveness of its bid, the bidder is barred from acquiring any additional target shares within six months of the date on which the result of the bid is published, unless through a new public offer.

## Exemptions

Mandatory offers are not required in the following four cases:

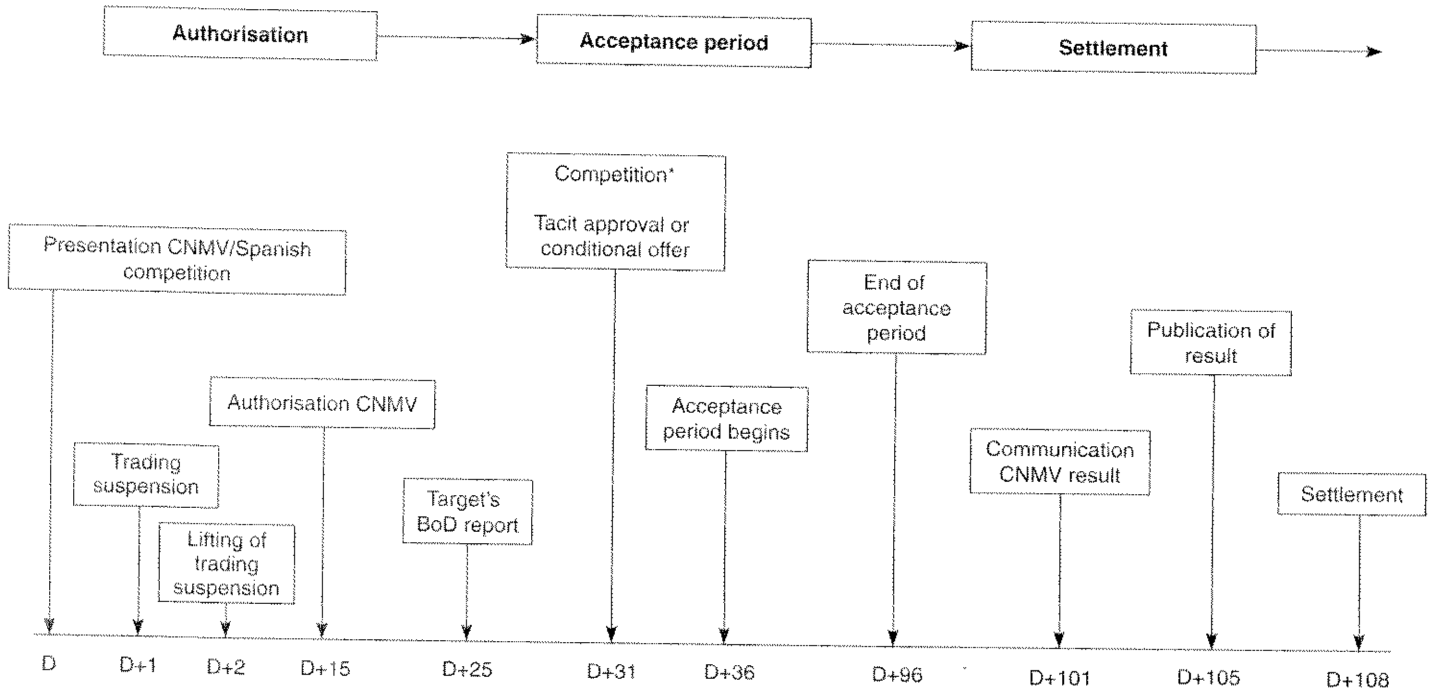
- purchases of shares by public/governmental institutions in the context of the salvage of a credit institution or insurance company in relation to an insolvency crisis;
- the exercise by governmental authorities of exceptional powers to expropriate pursuant to administrative law;
- significant participations acquired in connection with debt/equity exchanges or capitalisation of credits in the context of an agreement of the company's creditors within insolvency proceedings; and
- unanimous consent by the company's shareholders to sell or renounce the sale of their shares in a public takeover offer.

Nor is a mandatory offer required in cases that are deemed by the Spanish Competition Authority (Servicio de Defensa de la Competencia) to constitute joint control and that meet the following conditions:

- prior to the acquisition, the shareholders exercising joint control owned more than 50 per cent of the shares and appointed more than half of the board;
- the increase in the bidder's shareholding does not exceed 6 per cent in a 12-month period and in any event does not reach or exceed 50 per cent; and

Exhibit 24.1

**OPA calendar with no competing bid (with Spanish competition notification)**



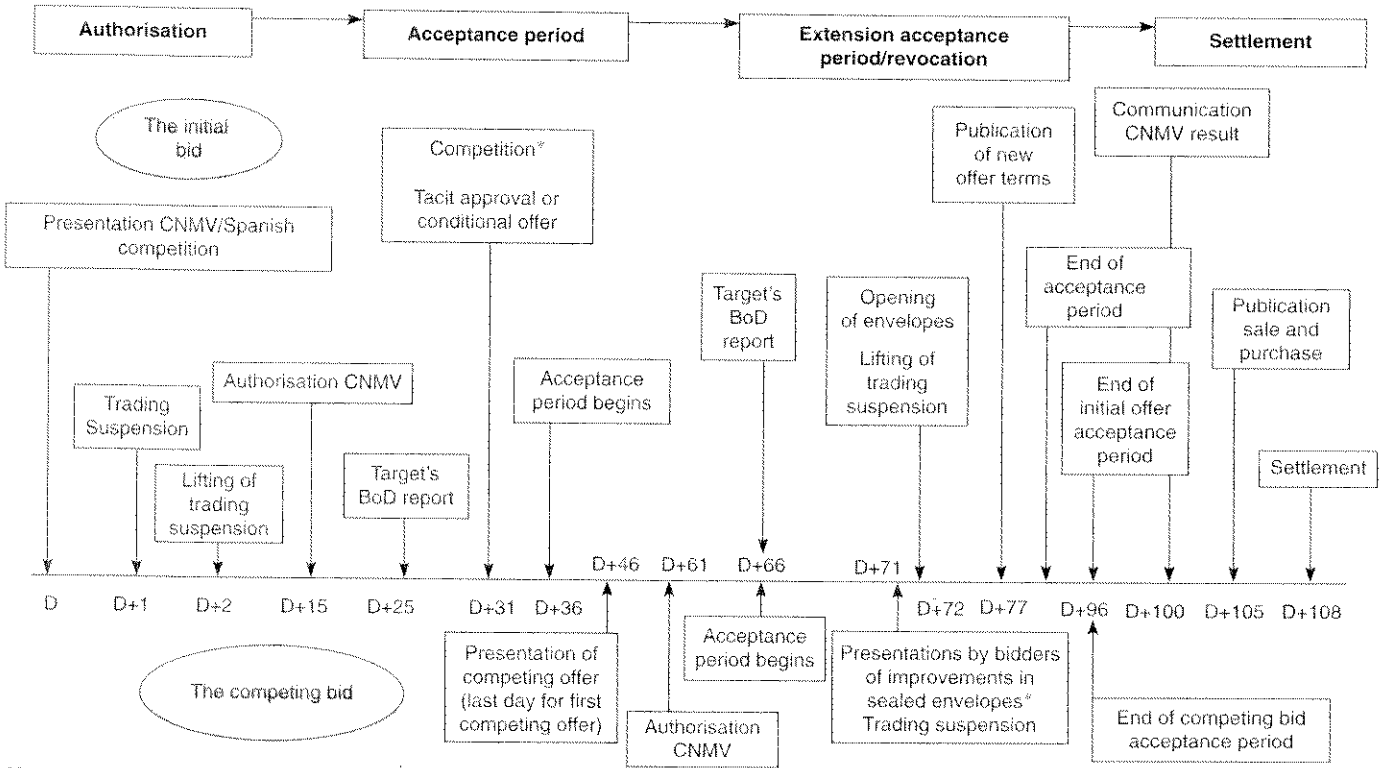

* If second phase is commenced, 90 days should be added to calendar.

*Note:* This timetable is merely tentative and may be subject to changes depending on specific circumstances

*Source:* LINKLATERS, *Tender offers in Spain*, April 2004.

Exhibit 24.2

**OPA calendar with one competing bid (with Spanish competition notification)**




* If second phase is commenced, 90 days should be added to calendar.

*Note:* This timetable is merely tentative and may be subject to changes depending on specific circumstances

*Source:* LINKLATERS, *Tender offers in Spain*, April 2004.

- the number of directors appointed by the bidder does not increase as a result of the acquisition.

Despite these new exemptions, certain exemptions present in other takeover regimes are missing from the Spanish regime. These include an exemption for the acquisition of a significant stake as a result of exercising pre-emptive rights when other shareholders do not exercise theirs, and an exemption for contributions in kind that are in the interests of the company.

## Defensive tactics and the role of the target company's board

In a pre-bid context, a public company can use classical defensive tactics by including in its by-laws super-majority provisions to approve certain resolutions, staggering its board and/or imposing voting ceilings on individual shareholders. The use of other defensive devices common elsewhere in Europe, such as multiple share classes, is rare in Spain.

However, key shareholders can enter into shareholders' agreements containing voting trust or pooling arrangements, which make contestability of control in the target company much more difficult. Whether Spain opts into or out of Article 11 of the Takeover Directive will be a key consideration, although a grandfathering provision applies to shareholder agreements entered into before the adoption of the Directive.

Once the bid has been formally launched, the target company's board can only take decisions in the ordinary course of business and is barred from taking action that could directly or indirectly frustrate the bid.

Finally, it should be mentioned that the target company's board has to issue a report to the shareholders with its comments and recommendations on the bid. It is increasingly common for a target's board to retain investment banks or financial advisers to produce appraisals or opinions of its recommendation on the 'fairness' of the consideration offered in the bid.

## Analysis of the competing bid system

Until the reform of 2003, the Spanish takeover regime included a highly controversial competing bid system whereby the first bidder was the only party allowed to improve its initial bid if it wished to do so, to the detriment of other competing bidders. This generated the undesirable form of opportunistic behaviour known as 'low balling' and prevented the target company's shareholders from extracting the greatest possible value. Additionally, to qualify as such, any competing bid had to provide an improvement in the consideration offered of at least 5 per cent.

From a general economic perspective, the entire subject of auction design and strategy is numbingly complex, with numerous variables coming into play. At any rate, the new system has removed the 'first mover advantage' and will clearly have beneficial effects for target companies' shareholders, as the Aldeasa case suggests (see below).

The new system provides for two phases in the handling of competing bids. In Phase 1, an ascending price auction ('English auction') takes place within 10 calendar days from the beginning of the acceptance period of the previous bid and no later than 30 calendar days from the beginning of the acceptance period of the initial bid. Any bidder is free to launch a competing bid as long as such a bid represents an improvement over the previous one, by, for example, setting a better price, reducing or removing take up conditions, or extending the bid to a larger number of the target company's shares. In Phase 2, all bidders have an opportunity to submit sealed bids, as long as this new bid offers at least the same consideration as the highest bid in Phase 1 and further represents an improvement over previous bids by extending the offer to a larger number of the target's shares. In addition, improvements no longer have to meet a minimum quantitative level, so that any improvement in the consideration offered now qualifies as such.

However, it is unfortunate that the issues at stake were not further discussed before these new rules were adopted, including, in particular, analysis of whether the second and final round of sealed bids would generate the most efficient outcomes in terms of both shareholder value and the overall dynamics of the takeover process.

**Case study: The battle for Aldeasa (2005)**

Aldeasa is a group of specialised airport retailing outlets in which Altadis, the Franco–Spanish tobacco company, held a 35 per cent interest. The battle over Aldeasa was highly interesting from a practical standpoint because it was the first test for the new competing bid rules enacted under RD 432/2003.

On 13 December 2004, the Spanish company Gestión de Exploitaciones Aeroportuarias (GEA) launched a takeover bid at €29.00 per share for 100 per cent of Aldeasa's share capital. This bid was formally authorised by the CNMV on 18 January 2005. On 24 January, the Swiss group Dufry Holdings launched a competing bid at €31.00 per share and reduced the minimum take up threshold to 50.1 per cent of Aldeasa's share capital. On 28 January, Altadis and Autogrill (controlled by the Benetton family of Italy) launched a joint bid at €33.00 per share, with no minimum take up conditions.

On 14 March 2005, the CNMV announced that, with all three bids having been registered, the deadline for the submission of sealed bids would elapse on 21 March. Once the sealed bids had been opened by the CNMV, the situation was as follows: GEA did not take part in the auction, Dufry maintained the terms of its initial bid and Altadis/Autogrill increased their bid to €36.57 per share.

## Taking the company private: mandatory bids in 'public to private' context

When a majority shareholder or group of shareholders decides that there is no longer any point in having a company publicly traded, Spanish law requires that any delisting resolution must be approved by the general shareholders' meeting and that a takeover bid must be launched by the company itself, or by the controlling shareholders, in order to afford minority shareholders a last chance of liquidity and exit from the company. The consideration offered is subject to 'fair price' provisions and has to be formally approved by the CNMV.

Although the takeover rules do not contain specific valuation parameters, in practice, the CNMV requires a 'fairness opinion' in relation to such delisting bids, using standard valuation methodologies such as discounted cash flow models and comparable transactions analysis, in the context of whether the company has been subject to a recent takeover bid.

As a matter of administrative practice, whenever there has been an arm's length bid to delist a public firm, on terms that satisfy the CNMV that the consideration offered is clearly above market value, the regulator has accepted the placement of a standing purchase order with a registered broker-dealer or bank at the offer price, instead of requiring the launching of a second bid. This allows minority shareholders to sell their shares at any time. The measure is most welcome because, while it affords the necessary levels of investor protection, it also dramatically reduces the transaction costs for the bidder; this is now often used by private equity funds in typical 'public to private' transactions.

**Case study: Telefonica/Terra Networks (2003/2005)**

In November 1999, in the midst of the 'dot com bubble', Telefonica floated its internet and e-business division through an initial public offering (IPO) of 23.6 per cent of the share capital of Terra Networks. The IPO was placed at €11.80 per share. Three months later, the stock was trading at an amazing €141 per share, which meant that Terra's market capitalisation topped €30 billion. Subsequently, Terra acquired the US internet company Lycos, in a deal which diluted Telefonica's stake down to approximately 40 per cent.

At the end of 2000, after the 'bubble' had burst, shares were trading at €11.60 and reached prices as low as €2.77 in September 2004. Further, corporate strategy changed and Telefonica found the need to provide broadband packages to its customers, which directly competed with Terra. On 28 May 2003, Telefonica launched a takeover bid for the 61.6 per cent of the share capital that it did not own for a consideration of €5.52 per share. The offering price sparked the anger of minority shareholders, representing 3 per cent of its share capital, who went as far as to file criminal charges against Telefonica's and Terra's boards of directors. Although the lawsuit was eventually dismissed, the main argument of the minority shareholders was that the IPO at €11.80 per share in 1999, which at the time took into account future profits and the increased value of the services provided by Terra, was a manipulative scheme to artificially increase Terra's price and, subsequently, to take the company private. This disguised the real purpose of the takeover bid in 2003 and thereby allowed Telefonica to elude the 'fair price' provisions applicable to such bids. Finally, the bid, which was conditional on acceptance by shareholders representing at least 36.63 per cent of the share capital, was accepted by 33.6 per cent, which gave Telefonica control over only 71.97 per cent of the share capital, after waiving the minimum percentage of acceptance initially required.

Subsequently, Terra undertook a treasury share buy-back, which increased the Telefonica stake to over 75 per cent. In February 2005, Telefonica proposed a merger with Terra by means of an exchange of nine shares in Terra in exchange for two shares in Telefonica, which represented a premium of 0.73 per cent on the day prior to the announcement, plus a dividend of €0.60 per share. Although in mergers minority shareholders are protected by the appointment by the Mercantile Registry of an independent expert in charge of evaluating the merger price, in this case, Telefonica gained full control over Terra without the requirement of launching a delisting takeover bid. Even after the CNMV stated that the nature of the transaction required its indirect supervision, this transaction was also challenged by Terra's minority shareholders on the same grounds as the takeover bid two years earlier. On 31 May and 2 June 2005, respectively, Telefonica's and Terra's shareholders approved the transaction, although criminal and other judicial proceedings are still pending.

## Potential impact of the Takeover Directive on the Spanish regime

In December 2003, after 15 years of negotiations, a political compromise was finally reached that led to the enactment of the Takeover Directive (Directive 2004/25/EC of 21 April 2004). This directive saw the light of day only after a long and acrimonious journey, and on the basis of a highly controversial compromise on two of its key provisions, which were made optional, allowing member states to opt out and firms in these states to opt back in:

- Article 9, which prohibits offeree companies from taking defensive action to frustrate bids without prior shareholder approval; and
- Article 11, which allows offerors to 'break through' certain target company restrictions (such as super-majority provisions or other by-law protections) or other measures that distribute control rights disproportionate to cash flow rights (such as dual-class shares) in order to achieve full control of the target company.

EU regulation is by definition supranational and hence harmonisation is its *raison d'être*. With respect to takeovers, the European Commission advocated harmonisation for the obvious reason that common takeover rules are a key requisite of an integrated market and promote the development of a level playing field for cross-border bids. Obstacles or distortions in cross-border takeovers, caused by differences in national legislation, are undesirable. However, common rules promote a level playing field only if the harmonised jurisdictions are sufficiently similar along other relevant dimensions. Given the considerable variations in ownership and control arrangements within the EU, this condition is far from being satisfied in the case of takeovers and the Takeover Directive has certainly not contributed to promoting the creation of this level playing field, because it will not result in a uniform regulatory framework.

At this stage, it is very difficult to assess the full impact of the directive on the Spanish takeover regime. Since the deadline for implementation of the directive (May 2006) is still relatively far away, there are no draft regulations or bills (at the time of writing) that would allow an analysis of the extent to which Spain will be implementing the directive, including whether it will be opting out of Articles 9 and 11. However, with the exception of the regulation of 'golden shares' in privatised companies, over which Spain was rebuffed by the European Court of Justice (see Commission vs. Kingdom of Spain, Case C-463/00, 13 May 2003), it is probably fair to say that Spain has generally not hampered the free movement of capital. Therefore, its position would probably be more aligned with the Commission or the United Kingdom, viewing the directive as an effective tool with which to subject companies to the market for corporate control and to outlaw obstructive defensive tactics, rather than with those Continental member states that approach capitalism from a larger stakeholder perspective and are more protectionist.

## Special topics in takeover practice in Spain

### Break-up fees

Break-up fees are a familiar practice in international mergers and acquisitions (M&A), for both public and private companies. The target company's shareholders and/or the target company itself undertake to pay a certain amount to a bidder, in exchange for launching a binding offer, if the offer is subsequently defeated by a higher bid. Break-up fees typically include out-of-pocket expenses incurred by the unsuccessful bidder, such as accounting and lawyers' fees or banking expenses. The rationale is that the target company's shareholders have managed to sell at a higher price because of the effort and cost incurred by the initial bidder, whose bid caused the target company to be put into play in the first place. Hence, the argument runs, it is only fair to reimburse at least the expenses of the bidder whose action lies at the origin of the target shareholders' ability to pocket a hefty premium.

On the other hand, there has been a substantial degree of criticism of break-up fees, particularly in scholarly studies, as it is argued that they act *de facto* as a sort of 'poison pill', which could make a competing bid substantially more expensive. The discussion then moves between those who hold the position that break-up fees paid by the target company should be considered illegal *per se* and those who consider that they are a matter to be decided on a case by case basis, under the business judgement rule and the general duties of care and diligence. The question becomes, essentially, how much is too much?

In Spain, the matter has yet to come before the courts and there had not been an administrative ruling until the CNMV took a stance in the recent CVC/Cortefiel case (2005).

**Case study: CVC/Cortefiel (2005)**

In the context of its €1.4 billion takeover bid for Cortefiel, a fashion retail business, CVC, a UK private equity house, agreed with the two controlling shareholder families, who jointly held over 57 per cent of the target's common stock, that if a successful competing bid was launched, the target company would pay CVC €3.5 million in break-up fees. The CNMV ruled that this provision was in violation of the principles of the Spanish takeover regime, although the specific grounds for its ruling have not been made public. The prospectus was accordingly modified and the controlling families agreed to assume their commitment directly with CVC.

It is difficult to envisage a judicial challenge in this case, because a decision takes too long and it is widely perceived that players in the M&A market, particularly private equity houses, do not want to antagonise the CNMV on relatively minor issues when their prospectus approval is still pending.

## Structuring irrevocables with target shareholders

The general principle established in the existing takeover rules is a shareholder in a target company is automatically released from any tender of his/her shares to a first bidder upon registration of a competing bid. Bidders tend to try to minimise uncertainty in the outcome of the process by building 'toeholds' in the target company and by securing contractual commitments with relevant shareholders of the target company. Both devices reduce the target company's free float, enhance the likelihood of a successful outcome and reduce the likelihood of a competing bid.

A classical topic is the negotiation of an 'irrevocable commitment' with key target's shareholders. While the shareholders in a target company are usually very keen to enter into contractual arrangements of this nature with potential bidders if this prompts the launching of a takeover bid, they normally seek to obtain opting out mechanisms enabling them to obtain release from such contractual commitments if competing bids are launched with sweetened terms, so that they can guarantee that any upside is captured. In practice, this leads to different kinds of irrevocable selling commitments being granted by the shareholders, which may be classified as follows:

- 'strong-form irrevocables' are akin to call options granted to a potential bidder and mean that the shareholder waives any right to sell its shares to any third party. This happened in the EDP-Cajastur/Hidrocantábrico case (2002) when, after failing to secure control of the Spanish utility Hidrocantábrico, TXU granted an irrevocable selling commitment to EDP-Cajastur at a price of €24.00 per share and was forced to forgo two subsequent bids at €26.00 and €27.2 per share. This also happened in the Recoletos bid by Retos Cartera (2005) when Pearson agreed to dispose of its shareholding interest in favour of the vehicle at a predetermined price, as well as in the recent bid launched by INSSEC for CIE Automotive (2005);
- 'semi-strong-form irrevocables' commit the selling shareholder to sell and permit release from that commitment only if a competing bid improves the selling price by a premium of at least x per cent over the agreed price. This was precisely the agreed structure in the recent CVC/Cortefiel case (2005), in which the key shareholding families irrevocably committed themselves to tender to CVC unless a competing bid with an 8 per cent premium over the agreed price was launched;
- 'weak-form irrevocables' involve a commitment to tender to the bidder's offer at a certain price, but release the target's shareholders from any commitment if a competing bid or offer is made.

In all cases, such contractual arrangements have to be disclosed by the bidder in the prospectus. The CNMV carefully scrutinises these arrangements to ascertain whether there are other provisions in these agreements that could breach the fundamental principle of equal treatment of all the target company's shareholders.

## Obtaining exclusivity and due diligence from the target company's board

Agreements entered into between the bidder and incumbent shareholders prior to the formal launching of a bid are increasingly common. Typical examples include exclusivity arrangements, due diligence access (Barclays/Banco Zaragozano, 2003; Advent/Parques Reunidos, 2003; Expo-An/Inmocaral, 2005 and WAM/Amadeus, 2005) and even collaboration to ensure an orderly completion of the transaction (Barclays/Banco Zaragozano, 2003).

There is, however, a significant legal loophole that is not easy to resolve when it comes to reconciling the general principles of equal treatment, freedom of contract and necessary confidentiality. Indeed, a potential bidder could also ask the target company's board to provide access to data as a prerequisite for the launch of a competing bid with improved terms. This would place the board in a difficult position. The board has a clear duty to maximise shareholder value and offer the possibility of purchasing the firm to a number of genuinely interested bidders. This was the case in Amadeus (2005) where, once Air France, Iberia and Lufthansa had decided that they would partially sell their stakes in the company, a formal auction period was organised. On the other hand, protecting confidentiality is a key concern, particularly where the potential bidder is a direct competitor. As yet, there are no precedents addressing this issue.

## Squeeze-out and sell-out

In Spain, neither the takeover regime nor corporate law envisage the possibility of 'squeezing-out' minority shareholders once a certain threshold in the target company has been achieved by the bidder. This matter will have to be addressed before May 2006, when (as mentioned above) Spain implements the Takeover Directive and, in particular, Articles 15 and 16.

It has been argued that there are ways of achieving a functionally equivalent result through Article 164.3 of the Ley de Sociedades Anónimas (Public Companies Act), which effectively allows a company to reduce its share capital by retiring its own shares as long as the majority shareholders can show there is a legitimate 'corporate purpose' (*interés social*) and the company has the cash to finance this share buy-back. Thus, those minority shareholders who did not tender for different reasons during the bid can be bought out at a 'fair price'. The bid price would presumably be deemed to be fair, although a fairness opinion would be required. The only apparent drawback of this procedure is that it also requires the approval of the majority of shareholders whose shares are subject to the retirement offer, but this can easily be circumvented in practice.

Finally, it should also be mentioned that a target company's shareholders have no 'sell-out' rights under Spanish law.

## Conditional bids

Until RD 432/2003 was implemented, takeover bids in Spain could only be conditional on acceptance by a minimum number of shareholders and on approval by the competition authorities. RD 432/2003 permits offers to be conditional on adoption or ratification by the target company, its board of directors or its shareholders' meeting through predetermined resolutions, agreements or plans.

One of the objectives of these new provisions was to facilitate the removal of takeover defences. For example, during its unsuccessful attempt to take over the Spanish electricity utility Hidrocantábrico (2002), TXU publicly stated its wish to condition its offer on the removal by the general shareholders' meeting of provisions in Hidrocantábrico's by-laws (*estatutos*) that limited the voting rights of significant shareholders. However, TXU was unable to do so under the then-existing takeover rules. Such a conditional offer would now be possible.

The right of the offeror to waive the condition that the offer be accepted by a minimum number of shareholders has been maintained. However, it should be stressed that no other conditions are acceptable.

## Appealing against decisions of the CNMV

Although the CNMV's decisions are subject to appeal before the Audiencia Nacional – Sala de lo Contencioso (the High Administrative Court), in practice, the right of appeal is almost entirely theoretical, because even provisional decisions could take three to four months to be rendered, which creates an impossible situation of legal uncertainty surrounding a takeover bid. However, in relation to delisting or 'going private' bids, minority shareholders have challenged the 'fair price' agreed to by the CNMV.

## Further case studies

### Three controversial takeovers (2002)

During 2002, there were three controversial acquisitions of stakes in public companies that, although they were below the 25 per cent threshold that would have triggered the MBR, did *de facto* involve a change of control. These transactions were the following:

- the acquisition in April 2002 by ACS from the Spanish bank BSCH of a 23.9 per cent investment in Dragados, a major construction company, at a 59 per cent premium;
- the acquisition in May 2002 by Sacyr, also from BSCH, of a 24.5 per cent interest in Vallehermoso, a large real estate company, at a 31 per cent premium; and
- the acquisition in June 2002 by Bami from the Spanish bank BBVA of a 23.9 per cent interest in Metrovacesa, a real estate company, at a 75 per cent premium.

In each case, the acquirer appointed a significant number of members to the target company's board of directors in the aftermath of the transaction. As discussed above, under the new regulations enacted in 2003, this is no longer possible.

**Case study: Metrovacesa/Quarta Iberica and Astrim (2003)**

Following the taking of control by Bami in 2002, Metrovacesa received a takeover offer for 100 per cent of its share capital at a 30 per cent premium from the Italian firms Quarta Iberica and Astrim. The board of Metrovacesa, influenced by Bami, opposed the deal. Accordingly, this hostile bid, which was conditional on 50 per cent of the shares being tendered, ultimately failed.

The CNMV undertook an investigation into Bami and its influence over the board of Metrovacesa, finding that it had violated the MBR in its acquisition of Metrovacesa shares because it controlled more than 25 per cent of the share capital. As a result, the voting rights of Bami in Metrovacesa were suspended.

There have also been in-depth investigations into allegations that Bami had agreed with a number of savings banks and other third parties to buy target shares and hold them with the sole purpose of frustrating the bid launched by the Italian companies. The CNMV could not prove the existence of such warehousing/parking arrangements, which would have triggered 'acting in concert' provisions. This highlights the practical difficulty of proving the existence of certain loose 'gentlemen's agreements', particularly when support is 'paid back' by way of long-term business flow that is entirely legitimate.

**Case study: Unwinding joint control – the FCC case (2004)**

FCC is one of Spain's largest construction conglomerates, with substantial interests in environmental services, water, cement and real estate. More than 52 per cent of its share capital was held by a holding company in which Esther Koplowitz and Veolia Environnement (formerly Vivendi) shared joint control, although Ms Koplowitz had a dominant say in the vehicle and in the operational subsidiaries. The European Commission cleared Veolia's acquisition and the shareholders' agreements as reflecting a 'joint control' situation.

When, after a series of disagreements with Ms Koplowitz, Veolia concluded that this partnership had come to an end, it placed its stake in the company up for sale; a group of private investors acquired it, changing the control structure of FCC in the process. Veolia's stake was acquired at a price above the prevailing market price and the transaction was notified to the Spanish Competition Authority on the basis of a change from 'joint control' to 'single control' by Ms Koplowitz. However, the CNMV did not conclude that Ms Koplowitz was under any obligation to launch a takeover to afford the remaining shareholders of FCC the opportunity to share in the control premium paid.

Whether this makes sense or not, one of the key conclusions to be extracted from this case is that the CNMV has refused to automatically apply standard 'control' categories and concepts used by competition lawyers in merger control analysis (joint control, decisive influence and negative control) to takeover law analysis. The case also highlights a potential loophole in the application of the MBR. Changes of control at the private holding company level (in a private/public company pyramid), even when the underlying asset is the control stake in a public company, seem to be exempt from the application of the MBR.

**Case study: The Amadeus bid (2005)**

Amadeus is a leading global distribution system and technology provider for the global travel and tourism industries. Controlled by Air France, Iberia and Lufthansa, Amadeus is a Spanish company whose shares are traded on the Madrid, Paris and Frankfurt stock exchanges. Sensing a strong appetite in the market for the business operated by the company, the three airlines organised a limited auction in which they accepted different offers from interested parties, finally choosing as partners BC Capital and Cinven Partners, which had submitted binding offers at €7.35 per share. Since the airlines wanted to retain significant stakes in the company, this was a complex deal in which the airlines were simultaneously sellers and bidders, because they joined the private equity investors in a Luxembourg holding company that in turn owned the Spanish bidding vehicle.

This bid is particularly interesting for the following reasons:

- the way the auction process was managed;
- the complex roll up structure agreed between the airlines and the private equity investors, which gave the airlines the option of reinvesting part of their cash proceeds in the vehicle;
- the firm's listing on three stock exchanges (Madrid, Paris and Frankfurt), which raised complex cross-border issues for the various supervisory authorities involved, compounded by publication/disclosure requirements and language issues; and
- the fact that only certain target shareholders (the airlines) were offered the chance to 'roll up' (reinvest part of the cash received in the bidding vehicle), which raised interesting issues as to whether this breached the target shareholder parity treatment principle and whether all target shareholders should have been offered the same opportunity.

## Some practical thoughts on takeovers in Spain

First, it is important to keep in mind that the MBR is a precondition for acquiring a significant stake in a public company and not an *ex-post* requirement. Overstepping the thresholds without having launched a bid could be legally considered as a serious securities infringement and give rise to not only the suspension of voting rights on the shares acquired, but also a significant fine.

Secondly, entering agreements with target shareholders prior to a bid requires a careful analysis to establish whether such agreements exclusively plan to structure irrevocables and/or if they attempt to regulate long-term shareholders' agreements in a post-bid scenario. In this regard, it is important to emphasise that shareholders' agreements (*pactos parasociales*) in public companies have to be fully disclosed to the CNMV and to the target company.

Thirdly, Spain is a relatively small market, in which takeovers tend to be financed by banks in Madrid or Barcelona, and the number of financial advisers and law firms involved in these transactions is relatively small. Hence, it is not always easy to achieve confidentiality of negotiations and potential bids. Organising small and reliable teams is crucial.

Fourthly, launching a bid in Spain requires that the bidder be fully funded from the outset, since a bank guarantee has to be deposited at the CNMV with the complete file. This is a major problem in some cases, for example those involving UK public companies, for which the bid could be a 'class 1' transaction requiring shareholder approval. Since conditional bids 'subject to funding' or to 'shareholder approval' are not permissible, this may require some sort of bridge funding, which is not always easy to obtain and could be expensive.

Finally, within the boundaries of the applicable takeover rules, the CNMV has broad discretion to apply and interpret such rules on the basis of general principles, such as investor protection, fairness and equal treatment of a target company's shareholders. There is no point in attempting to challenge a ruling of the CNMV before the courts, since the timing of judicial review is incompatible with the market and financial constraints of a takeover.