



# AM&AA GLOBAL

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**A Message from the Publisher**

On the occasion of AM&AA's 2009 Frankfurt Summit, the AM&AA is pleased to announce a new monthly publication of the Alliance of M&A Advisors, *AM&AA Global*. The M&A marketplace is increasingly global and this trend has been reflected both in the business of our membership and our increased international membership and affiliations. Our new publication responds to this reality, by providing a forum for the exchange of information, best practices & connections.

*AM&AA Global* will be edited by AM&AA member Karim Pakravan, an international strategist and a senior faculty member of the Department of Finance at DePaul University. Each issue will feature an economic commentary, as well as an invited article by one of our members. We encourage our members to submit articles for publication, as well as commentary on the content of the publications. We hope that this publication will offer yet another means of sharing experiences and best practices, as well as opportunities for furthering our membership's interests.

Mike Nall, Founder  
Alliance of M&A Advisors



## EDITOR'S NOTE: MONTHLY MACRO COLOR-EUROPE ON THE WAY TO RECOVERY

The impact of the global recession in the eurozone has been brutal, with a 5% decline in GDP from peak to trough since the European economies slipped into a downswing in the second quarter of 2008. However, positive surprises in recent data releases seem to indicate that the eurozone is set for a modest rebound in the second half of this year. According to the most recent indicators, output in the two largest eurozone economies, Germany and France, rose unexpectedly by 0.1% (relative to the previous quarter), leading to a contraction of 0.5% for the area as a whole. In addition, recent readings of business confidence in both Germany and France, have been positive, a trend reinforced by a rise of the Eurozone PMI (purchasing managers' index, a survey reflecting business confidence) for both manufacturing and services to close to 50, the tipping point between a contraction and an expansion. Financial markets have also rebounded, with the European STOXX600 index by 48% between its low point of March 9, 2009 and the end of August.

While the European consumers have been better protected than their American counterparts by an extensive safety net, they have also been buffeted by a rise in unemployment and are expected to stay on the sidelines. The key short-term recovery drivers of the

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eurozone, at least in its largest members, will initially come from manufacturing and exports. Those variables, in turn, are tied to global economic trends, which have turned positive, with global manufacturing and trade in an upswing. With the end of the severe inventory reduction cycle in sight, conditions for an economic rebound in the eurozone are in place. In addition, fiscal and monetary conditions are to remain supportive, with the G20 pledging to maintain fiscal stimulus measures in place, and the ECB in no hurry to raise interest rates. Overall, this should lead to economic growth of 1.5-2.5% (annualized) in the second half of 2009 and 3% in 2010.

We must also recognize that strong headwinds remain: low consumer confidence, an unresolved banking and financial crisis, and a generally anemic forecast for the United States, the key player in any global upswing. Moreover, the recovery is unlikely to reduce unemployment significantly. Finally, it will not be evenly distributed—Germany and France are likely to benefit from any upswing, with Italy, Spain, Portugal and Greece continuing to lag. These factors have led the ECB to maintain a very cautious stance driven by a pessimistic forecast. Nevertheless, the European green shoots are very real and could launch a self-reinforcing virtuous cycle of positive economic data and improved business and consumer confidence.

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## Lessons in Cross-Border M & A Transactions

By Ralph Hummel



The fundamental advice for international business transactions is obvious and easy to understand: different countries have different laws, business habits and cultures. These differences may range from minor nuances, such as lengthy French business lunches or unusual Spanish office hours, to significant legal roadblocks, such as strict European employment laws.

Many investors may be alert to some of these basic issues and may take them into account when considering a business deal overseas. But it is often the issues that are routine or common to many domestic transactions that can create roadblocks in international deals. Often, a buyer may not realize that a key issue in a U.S. deal must be handled differently – or may not be possible at all – in a foreign country.

The problem, of course, is that it is very difficult to raise questions regarding legal issues under foreign law if you have no reason to believe that there may be an issue at all. To make you aware of potential issues regarding cross-border deals in general and in Germany in particular, based on more than 20 years of experience in international transactions, I have listed below some key areas of concern.

### I. Legal Title

#### 1. Shares in a Corporation

Depending on the jurisdiction, you may verify share ownership using share certificates, share transfer documents or public registers. As a result, transferring shares may require the transferring of share certificate(s), executing transfer documents in written or notarized form, or possibly filing additional registrations.

For example, shares in a German closely held corporation (a "GmbH") can only be sold and transferred validly through a notarial sale and transfer document, which must be notarized by a German or possibly other civil law notary. (The German notary function normally requires a higher level of professional than is true in the U.S.) Because a GmbH very rarely issues actual share certificates, verifying the seller's title to the shares requires a thorough review of the initial incorporation document as well as an uninterrupted chain of valid notarial transfer deeds. The validity of these transfers must be reviewed very closely. During due diligence, you may often discover share transfers from prior transactions that fail to comply with strict formalities regarding the assignment, capital increase/split or combination of shares under German corporate laws. It is not uncommon for the selling shareholders to learn that they are not the legal owner of "their" shares and that they must enter into new valid transfer documents with the previous owners before the new buyers can acquire them. A recent reform of the GmbH-law provides for an acquisition of shares in good faith based on the most recent shareholders list filed with the register. However, the good-faith acquisition is subject to several conditions and limitations and does not eliminate the need for a thorough due diligence.

## **2. Real Estate**

Unlike in the U.S., German law does not allow for title insurance. Ownership to land and buildings, however, can be proven easily using an excerpt from the public land register maintained at the local court where the real estate is located. Title cannot be transferred without registration in the register, and any earlier registrations or applications to the register have preference over later entries or applications. The land register also establishes the face value of any mortgages related to the real estate, as well as any other third party's rights.

## **II. Security/Collateral**

In different countries you will also find many different ways to secure claims. Although registration of security interests does exist for real estate, Germany does not have a system for movable assets comparable to the provisions of the UCC in the U.S. Germany and most European countries provide that the title to goods sold and delivered to the purchaser may be retained subject to a security interest, but this is not registered in a public register. Instead, in due diligence, you have to rely on representations and warranties from the seller and a review of documents/agreements with banks and other creditors.

## **III. Employment and Labor Law**

All European member states have strict employee protection rights including protection against termination. When a buyer acquires a company's shares, he remains bound by all existing individual employment agreements and bargaining agreements. Employees are also protected against termination arising as part of an asset deal. As a result, the issue for buyers is not which employees should be kept, but whether and how the company can terminate any employees. Such terminations are frequently challenged by employees in court and generally result in generous severance payments to employees. If the company has an employees' representation body (known as a "Works' Council"), not only the individual employees' rights but also co-determination rights must be observed, which can be time consuming and costly. These consequences have to be considered when the level of employment is an issue during negotiations between the seller and purchaser of a business.

## **IV. Role of German Management**

Unlike a U.S. corporation, a German closely held corporation (GmbH) usually has no board, but only two bodies, the shareholders' assembly and the managing body, which consists of one or more managing directors ("Geschäftsführer"). A managing director usually does not need shareholders' approval to negotiate and sign contracts on behalf of the company with third parties. For internal purposes only, the shareholders can require that they give their prior approval to certain actions of the managing directors, and non-compliance could allow the shareholders to terminate a managing director for cause and/or pursue claims for damages against the managing director. However, third parties may still rely on the agreement which the managing director entered into on behalf of the GmbH.

## **V. Negotiations/Purchase Agreement**

Typically, negotiations will be held in English. In Germany and in many other European countries, business people have a fairly good knowledge of the English language. However, the level of English knowledge can be very different and you should be aware of hidden misunderstandings. Such misunderstandings may even occur if there are no language problems. Instead, different legal and business concepts may result in different interpretations and expectations of the parties based on the agreed wording.

German sellers will usually also accept an English purchase agreement – but will often insist on the application of German law. You will often find American-style agreements with changes made to accommodate legal necessities under German law. This can easily make U.S. parties feel comfortable, but they should never forget that the agreement is governed by a foreign law. You cannot simply rely on the provisions of the agreement as to the rights and obligations of the parties. As under the other civil law jurisdictions, German statutes provide various legal claims – which do not need to be mentioned in the purchase agreement – but which will always apply in addition, unless they have been validly excluded in the written document. This may include the right to withdraw from the agreement at any time post closing and all kinds of other claims for damages.

The formal requirements for a binding offer or purchase agreement vary, depending on the transaction. For example, the acquisition (including options, purchase offers, etc.) of shares in a GmbH or of real estate require a civil law notarization ("Beurkundung") by a German notary. This includes a requirement that the entire agreement must be read aloud by the

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notary to the parties or their proxies and the notary is obligated to advise the parties on the major rights and obligations under the agreement. The notary must have a legal education and is – depending on the state – very often also admitted as an attorney. Due to the reading requirements, be prepared for a notarization which will take hours or even a full day. Or send your German attorney as a proxy.

To summarize, don't learn the lessons of international M & A the hard way, through painful personal experience. Instead, prepare yourself for the deal in advance, and make sure you get in-country advice on local laws and business habits at the earliest stages of the transaction.

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