Austria

Negotiated M&A Guide

Corporate and M&A Law Committee

Contact

Christian Herbst

Schoenherr
Vienna, Austria

ch.herbst@schoenherr.eu

1. INTRODUCTION

Private M&A in Austria primarily relates to limited liability companies (GmbH), which is the most frequent type of company involved in a share or an asset deal, while stock corporations (AG) are primarily used for public companies. Other types of companies may be involved as targets as well, including limited liability partnerships (GmbH & Co KG or KG) or unlimited partnerships (OG). The popularity of asset deals, even for the sale of business units, has decreased because tax law changes now allow for similar beneficial tax structuring in share transactions and asset deals and the 2007 reform of the Commercial Code (*Unternehmensgesetzbuch*) introduced elements of universal succession to asset deals.

The following overview is not a comprehensive summary with respect to the sale and purchase of private companies. The guide shall provide an introduction to a foreign practitioner on key aspects of negotiated M&A transactions relating to the Austrian market.

2. STRUCTURE OF THE TRANSACTION

The acquisition of companies through the purchase of shares or assets is not subject to special regime legislation but various statutes apply. For privately negotiated transactions requirements and restrictions contained in various laws and, if applicable, in the target's by-laws must be observed. The legal issues vary according to whether the transaction is structured as an asset or share deal. Tax considerations (goodwill depreciation) and cherry-picking of assets may call for an asset deal, yet tax group structures allow good will depreciation also in share deals. For both asset and share deals, special purpose acquisition vehicles, i.e. local or foreign new companies, may be used to minimise tax exposure and reduce transfer costs. Business combinations can of course be effected through mergers and other reorganisations and cooperation structures; this overview, however, concentrates on the acquisition (sale) of shares and assets through privately negotiated deals.

Relevant regulations governing private M&A include the following civil, corporate, tax, employment, stock exchange and antitrust laws:

- Joint Stock Corporation Act and Limited Liability Company Act (AktG, GmbHG);
- Demerger Act (SpaltG);
- Minority Shareholders Squeeze Out Act (GesAusG);
- Corporate Transformation Act (UmwG);
- Stock Exchange Act (BörseG);
- Cartel Act (KartellG);
- Reorganisation Tax Act (UmgrStG);
- Co-determination Act (ArbVG);
- Employment Contract Adaptation Act (AVRAG);
- EU Merger Act;
- Act on the Societas Europea (SE-G);
- Law on Enterprises (UBG) and General Civil Code (ABGB);

- Foreign Trade Act
- EC Merger Regulation; and
- Law on exclusion of shareholders (GesAusG).

3. PRE-AGREEMENT

Pre-agreements, in the form of letters of intent, heads of agreements, memoranda of understanding or term sheets are the rule in private equity transactions, yet less frequent otherwise.

Following international standards, private equity transaction term sheets can be very detailed and will often include the terms of the subsequent purchase agreement documentation. Auctions will usually involve indicative offers, which will be non-binding, and binding offers.

Letters of Intent for private transactions outside the private equity environment tend to be short. LOIs may define a price or price range, which usually will be explicitly subject to further adaptation or negotiation following the outcome of due diligence, and will: (i) typically set out the content and time frame of the steps, perhaps the type of transaction (share/asset deal), scope of due diligence and the time frame for due diligence and contract negotiations; (ii) often provide non-solicitation covenants relating to the employees of the target company; (iii) sometimes provide for exclusivity, and (iv) set out whether buyer or seller will prepare the first draft of the documentation. With the exception of private equity term sheets, LOIs will rarely set out specifics of the contract terms and the representations and warranties, but rather provide a reference to "standard representations and warranties".

Except for statutory pre-agreements (*Vorvertrag*), which have strict requirements, and are rarely used in the M&A context, Austrian law does not provide specific rules for preliminary agreements. Thus and except in the case of statutory pre-agreements, the legal nature and any legal consequences resulting from preliminary agreements are governed by the contents of the agreements.

Although Austrian courts will usually interpret LOIs as non-binding, to avoid any risks of interpretation against the intent of the parties it is Austrian market practice and advisable to define which provisions of an LOI will be binding and enforceable. Usually the binding terms are limited to confidentiality (or the reference to a separate confidentiality agreement), applicable law, venue and, if included in the LOI, exclusivity. All other terms are usually explicitly stated to be non-binding. Penalties for violation of the binding terms (e.g. on non-solicitation, exclusivity) are the exception rather than the rule. More frequently in, but not limited to, private equity transactions, LOIs may provide for reimbursement of due diligence costs usually capped with a certain Euro amount.

In the context of negotiations preceding an M&A transaction, the parties should also be aware of the following: under Austrian court practice, the parties are subject to certain duties of transparency and disclosure of information to avoid misleading the other parties in the negotiation, *inter alia*, as to their intent regarding the conclusion of a potential transaction. Failure to inform the negotiation partner in a timely manner that the respective party is no longer interested in pursuing a transaction or failure to negotiate in good faith (violation of "culpa in contrahendo") may lead to damage claims of the party which has suffered damage (e.g. third party expenses). An LOI could provide for specific duties of the parties and for compensation in that respect or, on the contrary, specifically exclude liability for such situations.

4. DUE DILIGENCE

Formalised due diligence procedures with document disclosure made in virtual or physical data rooms have become the rule in private M&A transactions. The scope of disclosure and due diligence will usually be determined by the size of the transaction and the industry involved. Private equity transactions or competitive auctions may require vendor due diligence and information memoranda and/or vendor due diligence reports provided by seller followed by buyer due diligence. Extensive disclosure by sellers will usually be combined with a request by sellers to buyer to accept, as one of the contract terms, that the disclosed facts will relieve sellers from warranty obligation or liability.

Local Austrian law aspects particularly relevant for foreign buyers are usually the regulatory requirements, in particular public law requirements, as well as employment law, rental and tenant laws and tax aspects.

As to share deals, key review items will include change of control clauses and, particularly in the case of minority stake acquisitions, shareholder arrangements, if any, as well as third party consent requirements or other restrictions on the shareholdings.

As to asset deals, the review will usually focus on whether contracts can be taken over or need to be terminated and on the requirement for third party consents (secs 38 UGB*,* 69 *et seq*. Insurance Contracts Act and 12a Tenancy Act). Additionally, and following the EU Acquired Rights Directive, the rules of the AVRAG must be observed as to employment and pension agreements.

5. ACQUISITION AGREEMENT

Form Requirements

As to share deals, the transfer of shares in limited liability companies requires the form of a notarial deed; notarization must be by an Austrian notary or a notary subject to a comparable regime (e.g. German notary). The documentation does not necessarily have to be in the German language; English language documentation can be notarized as well. Acquisition agreements for shares of stock corporations do not require notarial form. Additionally, other corporate measures which may be required in connection with M&A transactions, such as changes in the articles of association or capital measures, require notarial form. Both in share and asset deals, form requirements must be observed which do not necessarily relate to the acquisition agreement, as such, but to the valid transfer of individual assets. This applies, for example, to the transfer of real estate, where the declaration of the current owner to transfer its property right to the purchaser requires notarisation, or to the transfer of trademarks.

Format of Contractual Documentation

In larger transactions, cross border M&A and multi-jurisdictional transactions, the UK/US style of contractual documentations have been increasingly adopted with some modifications: As a rule, and in particular if governed by Austrian law, the agreements tend to be shorter and less detailed than their common law counterparts. Sometimes there is a split between the US/UK style acquisition agreement serving as a master agreement which is complemented by short form (local law style) transfer deeds.

Purchase Price

In line with international practice, purchase price clauses can be straightforward cash price arrangements and may also involve earn out or complex price adaptation mechanisms linked to net equity, net assets or a closing balance sheet. Except in distressed M&A transactions, holdbacks and escrows will be the exception rather than the rule. If seller and buyer agree to protect buyer as to its potential warranty (or other liability) claims, seller will usually prefer to provide a bank guarantee as security. As to the payment of the purchase price, seller may require a bank guarantee or parent or group company guarantee for financially non-viable purchasers.

Conditions Precedent

Conditions precedent to closing regularly involve regulatory approvals like merger control (see point below) and, in case of financial institutions including banks and insurance companies, the approval by the Financial Market Authority.

The acquisition by non-EU citizens of real estate, including certain long-term leases, or of “controlling” interests in companies owning Austrian real estate, may be subject to notification or approval depending on the federal state where the real estate is located. The respective real estate commissions of the provinces where the real estate is located will usually grant approval, especially if the property serves business and not private purposes.

In the case of the acquisition of real estate or of companies holding real estate assets, approvals may be required by regional land authorities, in particular in the case of non-EU purchasers. Additionally, conditions precedent may, *inter alia*, relate to the delivery of waivers of contract partners waiving termination rights in the event of change of control, the absence of material adverse change (MAC) events between signing and closing and the delivery of resignation letters of (supervisory) board members.

Covenants

In line with international practice, covenants between signing and closing will usually relate to limitations on the conduct of business until closing (ordinary course) and information obligations on buyer as to business development and usually also provide for a prohibition of dividend or other payments to seller by target between signing and closing.

Representations and Warranties

In line with Anglo Saxon practice, standard catalogues of representations and warranties have become the rule. These can be directly worked into the agreement or attached as a schedule, which is then an integral part of the agreement. The scope and limitations of the representations and warranties depend on various factors, including whether the agreement is presented and negotiated as part of a competitive auction, whether the transaction is a private equity transaction or an MBO, the negotiation power of the parties involved, the scope of the due diligence allowed as part of the transaction and industry standards. Representations and warranties given by seller are a core feature of the acquisition agreement. Following UK/US style standards the representations and warranties by buyer are usually short and their nature and scope will be driven by the individual transaction circumstances.

There are Austrian statutory rules on warranties and damages, including a statutory regime relating to indemnities. Thus, state of the art acquisition agreements should include not only detailed representations and warranties but also detailed remedies which will apply in the case of violation of the representations and warranties (including the exclusion of remedies which are not specifically provided for in the contractual documentation). The contractual regime will seek to replace the statutory regime to the largest extent possible and usually will exclude rescission of the agreement (except for very special circumstances like defects in the ownership of the shares or core assets) and limit buyer to claim damages, which are contractually defined and limited in scope and amount. Certain mandatory rules of Austrian law may still apply and override contractual limitations and exclusion of claims, e.g. claims based on deceit or collusion.

Representations and warranties can be designed as independent guarantees or straightforward representations and warranties. They have legal effect as of signing or closing or both. Their scope is influenced by disclosure which usually is made by due diligence disclosure and/or disclosure in schedules to the contractual documentation.

The catalogue of typical representations and warranties is in line with international standards and refers to matters such as:

- ownership and corporate issues (including but not limited to ownership of shares and assets, corporate structure, bylaws, capital stock, capital maintenance, profit and loss agreements and shareholder agreements)

- assets, liabilities and financials of the target companies involved (including but not limited to balance sheet and books of account warranties)

- taxes and social security

- assets, inventories, receivables, main agreements

- intellectual property (trademarks, patents, licenses)

- employment (including shop agreements and pensions)

- insurance

- environment and regulatory permits

- real estate

- pending and threatened claims and disputes

The content and scope of the representations and warranties will also be determined by the industry of the target which may lead to industry specific warranties. Additionally, clauses confirming the accuracy of information and the completeness of disclosure and of stipulations, as well as on misrepresentations, are standard. Sellers will usually try to limit the scope of many warranties to best knowledge by the shareholder, whereas buyers will want blanket, broad warranties, limited qualifications of best knowledge and, if qualified by best knowledge, will want to include the knowledge of the target executive and second tier target managers. Parties need to also focus on the regulations regarding burden of proof since this will often be decisive in whether a warranty claim can later be pursued or successfully defended against.

Indemnification

Parties and advisers should pay particular attention to the section of the agreement which regulates the legal consequences of a contract breach, in particular a breach of the representations and warranties. The clauses on indemnification will not only set out the remedies available but also define, and usually thereby limit, the kind of remedies available, their scope, limitations as to amount and as to the cut-off date for pursuit of a claim. Given the difficulty to re-transact, rescission of the sale and purchase agreement will usually be excluded, whether based on impossibility to cure substantial (value) defects or error or on other grounds. On an exception basis, some contracts do allow for rescission, for example in the case of title defects. The indemnification regime usually also provides a notification duty by buyer of a breach of a warranty or defect within a stated time, and for the possibility for seller to cure the defect and, failing such remedial action, for buyer to be entitled to claim for damages, payable either by the seller or the target. Buyer will aim for a broad definition of loss; a point of negotiation is usually also whether, and to what extent, lost profit or certain types of indirect damage are excluded. Caps and floors, baskets defining and limiting the amount of damage entitlement are consistent with international practice and, as to the thresholds, are usually determined by the bargaining power of buyer and seller. Title, tax and, if applicable, environmental warranties are usually carved out from the regime of floors and may be governed by a special remedy regime and special limitations. Under Austrian law, unless otherwise provided contractually, claims for the recovery of losses due to a violation of a purchase contract can be based on either a violation of representations or warranties or on contractual tort. As to warranty claims, fault is not a requirement for a claim, however it is a requirement for tort claims. Prudent contract drafting will provide clarity as to which type of claims will be excluded under the contract.

The indemnification section usually also provides for a special regime applying to third party claims against the target company or against buyer (including, but not limited to, claims by tax authorities).

As to limitation periods, the minimum general time limit a buyer will usually seek is two years from closing, allowing buyer to have at least one full year of operation and subsequent audited balance sheet and sufficient time for claims, if any, to unravel. In seller friendly contracts the general time limitation for contractual (warranty) claims may be as short as one or one and one-half years from closing. However, for tax (including social security) claims, it is usually agreed that the applicable legal statute of limitation will apply; for title warranties and environmental warranties usually specific periods are agreed anywhere between 5, 10 and 30 years.

Non-compete

Depending on the type of transaction and industry, non-compete clauses relating to sellers (legal and individual persons) for particular segments of the industry could be part of the transactional documentation as ancillary constraints. To be valid and enforceable, non-compete arrangements need to be defined and limited in scope and time. Competition law, in particular EU law considerations, play a role and result in non-competes usually being limited to two years, or three years in the case of the transfer of know-how, from closing. Under Austrian court practise, non-compete clauses going beyond such time limitations will not be invalidated *in toto*, but reduced to the permissible limitations (i.e. partial invalidity). To avoid problems of proof, it is not uncommon to define penalty amounts for violation including repeat violation.

6. GOVERNING LAW AND DISPUTE RESOLUTION

Under Austrian private international law, parties are free to choose the law governing the asset or share sale and purchase agreement. However, rights *in rem* and the so-called modus, i.e. the requirements governing the transfer of the shares and of other assets (if located in Austria or otherwise subject to Austrian law according to Austrian private international law rules) must comply with local, thus Austrian, law requirements (for example, see above at Form Requirements). Thus agreements governed by a foreign law will need some localisation and/or local implementation. Whether the transaction documentation will be entirely or partly governed by Austrian law will depend on the respective negotiation power of the parties involved; sometimes a neutral law may be chosen as the governing law, typically German or Swiss law, because of the similarity of rules in company and corporate law matters. As to language, in larger cross border transactions it has become standard to use English as the governing language, bilingual agreements are rare, although parties may always procure translations, which are then non-prevailing.

In cross border or multijurisdictional transactions, parties usually agree on arbitration as the mechanism for dispute resolution. The most frequently chosen arbitration rules are the so-called Vienna Rules administered by the Austrian Federal Economic Chamber, the arbitration rules of the ICC Paris or the rules of the London Court of International Arbitration (LCIA). In relation to non-EU countries it is imperative or highly advisable to choose arbitration clauses to secure enforceability of an award, which as to arbitral awards may be secured under the New York Convention. Under Austrian law, agents executing an arbitration agreement under power of attorney may require a special power of attorney making specific reference to the arbitration clause to be executed.

7. MERGER CONTROL AND OTHER APPROVAL REQUIREMENTS

Merger Control

Where a concentration has a community dimension, the EC Merger Regulation applies and fully replaces the Austrian merger control regime.

Under the 2005 Austrian Cartel Act, mergers must be notified if the participating undertakings in the acquisition had turnover in the business year prior to the merger of either: more than €300 million worldwide; more than €30 million in Austria; and at least two of the undertakings each had a turnover of more than €5 million worldwide. The new Cartel Act provides an explicit exception for mergers where only one undertaking concerned has a national domestic turnover of more than € 5 million and all other undertakings concerned have a total worldwide turnover not exceeding € 30 million. As to transactions which are implemented from 1 November 2017, an entirely new additional notification threshold applies, which is built on a combination of turnover, transaction value and the target being active in Austria as follows: A notifiable concentration also applies, if cumulatively the combined worldwide turnover of the undertakings concerned exceeds € 300m, the combined Austrian turnover exceeds € 15m, the value of the concentration(purchase price plus liabilities taken over) exceeds € 200m and the target undertaking has significant activity in Austria (eg site in Austria or in the digital context, eg monthly active users with Austrian nexus). Additionally, article 24/2 of the new Cartel Act provides for an effects doctrine limiting the notification requirements for merger transactions to those transactions which have an effect on the Austrian market. Turnover is group turnover; direct or indirect participation of at least 25 per cent must be taken into account. Special rules apply to the calculation of turnover of banks, insurance companies and in media mergers.

Regulated Industries

Generally there are no direct Austrian inward investment restrictions. Under the Foreign Trade Act (FTA), as last amended 2013, acquisitions of 25% or more of the controlling interests in an Austrian enterprise by non-EU and non-EEA/non-Swiss investors require advance approval by the Austrian Ministry of Economic Affairs if the Austrian target belongs to a specific protected industry, as defined in the FTA. Specific sectors protected include those related to the internal and external security of Austria, in particular of the defence equipment industry and security services, as well as the sectors relating to public order and safety and to procurement and crisis services. These include energy and water supply, telecoms, traffic and infrastructure as to education and training. Furthermore, governmental agencies cannot influence or restrict the completion of an acquisition by foreign buyers unless: (i) “fit and proper” tests or approvals are required, or (ii) licences of the target are subject to revocation in case of unapproved shareholder changes. Such approval or review requirements are limited to regulated industries like banking, insurance, telecoms, airline and gambling.

8. POST TRANSACTION MEASURES

Implementing an asset deal is usually a challenge as to transferring the employees and individual assets and integrating them, procuring the transfer of required business and operational licences or re-applying for new licences. Also stamp duty (avoidance) aspects are to be observed in asset deals.

In corporate transactions, post transaction implementation matters usually relate to changes in the boards and to corporate documentation or tax driven restructurings. Measures may be required if post closing adjustments are to be calculated based on closing balance sheets drawn up post closing, or if an earn out mechanism applies. In practice, both in share and asset deals, parties often fail to implement a proper program to monitor potential claims and to secure the evidence for warranty and damage claims.

* * * * *