

# M&A Litigation 2019

Powered by



Contributing editors

William M Regan, Jon M Talotta and Ryan M Philp





Hogan  
Lovells

Providing valuable strategic and litigation counseling from the outset of an M&A transaction through post-closing disputes.

**Our Corporate and Shareholder Litigation team is proud to support Getting the Deal Through.**

Hogan Lovells is an international legal practice that includes Hogan Lovells International LLP, Hogan Lovells US LLP and their affiliated businesses. Images of people may feature current or former lawyers and employees at Hogan Lovells or models not connected with the firm.

[www.hoganlovells.com](http://www.hoganlovells.com)

© Hogan Lovells 2019. All rights reserved.

**Publisher**

Tom Barnes

tom.barnes@lbresearch.com

**Subscriptions**

Claire Bagnall

claire.bagnall@lbresearch.com

**Senior business development managers**

Adam Sargent

adam.sargent@gettingthedealthrough.com

Dan White

dan.white@gettingthedealthrough.com

**Published by**

Law Business Research Ltd

87 Lancaster Road

London, W11 1QQ, UK

Tel: +44 20 3780 4147

Fax: +44 20 7229 6910

The information provided in this publication is general and may not apply in a specific situation. Legal advice should always be sought before taking any legal action based on the information provided. This information is not intended to create, nor does receipt of it constitute, a lawyer-client relationship. The publishers and authors accept no responsibility for any acts or omissions contained herein. The information provided was verified between April and May 2019. Be advised that this is a developing area.

© Law Business Research Ltd 2019

No photocopying without a CLA licence.

First published 2018

Second edition

ISBN 978-1-83862-120-9

Printed and distributed by

Encompass Print Solutions

Tel: 0844 2480 112



---

# M&A Litigation

## 2019

**Contributing editors****William M Regan, Jon M Talotta and Ryan M Philp****Hogan Lovells US LLP**

---

Lexology Getting The Deal Through is delighted to publish the second edition of *M&A Litigation*, which is available in print and online at [www.lexology.com/gtdt](http://www.lexology.com/gtdt).

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Australia, Austria and China.

Lexology Getting The Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at [www.lexology.com/gtdt](http://www.lexology.com/gtdt).

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, William M Regan, Jon M Talotta and Ryan M Philp of Hogan Lovells US LLP, for their continued assistance with this volume.



London

May 2019

---

Reproduced with permission from Law Business Research Ltd

This article was first published in June 2019

For further information please contact [editorial@gettingthedealthrough.com](mailto:editorial@gettingthedealthrough.com)

# Contents

<b>Introduction</b>	<b>3</b>	<b>Italy</b>	<b>48</b>
William M Regan, Jon M Talotta and Ryan M Philp Hogan Lovells US LLP		Andrea Atteritano, Francesca Rolla and Emanuele Ferrara Hogan Lovells International LLP	
<b>Australia</b>	<b>5</b>	<b>Japan</b>	<b>56</b>
Scott Harris, Christopher Moses and Gabriella Plummer Hogan Lovells		Kenichi Sekiguchi Mori Hamada & Matsumoto	
<b>Austria</b>	<b>13</b>	<b>Netherlands</b>	<b>63</b>
Valerie Hohenberg and Markus Taufner Wolf Theiss Rechtsanwälte GmbH & Co KG		Manon Cordewener, Carlijn van Rest and Bas Keizers Hogan Lovells International LLP	
<b>China</b>	<b>19</b>	<b>Spain</b>	<b>70</b>
Dong Chungang, Hu Ke and Ge Xiangwen Jingtian & Gongcheng		Jon Aurrecoechea, Eugenio Vazquez and Manuel Martínez Hogan Lovells International LLP	
<b>France</b>	<b>24</b>	<b>Switzerland</b>	<b>75</b>
Christine Gateau, Pauline Faron and Arthur Boeuf Hogan Lovells International LLP		Harold Frey and Dominique Müller Lenz & Staehelin	
<b>Germany</b>	<b>31</b>	<b>Turkey</b>	<b>82</b>
Olaf Gärtner and Carla Wiedeck Hogan Lovells International LLP		Yavuz Şahin Şen and Ebru Temizer Gen & Temizer   Özer	
<b>Hong Kong</b>	<b>36</b>	<b>United Kingdom</b>	<b>89</b>
Chris Dobby and Grace Zhu Hogan Lovells International LLP		Neil Mirchandani, John Tillman and Katie Skeels Hogan Lovells International LLP	
<b>India</b>	<b>42</b>	<b>United States</b>	<b>96</b>
Naresh Thacker and Bhavin Gada Economic Laws Practice		William M Regan, Jon M Talotta and Ryan M Philp Hogan Lovells US LLP	

# Introduction

**William M Regan, Jon M Talotta and Ryan M Philp**  
Hogan Lovells US LLP

M&A transactions typically are transformational corporate events. From comparatively small private company transactions involving tens of millions of US dollars, to the largest multinational public company deals worth more than US\$100 billion, the purchase or sale of any company involves significant risks and many uncertainties. M&A transactions impact the participants – directors, officers, employees, stockholders, creditors and customers – at every level of the corporate enterprise. And even the most strategic and well-planned M&A transactions sometimes fail to deliver the economic benefits that the parties anticipated at signing. These factors individually and collectively make M&A transactions ripe for litigation.

M&A litigation also raises many important policy issues, ranging from the appropriate role of corporate directors and stockholders both in making business decisions and in pursuing internal corporate misconduct, to the enforceability of contract provisions allocating various risks in connection with private company deals. The individual chapters that follow this introduction summarise how key jurisdictions around the world address these policy issues, and the extent to which they permit, encourage or limit M&A litigation. A survey of these chapters reveals a number of significant similarities, but also a number of important differences.

## **Common themes in global M&A litigation**

Across common law and code law countries, there are a number of striking similarities with respect to how different jurisdictions address M&A litigation issues. For example, nearly every country addressed in this book expressly or impliedly embraces some form of what in the US is called the 'business judgement rule'. Whether characterised as a formal legal presumption or simply the inherent reluctance of judges to interfere with discretionary business decisions, jurisdictions around the world show a strong tendency to protect or defer to corporate decision-making in the M&A context where the board acts in good faith, on an informed basis and without conflicts of interest.

Similarly, nearly every jurisdiction requires that corporate actors in the M&A context comply with some variation of the duty of care and the duty of loyalty. To uphold a challenged M&A decision, courts broadly require that directors and management make decisions on a fully informed basis, acting with the care of a reasonably prudent person under the applicable facts and circumstances. Jurisdictions consistently require that corporate representatives disclose or avoid conflicts of interest, such that M&A decisions are made in good faith in the best interests of the corporate enterprise, and not in the personal interests of any individual director or officer.

Another commonality across jurisdictions concerns the impact of a stockholder vote. After a board has approved an M&A transaction, separate approval by the stockholders is often required before the transaction can close. In most jurisdictions, where the stockholder vote is made on a fully informed basis, subsequent claims challenging the deal or the directors' conduct in connection with the deal typically will be barred. This may be under a theory that the stockholder vote 'ratified'

the board's decision, that the vote 'cleansed' the transaction of any fiduciary duty issues or that stockholders are 'estopped' from challenging a transaction approved by a majority of investors.

One final recurring theme is that nearly every jurisdiction applies additional scrutiny with respect to responsive or defensive measures taken by a board in response to unsolicited takeover proposals. Some jurisdictions impose heightened judicial scrutiny on such measures, while others require separate stockholder or regulatory approval. But in all cases, jurisdictions recognise the increased risks and potential conflicts when a board acts in response to an unsolicited offer.

## **Notable differences in M&A litigation across jurisdictions**

There also are a number of stark differences in M&A litigation across jurisdictions. For example, outside of the United States, few jurisdictions allow individual stockholders to pursue broad class or collective actions on behalf of all similarly situated investors, and, in particular, few jurisdictions permit class actions that require investors to affirmatively 'opt out' to avoid being bound by a judgment. Note, however, that certain European jurisdictions, including the UK and the Netherlands, have seen the emergence of collective action rules and procedures that apply in certain types of cases and that have similar features to class actions. The 'internationalisation' of US-style class actions may continue in the coming years.

Jurisdictions also vary significantly on the extent to which they permit individual investors to pursue 'derivative' actions to recover damages incurred by the corporation (some allow broad derivative rights, some do not recognise the procedure at all, and still others provide for minimum ownership requirements or court approval before an investor will be permitted to proceed).

Similarly, few jurisdictions permit stockholders to take broad pretrial discovery in M&A litigation, although most recognise some form of a books-and-records inspection right. The majority of courts also limit the ability of corporate defendants to resolve M&A litigation through early dispositive motion practice.

Jurisdictions also follow significantly varying approaches with respect to whether a corporation may limit liability for directors involved in M&A transactions through exculpatory by-law or corporate charter provisions. Some jurisdictions broadly allow such provisions; others find them void as against public policy; and others permit them for certain types of claims (eg, claims sounding in ordinary negligence or claims by outside third parties).

One final notable difference is the extent to which jurisdictions permit corporations to require stockholders to bring M&A litigation in particular forums. Certain jurisdictions permit corporations to mandate that stockholders bring M&A litigation in particular courts or even in arbitration, while others apply their general jurisdiction and venue rules.

## **Conclusion**

Public company M&A litigation is most common in the United States and certain other countries discussed in this book. This appears to be

because of class action and discovery mechanisms that permit an individual investor to pursue claims on behalf of other similarly situated investors. It is important to note, however, that US public company M&A litigation is currently undergoing significant changes. Certain leading courts have changed the law to afford greater deference to arms-length transactions approved by a stockholder vote. These changes appear to have brought US law more in line with that of other jurisdictions permitting collective actions. Following these decisions, there has been a slight reduction in the overall number of suits filed, along with changes to the types of claims being asserted and the venues where cases are being filed. The ultimate impact of these recent changes remains to be seen, however, both within and outside the United States.

# Australia

Scott Harris, Christopher Moses and Gabriella Plummer

Hogan Lovells

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The main types of claims that shareholders may assert against companies, officers and directors in connection with M&A transactions include:

- a statutory claim under the Corporations Act 2001 (Cth) (Corporations Act) for oppressive or unfair conduct;
- a statutory claim under the Corporations Act for breach of duties owed by the directors and officers to the company, or an equivalent common law claim for breach of fiduciary duties;
- a statutory derivative claim under the Corporations Act, by which a shareholder (with leave of the court) can bring proceedings on behalf of the company;
- a claim against a publicly traded company for breach of the company's continuous disclosure obligations; or
- a statutory claim under the Corporations Act, the Australian Securities and Investments Commission Act 2001 (Cth) or the Australian Consumer Law in relation to misleading or inadequate disclosure documents, misleading or deceptive conduct, or false or misleading representations.

Other claims that shareholders may assert against companies, officers and directors, although perhaps less common in connection with M&A transactions, include:

- a claim by shareholders to enforce a personal right (for example, rights pursuant to an express contract or to enforce the company's constitution as a contract between the company and each shareholder); or
- seeking an order for the winding-up of the company on various grounds, including: directors have acted in their own interests rather than the interests of the company as a whole; there has been oppressive or unfair conduct; or it is just and equitable that the company be wound up.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

#### Claims for oppressive or unfair conduct

To bring a successful claim under section 232 of the Corporations Act for oppressive or unfair conduct, a shareholder must show that the conduct or the affairs of the company, an actual or proposed act or omission by or on behalf of the company, or a resolution or proposed resolution of members of the company, is either:

- contrary to the interests of shareholders as a whole; or
- oppressive to, unfairly prejudicial to, or unfairly discriminatory against a shareholder or shareholders.

#### Claims for breach of duties by directors or officers

A statutory or common law claim for breach of duty by a director or officer is generally actionable by the company, and a shareholder may need to seek leave to bring the proceeding as a statutory derivative claim (that is, in the name of the company), although the applicant may show that a director or officer has breached their statutory or common law duties, that is, the director or officer has:

- failed to exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they were a director or an officer in a corporation in the same circumstances of that corporation, and occupied the position and had the same responsibilities within the corporation as that director or officer;
- failed to exercise their powers and discharge their duties in good faith in the best interests of the corporation;
- failed to exercise their powers and discharge their duties for a proper purpose; or
- improperly used their position, or information gained in their position, to gain an advantage for themselves or someone else, or to cause detriment to the company.

#### Statutory derivative claim

See question 8.

#### Claims for breach of continuous disclosure obligations

To bring a successful claim for breach of continuous disclosure obligations, a shareholder must show that:

- a publicly listed entity that is required to disclose information to the market operator has information that the Australian Securities Exchange (ASX) Listing Rules require be notified to the market operator;
- that information is not generally available to the market and is information that a reasonable person would expect, if it were generally available, to have a material effect on the price or value of the securities of the entity;
- the entity failed to notify the market operator of that information in accordance with the disclosure requirements under the ASX Listing Rules and the Corporations Act; and
- the shareholder suffered damage as a result of the contravention (although a number of courts have recently accepted indirect market-based causation in such claims).

#### Claims in relation to inadequate disclosure documents

To bring a successful claim in relation to inadequate disclosure documents, a shareholder must show that:

- the relevant disclosure document contained a misleading or deceptive statement (or that in relation to certain documents, there was an omission of material required to be included in the document by the Corporations Act);
- the misleading or deceptive statement or omission is materially adverse from the point of view of the holder of securities to whom the document is given; and
- the shareholder suffered loss or damage as a result.

Claims in relation to inadequate disclosure documents may more commonly be made to the Takeovers Panel (see further question 4).

### Publicly traded or privately held corporations

#### 3 | Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Shareholders in publicly traded and private companies are equally eligible to bring the claims explained in question 2. In addition, further claims or grounds for claims may arise in the following instances:

- in respect of public companies, by virtue of their regulation by the Takeovers Panel and, where their shares are publicly traded, the ASX Listing Rules. For example, public companies are required to continuously disclose information that may have a material effect on the price or value of its securities. The Corporations Act also imposes additional obligations on public companies for certain transactions. For example, member approval is required for giving financial benefits to related parties such as directors and their spouses. This is to ensure the interests of a public company's members as a whole are protected; and
- in respect of private companies, by virtue of any additional obligations or restrictions imposed under the company's constitution or any shareholders' agreement.

A breach of these obligations may, in certain circumstances, be actionable by shareholders.

### Form of transaction

#### 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

The basis of any claim is likely to be one of the claims outlined in questions 1 and 2. However, the formulation of the claim may differ depending on the form of the transaction that is the subject of the dispute.

Control transactions in Australia for entities listed on the ASX are primarily effected by way of a takeover bid or a scheme of arrangement. The Takeovers Panel is the primary forum for resolving disputes about these types of transactions.

In a takeover bid, the acquiring company makes a regulated offer to the target's shareholders to buy shares. The bidder must comply with disclosure obligations by sending a Bidder's Statement to all target shareholders. Any inadequacies or perceived inadequacies with disclosure may become grounds of complaint to the Takeovers Panel.

A scheme of arrangement is an agreement, approved by the court and the target's shareholders, to acquire all shares in the target company. Before a vote is taken, the target is required to send a disclosure document to its shareholders with a view to informing the shareholder's decision. The Scheme Booklet will contain similar information to the Bidder's Statement mentioned above, and as such may form grounds for a Takeovers Panel complaint. Furthermore, schemes of arrangement are more readily open to shareholder opposition owing to the court approval process involved.

### Negotiated or hostile transaction

#### 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

In principle, the types of claims available would not differ. However, as outlined in question 4, the nature of the transaction may affect the formulation of a claim, noting in particular the different position of directors, officers and shareholders of a company as between a negotiated transaction and a hostile or unsolicited offer. A negotiated transaction must be approved by directors but may not require approval by shareholders (for example, if it is the sale of a subsidiary or an acquisition), whereas a hostile offer for a public company would not, at least when made, be recommended by the directors of the target company although the offer will only be successful if a sufficient number of shareholders accept the offer.

Claims made in control transactions involving entities with more than 50 shareholders, or entities listed on a stock exchange, must be made to the Takeovers Panel.

Takeovers Panel claims are more likely to be made in hostile situations as parties seek tactical advantages from doing so. Complaints to the Takeovers Panel about the takeover bid generally can be made on the broad grounds of 'unacceptable circumstances', and the Takeovers Panel can declare that circumstances are unacceptable circumstances whether or not the circumstances constitute a contravention of the Corporations Act.

### Party suffering loss

#### 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes. Claims for loss suffered by the company may be brought by a shareholder pursuant to the statutory derivative action, and such claims require leave of the court (see question 8).

Claims for loss suffered by a shareholder may include the following types of claims:

- oppressive or unfair conduct;
- breaches of the company's continuous disclosure obligations;
- misleading or inadequate disclosure documents, misleading or deceptive conduct, or false or misleading representations;
- enforcing contractual rights (for example, rights under a shareholders' agreement between shareholders, or rights under a contract between the company and the shareholder);
- enforcing the company's constitution as a contract between the company and each shareholder; and
- seeking an order for the winding-up of the company.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

#### 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Collective or class action by shareholders is possible under Australian law. This can be conducted in a number of ways, including:

- commencing 'representative proceedings' in the Federal Court of Australia and in certain State Supreme Courts, where a wider group of claimants are represented by one or more representative claimants;
- consolidation of claims by the courts; or
- claims being brought jointly by shareholders.



## Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Shareholders (including former shareholders or a person entitled to be registered as a shareholder) can apply for leave to bring a derivative action in the name of the company under Part 2F.1A of the Corporations Act. The court must grant leave to the applicant shareholder if the court is satisfied that:

- it is probable that the company will not itself bring the proceedings, or properly take responsibility for them or the steps in them;
- the applicant is acting in good faith;
- it is in the best interests of the company; and
- there is a serious question to be tried.

Where the proceedings involve a third party, there is a rebuttable presumption that granting leave will not be in the best interests of the company, if the company decided not to bring, defend or continue proceedings, and where the directors who made that decision acted in good faith and for a proper purpose, did not have a material personal interest in the decision, informed themselves about the subject matter of the decision to the extent they reasonably believed to be appropriate, and rationally believed that the decision was in the best interests of the company.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Courts have a wide discretion to make appropriate orders for relief at general law, including to make orders for:

- an interim injunction where there is a serious issue to be tried and the balance of convenience requires that an order be made; or
- a final injunction where an applicant has established a legal or equitable right and the court considers it just in exercising its discretion to make such an order.

Courts also have a broad statutory jurisdiction to grant an injunction to prevent the closing of an M&A transaction if it constitutes or would constitute: a contravention of the Corporations Act; an attempted contravention; aiding, abetting counselling or procuring, inducing or attempting to induce, being directly or indirectly knowingly concerned in or a party to a contravention; or conspiring with others to contravene the Corporations Act. A statutory injunction can be granted on an interim or final basis, with similar tests as under the common law. Supplementary orders can also be made.

Although courts have a wide discretion to grant appropriate relief, a court is unlikely to make an order preventing a transaction from closing or to modify or redraft the terms of a proposed transaction. However, in interpreting a contract that has been entered into, the court can:

- imply a term into a contract to give business efficacy to the contract;
- sever a term from the contract if the court considers the term to be unlawful or unenforceable; or
- 'rectify' a contract so that it reflects, at the time that an agreement has been entered into, the true intentions of the parties.

## Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

A defendant can seek early dismissal of a shareholder complaint by applying under the procedural rules or the inherent power of a court:

- for summary dismissal of a claim if it appears to the court: that the proceedings are frivolous or vexatious; that no reasonable cause of action is disclosed; or that the proceedings are an abuse of process; or
- for pleadings to be struck out in whole or part if the pleading: discloses no reasonable cause of action; has a tendency to cause prejudice, embarrassment or delay in the proceedings; or is otherwise an abuse of process.

Additional avenues for early dismissal of a shareholder complaint are available depending on the type of claim being brought, for example:

- if a shareholder commences a statutory derivative claim, a defendant might oppose the grant of leave to the applicant – while this is not an early dismissal per se, it will prevent the claim being brought; or
- if representative proceedings are commenced on behalf of a group of shareholders, the defendant can apply (or the court can of its own motion) order that proceedings no longer continue if it is satisfied that it is in the interests of justice to do so.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

It may be open to shareholders to bring claims against third-party advisers that assist in an M&A transaction, including where it can be established that the third-party advisers:

- owed a duty of care to the shareholder, were in breach of that duty, and this breach caused loss to the shareholder;
- made false or misleading representations to the shareholder; or
- engaged in misleading or deceptive conduct.

Shareholders may, additionally, be able to bring a statutory derivative claim on behalf of the company against a third-party adviser (see question 8).

The liability of professional advisers may be capped or limited by statute.

Additionally, the ability of a shareholder to bring a claim (or the liability in respect of any such claim) may be limited by transaction documents (including for example, a due diligence report), which may impose a cap on liability in respect of the relevant advisers, limit reliance on those documents by third parties, or require a party to rely solely on their own investigations/diligence.

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Yes, shareholders can bring derivative claims against counterparties to an M&A transaction (being claims on behalf of the company). Shareholders might also have personal rights against counterparties to M&A transactions in relation to, for example, misleading or deceptive conduct.

In addition, if shareholders bring a claim for unfair or oppressive conduct, the court has a wide discretion as to the appropriate relief to be granted and such relief may, depending on the nature of the conduct in question, directly affect a counterparty to an M&A transaction.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

Directors have a duty to comply with a company's constitutional documents, which may impose more rigorous standards than those in the Corporations Act.

A company's constitution cannot contract out of, or limit or dilute the statutory duties set out in the Corporations Act, however the constitution can limit the role that directors play in managing the entity, which in turn may impact upon the applicability of those duties to the relevant actions of the company. As mentioned in questions 21 and 24, the Corporations Act places limits on indemnification of directors and insurance premiums for certain liabilities.

### Statutory or regulatory limitations on claims

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

If members of a company ratify or approve conduct of directors and officers in connection with M&A transactions, the Corporations Act provides that an applicant is not precluded from bringing a statutory derivative claim under Part 2F.1A of the Corporations Act, although the court may take such ratification or approval into account in determining what order or judgment to make in proceedings brought or intervened in under that part. In doing this, the court must have regard to how well informed about the conduct the members were when they decided to ratify or approve the conduct, and whether the members who ratified or approved the conduct were acting for proper purposes.

If a claim is brought against directors and officers in connection with an M&A transaction for a breach of their duties, a number of defences are available under the Corporations Act. Depending on the claims being brought, these defences may include:

- where the director or officer: has made a 'business judgement' (that is, a decision to take or not take action in respect of a matter relevant to the business operations of a corporation, including in connection with an M&A transaction) in good faith and for a proper purpose; does not have a material interest in the subject matter of the judgement; informed themselves about the subject matter of the business judgement to the extent they reasonably believed to be appropriate; and rationally believe that the judgment is in the best interests of the company; or
- where the director or officer delegated a duty to another person, believed on reasonable grounds (in good faith and after making appropriate enquiries) that the person to whom they delegated was reliable and able in relation to that duty, and believed on reasonable grounds that the person to whom they delegated would exercise the relevant power in accordance with the duties set out in the Corporations Act and the constitution of the company.

The courts also have the power to wholly or partly relieve a director of liability for:

- a contravention of the Corporations Act; or
- negligence, default, breach of trust or breach of duty in their capacity as a director or officer of the company.

If the person has acted honestly and, having regard to the circumstances of the case, the person ought fairly to be excused. The court

can even grant such an order before proceedings are commenced (that is, if a director or officer has reason to apprehend that any claim will or might be made against them).

### Common law limitations on claims

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

At common law, a shareholder does not have standing to litigate in respect of wrongs characterised as done to the corporation rather than the shareholder individually, unless the member can bring proceedings pursuant to the statutory derivative action (see question 8) or the member has a personal right to bring proceedings (see question 6).

Further to question 14, which sets out the statutory consequences of ratification by shareholders, there are also common law rules that provide that ratification will be ineffective in certain circumstances, including if the ratification:

- relates to a breach of duties in relation to which the majority shareholders participated or the majority vote was made for an illegitimate purpose, such that the ratification would amount to a fraud on the minority shareholders;
- is in respect of breaches of statutory duties imposed upon directors; or
- would have the consequence of removing the personal right of a shareholder.

## STANDARD OF LIABILITY

### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

The Corporations Act prescribes a standard for directors and officers of a company. A board member is a director of the company. An executive will be an officer of the company (for the purposes of the Corporations Act) if they:

- make or participate in making decisions that affect the whole or a substantial part of the business of the company;
- have the capacity to significantly affect the company's financial standing; or
- the directors of the company are accustomed to acting in accordance with their instructions or wishes.

If a board member or executive is a director or officer of the company, the Corporations Act requires them to exercise their powers and discharge their duties (including in connection with an M&A transaction):

- with the degree of care and diligence that a reasonable person would exercise if they were a director or an officer in a corporation in the same circumstances of that corporation, and occupied the position and had the same responsibilities within the corporation as that director or officer;
- in good faith in the best interests of the corporation; and
- for a proper purpose.

A similar standard applies under common law.

Note that a director or officer who makes a 'business judgement' is taken to have exercised their powers and discharged their duties with the appropriate degree of care and diligence (that is, the first bullet point above) if they:

- made the judgment in good faith and for a proper purpose;

- do not have a material personal interest in the subject matter of the judgement;
- inform themselves about the subject matter of the judgement to the extent they reasonably believe to be appropriate; and
- rationally believe that the judgement is in the best interests of the corporation.

#### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

No.

#### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

#### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

The role of a director in an M&A transaction will be considered in the context of the directors duties enshrined in the Corporations Act (see question 16). The standard of care owed by a director or officer does not vary depending on whether he or she has a potential conflict of interest in connection with an M&A transaction, although a director or officer will not be able to rely on the 'business judgement rule' set out in the response to question 16.

Note also that, under section 191 of the Corporations Act, directors have a duty to notify other directors of a material personal interest in a matter that relates to the affairs of the company in circumstances where a conflict may arise, and failure to notify other directors is an offence of strict liability. The Constitution of the company may also provide for specific criteria in relation to conflicts of interest in connection with an M&A transactions or otherwise.

#### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

The standard of care owed by a director or officer does not vary, although a director or officer also must not use their position or information gained because of their position to gain an advantage for themselves or someone else or cause detriment to the company.

## INDEMNITIES

#### Legal restrictions on indemnities

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

The Corporations Act prohibits companies from exempting a liability to the company incurred as an officer of the company.

Companies will typically indemnify directors and officers for legal costs and liabilities by entering into a deed of access and indemnity with the director or officer, although the Corporations Act limits the indemnities that a company can provide.

#### Indemnities for liabilities other than legal costs

A company or a related body corporate must not indemnify a person against any of the following liabilities incurred as a director or officer of the company:

- a liability owed to the company or a related body corporate;
- a liability to pay a penalty or compensation order under the Corporations Act; or
- a liability that is owed to someone other than the company or a related body corporate and did not arise out of conduct in good faith.

#### Indemnities for legal costs

A company or a related body corporate must not indemnify a person against legal costs incurred in defending an action for a liability incurred as a director or officer of the company if the costs are incurred:

- in defending proceedings in which the person is found to have a liability for which they could not be indemnified, as outlined above;
- in defending criminal proceedings in which the person is found guilty;
- in defending proceedings brought by the Australian Securities and Investment Commission (ASIC) or a liquidator for a court order if the grounds for making the order are found by the court to have been established; or
- in connection with proceedings for relief to the person under the Corporations Act in which the court denies the relief.

#### Insurance

Access and indemnity deeds will often require a company to, or a company may otherwise, obtain directors' and officers' insurance to protect directors and officers from loss resulting from claims made against them in relation to the discharge of their duties (see further question 24). However, a body corporate is not permitted to pay a premium to insure an officer of the company against liability arising out of:

- conduct involving a wilful breach of duty in relation to the company; or
- conduct involving misuse of position or company information.

## M&A CLAUSES AND TERMS

#### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

A shareholder has no express personal right to challenge the terms of an M&A transaction document.

However, in principle, a shareholder may be able to challenge a particular term of an M&A transaction documents as follows:

- if those terms were oppressive to, unfairly prejudicial to or unfairly discriminatory against, a shareholder, or was contrary to the interests of the shareholders as a whole, then a shareholder may be able to challenge the term by bringing a claim for oppressive or unfair conduct;
- if a particular term is damaging to a company's interests, a shareholder may be able to argue that in agreeing to that term, a director or officer of the company has acted in breach of duty;
- a concerned shareholder may apply to the Takeovers Panel for a declaration of unacceptable circumstances on the basis that they are a person whose interests are affected by the relevant circumstances; or
- a shareholder may exercise indirect rights by calling a general meeting or proposing resolutions to remove directors.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

See questions 14 and 15.

### Insurance

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors' and officers' (D&O) insurance policies may cover losses or legal fees that a company or its directors and officers incur in defending a shareholder action.

Cover for directors and officers is referred to as 'Side A Cover' and typically includes defence costs, damages/compensation and interest or costs awarded against directors and officers. 'Side B Cover' provides reimbursement to the company in respect of indemnity provided to the directors and officers. Cover in respect of securities claims brought against the company by security holders is known as 'Side C Cover.'

D&O policies provide an important protection for directors and officers, particularly where a company cannot exempt liability or provide an indemnity in favour of the directors and officers (as to which see question 21). However, directors and officers may not be able to rely on the D&O insurance policy depending on the nature of the claim and the terms of the policy (in particular, any exclusion to the policy).

Note also that it is an offence for a company or a related company to pay a premium for a contract insuring a current or former director or officer of the company against a liability (other than for legal costs) arising out of:

- conduct involving a wilful breach of duty in relation to the company; or
- a breach of the duties not to improperly use their position or company information.

### Burden of proof

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The party bringing the claim has the burden of proof. The burden of proof does not shift during proceedings.

### Pre-litigation tools

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

A shareholder may investigate potential claims against board members or executives by:

- applying for an order for preliminary discovery, which may include discovery of documents from either a prospective defendant or from another person (if it appears to the court that the person may have or have had possession of a document that relates to any question in the proceeding), or preliminary discovery in relation to a prospective defendant's identity or whereabouts;
- applying for an order under section 247A of the Corporations Act to inspect the books of the company;
- requesting a copy of the company's constitution pursuant to section 139 of the Act; or
- reviewing publicly available information (including documents or information lodged with either the ASX or the ASIC).

The court will have jurisdiction to grant preliminary discovery if:

- it appears to the court that the shareholder may be entitled to make a claim against the board member or executive;
- the shareholder has made reasonable enquiries but it has been unable to obtain sufficient information to decide whether or not to commence proceedings;
- the board member or executive has documents in its possession that can assist the shareholder to determine whether or not to pursue the claim; and
- inspecting that document would assist in deciding whether or not to commence proceedings against the board member or executive.

### Forum

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Shareholder agreements and M&A transaction documents will typically contain a choice of jurisdiction clause or a choice of law clause that may dictate where any proceedings under those documents can be brought. These agreements may also contain an arbitration clause. Absent such provisions, the appropriate forum would ordinarily be the company's place of incorporation.

The nature of a claim being brought by shareholders may also dictate the appropriate forum. For example:

- a statutory claim under the Corporations Act will generally be brought in a court with jurisdiction to hear such statutory claims; and
- a claim in relation to a contract may also be subject to an exclusive jurisdiction clause or an arbitration clause.

### Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

#### Proceedings

Courts can expedite proceedings pursuant to general case management powers, however it is a matter of judicial discretion (and often subject to court availability). Court rules also permit applications for expedited hearings before certain courts of appeal.

#### Discovery

While the procedure for discovery differs between federal and state courts in Australia, generally, the Court will order discovery after the close of pleadings (for the issues to be defined) but before the parties have exchanged evidence. Courts can also expedite discovery pursuant to general case management powers. (Practically, if the scope of documents sought in discovery can be narrowed between the parties, the discovery process is likely to be quicker.)

Common discovery issues that arise in Australia include:

- claims of legal profession privilege – parties are not obliged to disclose documents that are legally privileged;
- whether a document is within the control of a party – it is not discoverable if it not within their control; and
- disputes regarding the scope of discovery – discovery is not a fishing expedition, and orders for discovery may be opposed if they are too broad or the documents are not relevant to a fact in issue.

## DAMAGES AND SETTLEMENTS

### Damages

#### 29 | How are damages calculated in M&A litigation in your jurisdiction?

Under Australian law, damages are compensatory in nature and not punitive. The precise calculation of damages will depend on, among other things, the nature of the claim, the alleged wrongdoing, and the particular remedy sought.

The court has broad discretion in relation to the remedies it may award for a statutory oppression claim or derivative action under the Corporations Act, including orders that a company be wound up, regulating the conduct of the company's affairs in the future, and for the purchase of shares. Compensation can also be sought for the company and shareholders in respect of loss suffered.

Under the Corporations Act, a court may order a person to compensate a company where that person has contravened certain provisions of the Act in relation to the company (including breaching duties as directors or continuous disclosure obligations), and damage resulted from that contravention. In determining the amount of compensation to be awarded, profits resulting from the contravention that are incurred by a person will be taken into account.

### Settlements

#### 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

If shareholder M&A litigation is commenced as a representative proceeding (ie, class action), court approval is required before such proceedings are settled or discontinued. If the court does give its approval, it may make such orders as are just with respect to the distribution of any money under the settlement. The court will consider, among other things, whether the proposed settlement is a fair and reasonable compromise of the claims of the group members.

## THIRD PARTIES

### Third parties preventing transactions

#### 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

It is unlikely that third parties will have standing to bring litigation to break up or stop M&A transactions that have been agreed prior to closing, unless they can argue that they are a person whose interests are affected by the relevant circumstances and seek a declaration of unacceptable circumstances from the Takeovers Panel.

Other tactics, such as acquiring a shareholding in the company, or intervening on the basis that the board is not acting in accordance with their duties, may be used in an effort to prevent transactions from proceeding.

Additionally, where Australian Competition and Consumer Commission approval is required for the transaction to proceed, it will generally seek submissions from interested third parties, and during such submissions and subsequent consultation, third parties may raise objections to a transaction proceeding. Where a third party is dissatisfied with a determination, it may apply under the Competition and Consumer Act 2010 (Cth) to the Australian Competition Tribunal for a review of a determination. Where the Australian Competition Tribunal is satisfied that this third party has a 'sufficient interest' in the determination, it will review it.



#### Scott Harris

scott.harris@hoganlovells.com

#### Christopher Moses

christopher.moses@hoganlovells.com

#### Gabriella Plummer

gabriella.plummer@hoganlovells.com

Level 17, 20 Martin Place  
Sydney NSW 2000  
Australia  
Tel: +61 2 9093 3500  
Fax: +61 2 9221 9541  
www.hoganlovells.com

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Third parties cannot use litigation to force corporations to enter into M&A transactions; however it is open to third parties to consider all commercial options (which may include the use of litigation if they have any rights to enforce or protect or standing to bring proceedings, or an application to the Takeovers Panel for a declaration of unacceptable circumstances if their interests are affected by the relevant circumstances) to pressure a party to enter into M&A transactions.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

The duties of directors are set out in the response to question 2.

If a corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction by way of a bidder's statement, the directors will need to consider, among other things:

- engaging and briefing advisers or independent experts (for example, to value the company);
- advising shareholders;
- to the extent that the corporation is listed on a stock exchange or the transaction is regulated by the Corporations Act, ensuring that applicable rules and statutory provisions are complied with; and
- if required, applying to the Takeovers Panel (for example, if there are issues in relation to the bidder's statement).

**COUNTERPARTIES' CLAIMS****Common types of claim**

34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

Litigation between counterparties to an M&A transaction most commonly involve the following types of claims:

- conditions precedent not being met before closing;
- disputes regarding due diligence and disclosure documents;
- breaches of representations or warranties;
- indemnity claims;
- post-completion adjustments (such as working capital and net debt adjustments);
- restraint of trade clauses; and
- misleading and deceptive conduct or similar claims (although M&A transaction documents typically seek to limit the ability of parties from making statutory or contract claims, to the extent possible).

**Differences from litigation brought by shareholders**

35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

The types of claims brought between parties to an M&A transaction (as set out in question 34) differ significantly from the types of claims brought by shareholders (as set out in the responses to questions 1 and 2). The remedies sought often differ between these claims, although the precise remedies will, of course, depend on the nature of the claim.

# Austria

Valerie Hohenberg and Markus Taufner  
Wolf Theiss Rechtsanwälte GmbH & Co KG

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The main claims shareholders can assert against corporations in relation to M&A transactions are the following:

- claims for challenging shareholder resolutions approving an M&A transaction, inter alia, based on the violation of fiduciary duties or a breach of the corporation's articles of association;
- claims for an appropriate cash compensation related to a merger, spin-off, legal transformation or squeeze-out; and
- tort claims based on the violation of statutory law aiming at the protection of shareholders.

The main shareholder claims against members of the management board or supervisory board are the following:

- derivate claims on behalf of a limited liability company based on the violation of the board members' duty of due care (*actio pro socio*);
- claims based on the violation of the board members' duty of loyalty towards the shareholders;
- claims related to the violation of information or reporting duties in the course of a merger, spin-off, legal transformation, squeeze-out or takeover;
- claims related to insider dealing and market manipulation;
- claims related to the violation of the 'non-frustration rule' under the Austrian Takeover Act; and
- other tort claims based on the violation of statutory laws aiming at the protection of shareholders.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

In general, it is up to the claimant to allege and provide proof of all facts supporting the claim. Only in case a shareholder brings (i) a claim related to a damage suffered in the course of a merger, spin-off or transformation or (ii) a derivate (damage) claim on behalf of the company against a director, does the burden of proof shift to some extent. The claimant is required to make a showing of the damage suffered and provide sufficient facts that indicate that such damage was caused by a breach of the director's duties. If this is established, the director bears the burden of rebutting this proof by evidencing that he or she fulfilled his or her duty. This shift in the burden of proof is, therefore, to the shareholder's advantage.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

The claims differ insofar as the company's or the directors' obligations differ depending on whether the company is public or private. For example, fiduciary duties of managing directors are deemed to be much stronger in privately held companies, whereas certain information or disclosure obligation duties only apply to publicly traded companies. A further good example is the decision of the Austrian Supreme Court in which it held that a shareholder resolution regarding the merger of a listed company with a privately held company, aiming at a 'cold de-listing', was vexatious and therefore void, because the interests of minority shareholders, such as the interest of publicly trading their shares on the stock market, was not sufficiently taken into account.

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

The claims differ insofar as the company's or the directors' obligations differ depending on the form of the transaction. Furthermore, Austrian law provides for certain proceedings with the purpose of securing a fair cash compensation for shareholders exiting the company in the course of a merger, spin-off, transformation or squeeze-out. These proceedings offer major procedural advantages to minority shareholders, including their representation by a court-appointed 'joint representative' and the allocation of procedural costs to the company (or the majority shareholder).

### Negotiated or hostile transaction

- 5 Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

Pursuant to the Austrian Takeover Act, the management and supervisory boards of the target company shall refrain from implementing any measures that may lead to the frustration of the offer, without the prior approval of the general meeting. This obligation starts when the target becomes aware of the bidder's intention to make an offer and ends when the offer is implemented. However, the target company's board is explicitly entitled to search for and negotiate with other potential bidders ('white knight'). Furthermore, the implementation of board decisions passed prior to that point in time requires the general meeting's approval if such measures may lead to the frustration of the offer and fall outside the scope of the company's ordinary course of business.

### Party suffering loss

- 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

The claims differ insofar as the loss suffered by the corporation may be pursued by a (minority) shareholder on behalf of the company (see questions 8 and 14).

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

- 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Class or collective actions are not permitted in Austria. However, proceedings with the purpose of securing a fair cash compensation paid to shareholders in the course of certain transactions (see question 4) can be initiated upon the application of only one shareholder, whereas the court ruling has effect *erga omnes*.

### Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

A shareholder of a limited liability company can bring a claim for a loss suffered by the corporation against other shareholders, managing directors or members of the supervisory board if such shareholder holds at least 10 per cent of the share capital or shares in a nominal amount of €700,000 or a smaller amount if specified in the articles of association (*actio pro socio*).

Asserting such claim on behalf of the company is only possible if asserting the claim by the company was already refused by shareholder resolution or the respective motion in a general meeting was not put to vote, even though filed in due time. The claim must be filed within one year of the date on which the resolution was adopted or prevented from being adopted. For as long as the proceedings are pending, the claimants shall not sell their shares without the approval of the company. Upon application of the defendant, the claimant can be required to provide security to the defendant as determined at the free discretion of the court. If it turns out that the action was unfounded, and if the claimant acted with malicious intent or gross negligence, the claimant shall be liable to indemnify the defendant.

A different regime applies to Austrian stock corporations. The corporation's claim against shareholders, members of the management or supervisory boards must be asserted if the general meeting passes a resolution to this effect by a simple majority of votes cast. The same shall apply if such assertion is requested by a minority holding at least 10 per cent of the share capital and the claims asserted by it are not manifestly unfounded. If facts have been established in an audit report that give rise to such claims, the threshold for the required minority is reduced to 5 per cent of the share capital. The general meeting may appoint special representatives to represent the corporation in such proceedings. If the minority demands the assertion of the claim and if the claim is not manifestly unfounded, the court shall appoint a person designated by the general meeting as representative of the corporation, unless an important reason to the contrary is given.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

To ensure that at the end of the civil procedure, the relief sought is still possible, provisional measures in the form of preliminary injunctions can be used. The party seeking such injunction bears especially the burden of proof that reasons exist to assume that the aim of the civil proceedings is put in jeopardy. In general, injunctions cannot be issued if they lead to irreversible results. Inter alia, preliminary injunctions can be used to secure the present legal situation provided that the party seeking such injunction would otherwise suffer irreparable damages. In M&A litigation, preliminary injunctions could be used to block the closing of a transaction (eg, in case of a violation of a shareholder agreement). However, courts do not have the power to modify deal terms in such proceedings.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

The concept of 'early dismissal' does not exist in Austria. However, a claim may be rejected due to lack of jurisdiction or other procedural grounds.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

In M&A transactions, auditors are engaged to provide opinions (eg, on whether the exchange ratio of shares is appropriate or whether compensation payments offered to squeezed-out shareholders are fair).

The auditor is liable for any errors or omissions in the audit report; not only towards the involved company or companies, but also towards their shareholders. Each shareholder that suffered a loss due to an incorrect report is entitled to claim compensation. In case of slight or gross negligence, statutory law stipulates certain maximum amounts of compensation, depending on the size of the company. The court decision has effect only *inter partes* (ie, between the shareholder and the auditor).

However, in practice this path is not pursued, because shareholders are also entitled to initiate non-adversary civil proceedings with the purpose of securing an appropriate exchange ratio or fair compensation, which have major procedural advantages (see question 4).

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Such claims can be brought based on tort. In addition, the Austrian Act on Stock Corporations provides that any person who, to obtain special benefits for himself or for any other person, intentionally instructed a member of the management or supervisory board to act to the detriment of the company or its shareholders by using their influence on the company, shall be obliged to compensate the damages caused thereby. In addition, the members of the management and supervisory board shall be jointly and severally liable if they have acted in breach of their duties.



## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

In principle, Austrian law does not permit a limitation or reduction of a director's liability in the articles of associations or any other constituting documents. However, distributing responsibilities among specific board members can lead to a weakening of the responsibility for matters that are not part of the individually assigned duties and responsibilities. The primary responsibility lies with the responsible member, but all board members must fulfil a monitoring obligation. In any case, core competences are necessarily the responsibility of the entire management board.

### Statutory or regulatory limitations on claims

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Austrian statutory law provides for a 'business judgement rule', which only applies to claims asserted by the company against its directors. This claim can be raised by a shareholder only under the circumstances outlined in question 8.

In 2015, Austria introduced the Criminal Law Amendment Act, which implemented the 'business judgement rule' into statutory law. Before that, the 'business judgement rule' was already a principle in Austrian case law that allowed for an exemption of liability for management decisions. Pursuant to the respective rules in the Act on Limited Liability Companies and the Act on Stock Corporations, a director acts in accordance with the due diligence of a prudent businessperson if he or she is not guided by extraneous interests and, based on adequate information, can assume to be acting for the benefit of the company. This rule applies to members of both the management and supervisory board.

### Common law limitations on claims

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

No. For the 'business judgement' rule that was implemented by statutory law, see question 14.

## STANDARD OF LIABILITY

### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

If a derivative claim is brought by a shareholder on behalf of the company, the 'business judgement rule' applies (see question 14). Austrian law applies an objective standard when testing a director's liability, which is determined by the nature and size of the company's business and assessed from an ex ante perspective.

In case of tortious acts committed towards shareholders, the standard is determined by the respective statutory law that is violated by the board member and which varies from slight or gross negligence to intention. A possible legal basis for tort claims against board

members are criminal laws, inter alia, aiming at the protection of shareholders (eg, offence of dishonesty).

### Type of transaction

- 17 | Does the standard vary depending on the type of transaction at issue?

In case of tortious acts committed towards shareholders, the standard is determined by the respective statutory law that is violated by the board member, which varies from slight or gross negligence to intention.

### Type of consideration

- 18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

### Potential conflicts of interest

- 19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

The standard mentioned in question 14 varies insofar, as the business judgement rule requires that a decision is made free from any self-interest. Therefore, this rule does not apply in this case.

### Controlling shareholders

- 20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

The standard does not vary. However, in case a consideration is paid to a shareholder that is not shared ratably with all shareholders, two separate issues may arise. First, if the consideration does not comply with the Austrian capital maintenance rules, the transaction could be null and void. The concept of capital maintenance is based on the principle that the entire assets of the company should be protected on behalf of the company's creditors. To this end, a business transaction that provides for any value transfer to a shareholder or a shareholder's affiliate must be concluded at arm's-length terms. Second, if the consideration should favour the controlling shareholder the principle of equal treatment of all shareholders could be violated. In both cases, the directors could be held liable. Furthermore, the agreement underlying a merger or spin-off needs to indicate whether any 'special benefits' are granted to a company involved in such transaction (eg a controlling shareholder). The respective agreement is legally invalid otherwise.

## INDEMNITIES

### Legal restrictions on indemnities

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

In general, Austrian law does not prohibit a company from indemnifying or advancing the legal fees of its directors or officers named as defendants in civil proceedings. However, the indemnification for legal fees has the character of a payment and is considered as remuneration. Therefore, the indemnification for legal fees of a managing director of a joint stock company must be approved by the supervisory board and in case of a limited liability company by the general meeting. Without

such approval, the payment of the legal fees might be considered as a breach of fiduciary duty.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

In principle, shareholders can only challenge clauses or terms in transaction documents to which they are party. A means for shareholders to (indirectly) challenge such documents is to file a claim for challenging the shareholder resolution approving such transaction.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

For managing directors of a limited liability company, a shareholder resolution is binding and needs to be complied with unless it violates the law. In contrast, managing directors of a stock corporation are independent from and not bound by a shareholder resolution. A shareholder resolution approving a merger, spin-off, transformation or the sale of a company's entire assets is mandatorily required. However, in case of a merger, spin-off or transformation a shareholder resolution cannot relieve the transferring company's management or supervisory board members from any liability towards their company (see, for example, sec 227 para 1 Austrian Act on Stock Corporations). Furthermore, the claim for challenging a shareholder resolution by which an M&A transaction was approved is an often-used means by (minority) shareholders.

### Insurance

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Following the international trend, directors' and officers' insurances have also found further distribution in Austria in recent years and, in general, companies have insurances for members of the management and supervisory board in place. It does not matter whether the manager is being held liable by his or her company for damages or by a third party, such as a shareholder or a company's creditor. Possible claims of a shareholder arising from M&A transactions may, therefore, be covered by such an insurance. In recent years, insurance companies have also been involved at an earlier stage of the dispute in order to find an early amicable solution.

### Burden of proof

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

In general, it is incumbent upon the claimant to establish the existence of all facts entitling him or her to the judgement sought. Only in certain cases does the burden of proof shift as outlined in question 2.

### Pre-litigation tools

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Austrian statutory law provides for certain cases, in which internal investigations shall be performed that can be further used as pre-litigation tools by shareholders. For instance, a shareholder minority holding at least 10 per cent of the company's share capital can file a court application for the appointment of a special investigator, if a prior shareholder resolution aiming at conducting such investigations could not be passed in a prior general meeting with the required majority of votes. While such investigation is limited to the audit of the latest financial statements of a limited liability company, every action in the course of the incorporation or every action performed by the managing directors within the past two years can be subject to such investigations of a stock corporation. Furthermore, shareholders of a limited liability company have an extensive information right towards the company (including the right to inspect the corporate books and records), which can be judicially enforced.

At the general meeting of a stock corporation, shareholders are entitled to be provided with information regarding the company's affairs to the extent necessary for the proper assessment of an item on the agenda. The duty to provide information also extends to the company's legal and business relationships with an affiliated company. In case the consolidated financial statements are presented at the general meeting of a parent company, the duty to provide information also extends to the situation of the entire group and the companies included in the consolidated financial statements.

### Forum

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

As to jurisdiction, it needs to be distinguished against whom the claim is brought. If it is brought against the company (eg, for challenging shareholder resolutions), both Austrian law and the Brussels Recast Regulation provide for the exclusive jurisdiction of the court (of the member state), where the company has its registered seat. Furthermore, Austrian law provides for an additional elective place of jurisdiction for disputes resulting from corporate relationships (eg shareholder disputes) at the seat of the company. Apart from that, any other claim related to M&A follows the defendant's domicile rule. The parties may also conclude a choice-of-court agreement or agree on an arbitration clause (eg, in a share purchase agreement or shareholder agreement).

### Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Discovery proceedings do not exist under Austrian law. For interim injunctions, see question 9.

## DAMAGES AND SETTLEMENTS

### Damages

29 | How are damages calculated in M&A litigation in your jurisdiction?

Damages incurred in M&A transactions are 'financial damages', which are divided into 'positive damages' and 'lost profits' pursuant to Austrian law. Whereas the former term refers to a loss or a devaluation of an

already existing right or asset, the latter is defined as the failed or missed opportunity to increase future profits. In court proceedings, such damages are calculated by court-appointed accounting experts. The parties have the opportunity to question the expert, inter alia, by oral examination with the support of a private expert.

In M&A litigation, the main focus of the expert opinion is usually the valuation of a company. In this context, the Austrian Chamber of Professional Accountants and Tax Advisers has issued a general expert opinion, which is also used by court experts and often referred to in M&A transaction documents that are subject to Austrian law. This general expert opinion uses income-based and discounted cash-flow methodologies for the evaluation of companies.

### Settlements

**30** | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

In general, there are no special legal issues with respect to settling shareholder M&A litigation. However, especially in proceedings aiming at challenging shareholder resolutions it can be seen in practice that minority shareholders often bring a claim with the sole aim of pressuring the company into concluding a settlement agreement. If a claim for challenging a shareholder resolution is pending, the closing of the transaction may be delayed. The reason for this delay is that certain transactions (such as a merger) require the registration with the Austrian companies register to be legally effective. As the registration is based on the shareholder resolution, the cancellation proceedings can prevent the register court from registering the merger, which, in turn, delays the effectiveness of the transaction.

As to claims brought by a stock corporation against its board members, a settlement requires that:

- a period of five years has elapsed since the claim originated;
- the general meeting approves the settlement; and
- a shareholder minority representing 20 per cent of the company's share capital does not object to such settlement.

## THIRD PARTIES

### Third parties preventing transactions

**31** | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

In principle, Austrian law does not allow third parties to bring a claim to break up or stop M&A transactions. However, a (preventive) cease-and-desist claim based on Austrian competition law could be considered to prevent unfair business practices which would be realised by the closing of an M&A transaction. Apart from competition law, third parties may also be entitled to prevent an M&A transaction closing on contractual bases, such as provisions in shareholder agreements. Furthermore, activists could acquire a share in a company to be entitled to bring litigation in their capacity as (minority) shareholders (eg, by challenging shareholder resolutions approving an M&A transaction), which could prevent the transaction from closing.

### Third parties supporting transactions

**32** | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

**33** | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Pursuant to the Austrian Takeover Act, management and supervisory boards have to issue statements regarding the offer of a takeover immediately after the offer has been published. In general, the boards must be objective and impartial. In particular, they must not perform any actions or measures depriving shareholders of the opportunity to form their own informed decision on the offer. From the moment the target becomes aware of the bidder's intention to make an offer until the implementation of that offer, the boards require the approval of the general meeting for all measures that could potentially frustrate the outcome of the offer.

## COUNTERPARTIES' CLAIMS

### Common types of claim

**34** | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

A general distinction is drawn between 'pre-merger' (or 'pre-closing') and 'post-merger' litigation, dependent on whether the dispute arises before or after closing.

Pre-merger disputes may include, for example, claims relating to the breach of pre-contractual disclosure or information obligations (*culpa in contrahendo*), the breach of non-disclosure agreements, disputes regarding allegedly binding agreements (eg, letter of intent, memorandum of understanding) or deviations therefrom in the process of negotiating the transaction, disputes regarding the interpretation of conditions precedent or whether a material adverse change occurred, the breach of certain obligations or undertakings in the phase between signing and closing as well as claims for payment of the purchase price or the transfer of shares or assets.

Post-merger disputes between the parties to a share or asset purchase agreement are far more common in Austria. Claims raised post-merger can still be based on the breach of pre-contractual obligations, but also on the breach of contractual obligations or representations and warranties. Post-merger litigation in Austria often relates to financial aspects, such as purchase price adjustments or earn-out clauses.

### Differences from litigation brought by shareholders

**35** | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between the parties to an M&A transaction differs insofar as the contracts often provide for alternative dispute resolution mechanisms and/or an arbitration clause. Especially in a global context, the recognition and enforcement of arbitral awards under the New York Convention is often seen as favourable by the parties. Furthermore, M&A contracts often provide for limitation periods deviating from statutory law or certain thresholds to bring a claim against the counterparty.

**UPDATE AND TRENDS****Key developments**

36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

With the reforms of the Austrian Stock Exchange Act and the Austrian Takeover Act, the delisting from the Vienna Stock Exchange has been facilitated. It is now, inter alia, based on a resolution of the public company's general meeting. In addition, a 'delisting offer' has been newly introduced in Austria. These reforms may pave the way for a potential increase in delistings and subsequent squeeze-outs of minority shareholders. Thereby, non-adversary civil proceedings with the purpose of securing a fair share price for squeezed-out shareholders will potentially gain in importance in the future.

Furthermore, the revised EU Shareholder Rights Directive, to be transposed into statutory law in Austria (and other EU member states) by 10 June 2019 that, inter alia, aims at shareholder empowerment and engagement, and will potentially lead to more friction and disputes between (institutional) shareholders, public companies and their boards.

**WOLF THEISS**

---

Valerie Hohenberg

valerie.hohenberg@wolftheiss.com

Markus Taufner

markus.taufner@wolftheiss.com

---

Schubertring 6

1010 Vienna

Austria

Tel: +43 1 51510

Fax: +43 1 51510 25

www.wolftheiss.com

# China

Dong Chungang, Hu Ke and Ge Xiangwen

Jingtian & Gongcheng

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

Under the PRC law, shareholders' potential claims against a corporation and its officer or director in relation to M&A transactions can generally be categorised as follows.

- A claim seeking an order that the corporation shall provide with the corporate documents for inspection in relation to the M&A transaction, such as a resolution passed by the board of directors (inspection claims). However, the scope of the above-mentioned corporate documents is strictly limited to that provided under articles 33 and 97 of the PRC Company Law (amended in 2018).
- A claim seeking an order that the corporation shall purchase the shares held by the dissenting shareholders who vote against the M&A transaction in the shareholders' meeting as provided by paragraph 2, article 74 of the PRC Company Law (repurchase claims). It is worth noting that repurchase claims are only applicable to shareholders of limited liability companies.
- A claim seeking a declaration that the resolution passed by a shareholders' meeting or board of directors in relation to the M&A transaction is null and void, voidable or ineffective, according to article 22 of the PRC Company Law (claims for invalidation of resolution).
- A claim seeking a declaration that the contract for the M&A transaction is null and void under the circumstances provided in article 52 of the PRC Contract Law, including malicious collusion to damage the interests of a third party (including corporations and shareholders that are not a party to the transaction) and violation of mandatory provisions of law (claims for invalidation of the transaction contract).
- A claim seeking damages against the officers or directors for their breach of fiduciary duty or duty of diligence under the PRC Company Law and the articles of association of the company (damage claims).

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

For inspection claims, the shareholder needs to show:

- that he or she is a shareholder of the company at the time of filing the lawsuit; and
- that his or her request for inspection of related corporate documents has been explicitly or implicitly rejected by the company.

For repurchase claims, the shareholder of limited liability companies needs to establish:

- that he or she voted against the M&A transaction in the general shareholders' meeting; and
- that there is no share(s) acquisition agreement entered into between the dissenting shareholder (plaintiff) and the company within 90 days since the pass of the resolution.

For claims for invalidation of resolution, the shareholder needs to prove:

- that he or she is a shareholder of the company at the time of filing the lawsuit; and
- that the concerned resolution violates provisions of laws or administrative regulation as provided by article 22 of the PRC Company Law.

For direct damage claims, the shareholder needs to show:

- that the director, supervisor or senior officer violated provisions of laws, administrative regulations, or the articles of association in the course of performing his or her duties; and
- that the shareholder's interests were damaged thereby.

For derivative damage claims, the shareholder needs to prove:

- that he or she has being a shareholder of the limited liability company or the joint stock company holding 1 per cent or more of stocks of the company for 180 consecutive days or more;
- that he or she has fulfilled the internal request requirement as provided by article 151 of the PRC Company Law;
- that the director, supervisor or senior officer violated the provisions of laws, administrative regulations or articles of association in the course of performing his or her duties; and
- that the company has suffered losses thereby.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes. Repurchase claims can only be brought by shareholders of limited liability companies. Additionally, similar to many countries, publicly traded companies (the 'listed companies') are confronted with more regulations than privately held companies. Specifically, shareholders of listed companies may file lawsuits against the obligor for information disclosure who made a false statement in violation of the law and thus causes losses to the investors as provided by Several Provisions of the Supreme People's Court on Trial of Cases of Civil Compensation Arising from False Statement in Securities Market.

### Form of transaction

#### 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Yes. As tender offers are only defined and applied in the context of the PRC Securities Law and repurchase claims may only be brought by shareholders of limited liability companies, shareholders cannot raise repurchase claims against tender offers.

For forms of transaction of merger, asset sale and share purchase, shareholders can raise all the claims listed under question 1.

### Negotiated or hostile transaction

#### 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No. As to types of claims, there is no substantive difference in claims in different types of transactions.

### Party suffering loss

#### 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes. Where the loss is suffered by the shareholder, the shareholder may raise damage claims in a direct litigation against the director or senior officer in accordance with article 20 and 152 of the PRC Company Law. Usually, the loss suffered by the shareholder is associated with shareholder's right over management of the corporation, such as the voting rights, inspection rights, etc.

Where the loss is suffered by the company, the shareholder, after completing the preconditioned procedures provided by article 151 of the PRC Company Law, may raise damage claims in a derivative litigation against the senior officer or director.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

#### 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Yes. There is no American-style class action in the PRC. However, there is joint action in the PRC that if the object of the action is of the same category and there are many persons on one side, and upon institution of the action the number of persons is not determined yet, the people's court may issue a public notice stating the particulars of the case and the claims and requesting that claimants register with the people's court within a certain period of time. No specific requirement is provided by the Company Law, shareholders who have registered with the people's court may elect a representative to engage in litigation; if no such representative can be elected, the people's court may discuss selecting the representative with the shareholders.

In particular, the investor protection agency, being the representative of the group of investors, is encouraged to take part in the joint action.

### Derivative litigation

#### 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes. Shareholders can bring derivative litigation on behalf of the corporation (but in the shareholder's own name) where the company suffered a loss caused by the M&A transaction.

Article 151 of the PRC Company Law provides for the preconditioned requirements or procedures for derivative litigations as follows.

- The plaintiff needs to be:
  - any shareholder or group of shareholders of the limited liability company; or
  - any shareholder or group of shareholders of the joint stock company who holds 1 per cent or more of the stocks for 180 consecutive days or more.
- The plaintiff needs to request, in writing, the supervisor or the board of supervisors to initiate a legal action for the suffered losses.
- The supervisor or the board of supervisors refuse to initiate a lawsuit or fails to initiate a legal action within 30 days of receiving the request; or in the event of any urgent situation in which failing to initiate a lawsuit forthwith will cause irreparable damages to the interests of the company.

The benefit of winning the lawsuit shall be allocated to the company.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

#### 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

The core objective of interim relief is to secure the enforcement of judgment and to prevent plaintiffs from suffering irreparable loss. Although injunctions are rarely and very cautiously awarded by the PRC Court in commercial litigations (including M&A litigation), the court may, upon application of the plaintiff (the court may, from time to time, request the plaintiff to provide warranties for the application), issue a property preservation order against the defendant, as an interim relief, to freeze the trading shares or stocks and essentially enjoin the transaction.

The court has no discretion to modify deal terms during the litigation, but could confirm, at the request of both parties, an amendment to deal terms and issue a mediation statement accordingly.

### Early dismissal of shareholder complaint

#### 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Yes. Defendants in derivative litigations may apply to the court, without reviewing the merits of the case, for a summary dismissal based on the following grounds:

- the shareholder fails to meet the preconditioned requirements on quantum and duration of the shareholding; and
- the shareholder failed to fulfil the preconditioned procedures of derivative litigations as mentioned in question 8.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

#### 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Yes. Generally, shareholders can bring claims against third parties (including but not limited to third-party advisers) for the loss of companies caused by them in M&A transactions, according to paragraph 3, article 151 of the PRC Company Law.

Additionally, shareholders of listed companies can file a lawsuit against third-party advisers including securities underwriters, sponsors and professional agencies (such as accounting firms, law firms and

asset appraisal agencies) in accordance with the Several Provisions of the Supreme People's Court on Trial of Cases of Civil Compensation Arising from False Statement in Securities Market.

### Claims against counterparties

12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Yes. According to paragraph 3, article 151 of the PRC Company Law, if the loss suffered by the company was caused by aiding and abetting of the counterparties, shareholders of a company that is a party to an M&A transaction may raise damage claims in derivative litigations against any third party (including the counterparties to the transaction).

Moreover, shareholders can bring claims for invalidation of transaction contract in direct litigations to nullify the contract under article 52 of the PRC Contract Law.

### LIMITATIONS ON CLAIMS

#### Limitations of liability in corporation's constitution documents

13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

As an important reference, articles of association of companies, together with laws and administrative regulations are critical in deciding whether the executive shall be held liable in relation to the M&A transaction.

Apart from the required items provided by article 31 and 81 of the PRC Company Law, the power to decide the content of articles of association (including setting up limitations on executives' liabilities) still vests in the shareholders' meeting. Nevertheless, the content of articles of association cannot go against the compulsory provisions of laws and administrative regulations.

Meanwhile, according to paragraph 3, article 112 of the PRC Company Law, directors of joint stock companies, whose dissenting opinions to resolutions of M&A transactions have been recorded under the minutes for meetings of board of directors, can be exempted from being held liable for the companies' loss caused by M&A transactions.

#### Statutory or regulatory limitations on claims

14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Yes. Statutory provisions limiting shareholders' ability to bring claims are mainly embodied in the preconditioned requirements or procedures set out by article 151 of the PRC Company Law, which are further detailed in question 8.

#### Common law limitations on claims

15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Yes. Although the PRC is a civil law jurisdiction and most common law rules are inapplicable in the PRC, there are rules developed by the judiciary. For instance, the business judgement rule is usually adopted and applied in dealing with claims for invalidation of resolutions. In a guiding case published by the Supreme People's Court, *Li Jianjun v Shanghai Jiadongli Environmental Technology Co, Ltd*, the court held that internal legal relationships within companies shall be governed by

autonomous mechanisms therein and that judiciary will principally not intervene in domestic affairs of companies.

### STANDARD OF LIABILITY

#### General standard

16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Under the PRC laws, executives will be held liable to companies, instead of shareholders, for their breach of fiduciary and diligent duties.

Specifically, executives shall be held liable for their breach of fiduciary and diligent duties where executives:

- misappropriate company funds;
- divert company funds into an account held in their own names or in the name of any other individual;
- unlawfully loan company funds to others, or provide guaranty to any other person by using companies' property, without approval of shareholders' meeting or board of directors;
- unlawfully enter into agreements or carry out transactions with other companies, without approval of the shareholders' meeting or board of directors;
- seek business opportunities originally belong to the company for himself or for any other person by taking advantage of his or her position, or operate on his or her own or other's behalf any business similar in nature to that of the company, without approval of the shareholders' meeting or board of directors;
- accept and seize any commission on any transaction to which the company is a party, or
- unlawfully disclose confidential information of the company.

#### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

No. The standard in determining executives' liabilities is the same for different types of transactions.

#### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No. The type of consideration being paid to the seller's shareholders will not affect the standard for determining whether executives may be held liable in connection with M&A transactions.

#### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

No. The fact that directors or officers have potential conflicts of interest or affiliated relationship to an M&A transaction will not change the standard.

#### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

No. The standard remains unchanged under these circumstances.

## INDEMNITIES

### Legal restrictions on indemnities

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

No. There is no legal restriction as to a company's ability to pay legal fees for its officers or directors listed as defendants in litigations.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

- 22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

Yes, but only limited to certain circumstances. Admittedly, shareholders are not a contracting party to the transaction contract and therefore lack direct standing to challenge the contract. However, if the clauses or terms under the contract are null and void according to article 52 the PRC Contract Law, the shareholder is entitled to raise claims for invalidation of the contract.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

- 23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

Normally, a shareholder vote will not influence M&A litigation. However, the shareholder will be estopped from denying the vote in subsequent litigations, if he or she had been fully informed before voting.

### Insurance

- 24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors' and officers' insurance (D&O insurance) is not commonly adopted in the PRC. According to the data provided by some commentators, the percentage of listed companies purchasing D&O insurance is less than 5 per cent, although provisions in relation to D&O insurance had been incorporated into the Code of Corporate Governance for Listed Companies in 2002.

### Burden of proof

- 25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

Basically, it is on the shareholders who instituted the litigation to bear the burden of proof in the proceeding to support his or her claims.

Where companies or executives are proved to be in possession of evidence against themselves but refuse to provide it without good reason, the court may infer that the shareholder's claim is sound.

Where no specific statutory provision exists and it is not possible to define which party is responsible for producing evidence on the basis of these provisions or any other judicial interpretation, the court may allocate the burden of proof according to the principles of fairness, honesty and credibility and by considering factors such as the parties' overall ability to produce evidence.

### Pre-litigation tools

- 26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Yes. Shareholders are entitled to inspect specific corporate books and records as provided by article 33 and 97 of the PRC Company Law. Where shareholders' inspection rights were infringed by companies, shareholders can raise inspection claims against companies.

Moreover, according to article 101 of the PRC Civil Procedure Law, in the event of emergency where it is likely that corporate books and records may be destroyed, lost or become difficult to obtain later on, shareholders may, prior to instituting a lawsuit, apply to the court to preserve the books and records.

### Forum

- 27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Yes. According to the PRC Civil Procedure Law and related judicial interpretations, most of the cases in relation to M&A transactions shall be under the jurisdiction of the people's court at the domicile of the company. The articles of association or by-law of a company may provide the forum selection clause, but such a clause shall not contradict the provisions of laws regarding court-level jurisdictions and exclusive jurisdictions.

### Expedited proceedings and discovery

- 28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Expedited proceedings, which are applied to cases with simple facts and undisputed issues, are rarely applied in M&A litigation in view of the complexity and controversies therein.

There is no discovery in litigations conducted in accordance with the PRC Civil Procedure Law.

## DAMAGES AND SETTLEMENTS

### Damages

- 29 | How are damages calculated in M&A litigation in your jurisdiction?

Calculation of damages in M&A litigation is usually conducted by an independent appraisal agency in regard of huge workload and complexity.

Different from the approach of engaging expert witness adopted by most common law jurisdictions, the PRC courts have the power to appoint appraisal agency where parties in M&A litigation failed to reach consensus as to the selection of appraisal agency.

### Settlements

- 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

First of all, as no compulsory disclosure is required in litigation, shareholders usually choose to raise inspection claims to obtain evidence before taking further actions in relation to M&A transactions.

Second, as confidential information is potentially involved in, M&A litigations are usually conducted privately at the request of both parties.

Third, there are many special regulations on transactions involving state-owned assets or foreign investment, therefore sometimes the court will refer to such administrative regulations in deciding those cases.



## THIRD PARTIES

### Third parties preventing transactions

- 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Yes. Technically, any third party can raise claims for invalidation of contract whereby to deter the performance of the transaction agreement. Usually, the claimant may seek a property preservation order from the court to freeze the trading assets or shares.

### Third parties supporting transactions

- 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No. However, litigation, as a leverage, may influence company's final decision as to whether or not to enter into an agreement for an M&A transaction.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

- 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Directors are obliged to fulfil fiduciary and diligent duties in dealing with hostile takeovers. Specifically, where listed companies receive an unsolicited or unwanted proposal to enter into an M&A transaction, directors shall:

- treat all acquirers who are contemplating in taking over of the company fairly;
- make decision and adopt measures that are beneficial to safeguard of interests of the company and its shareholders;
- restrain from abusing his or her official powers to create inappropriate obstacles for a takeover;
- refrain from using companies' resources to provide any form of financial assistance to the acquirer; and
- not undermine legitimate rights and interests of the company and its shareholders.

## COUNTERPARTIES' CLAIMS

### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

Based on a search we conducted recently, the most common types of claims asserted by and against counterparties to an M&A transaction are breach of contract and misrepresentations or fraud.

As for breach of contract, plaintiffs usually seek remedies by requesting defendants to:

- perform their duties continuously;
- pay liquidate damages; and
- compensate for losses caused by the breach.

As for misrepresentations or fraud, plaintiffs usually seek to nullify the contract in accordance with article 52 of the PRC Contract Law.

競天公誠律師事務所  
JINGTIAN & GONGCHENG

### Dong Chungang

dong.chungang@jingtian.com

### Hu Ke

hu.ke@jingtian.com

### Ge Xiangwen

ge.xiangwen@jingtian.com

34/F, Tower 3, China Central Place  
77 Jianguo Road  
Chaoyang District  
Beijing 100025  
China  
Tel: +86 10 5809 1039  
Fax: +86 10 5809 1100

## Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

With regard to substantive laws, litigations between contracting parties are governed under the PRC Contract Law, whereas applicable laws to litigations brought by shareholders are the PRC Company Laws and the Securities Laws.

With regard to cause of action, litigations between the parties to an M&A transaction are usually arouse out of counterparties' breach of contract in performance, and shareholders' litigation usually focused on executives' breach of fiduciary or diligent duties.

With regard to benefit of litigations, the benefit of winning a direct litigation belongs to the wining party, whereas the benefit of winning a derivative litigation usually belongs to the company.

## UPDATE AND TRENDS

### Key developments

- 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

To protect minority investors' rights from being infringed and bullied by companies, executives and controlling shareholders, the China Securities Investor Service Centre, which was founded by the CSRC, has recently organised and supported minority investors to bring actions against companies or management in many cases caused by false statements and executive misconduct.

# France

Christine Gateau, Pauline Faron and Arthur Boeuf  
Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

M&A litigation initiated by shareholders is not as developed in France as it is in other jurisdictions such as, for instance, the United States. However, shareholders who are suffering a loss in connection with an M&A transaction can assert various claims under French law.

Regarding mergers or split-ups, before completion of an operation, shareholders can initiate summary proceedings to postpone the date of the board meeting during which the draft terms of the merger or split-up should be adopted, or of the general shareholders' meeting at which the contemplated operation should be approved. They may also request the court to appoint an independent expert whose mission, determined by the court, is often to review the criteria directors use to set the exchange parity in cases of mergers or split-ups.

After completion of a merger or split-up, shareholders can launch judicial proceedings to get the operation annulled, damages to compensate their loss, or both. Most of the time, this action will be launched by minority shareholders arguing that majority shareholders abused their position, and it is rarely successful in practice. Annulment may also be sought on other grounds such as fraud or failure to comply with the strict rules governing the organisation of general meetings.

More generally, in any M&A transaction, shareholders can bring claims for damages against officers and directors who concluded the transaction. This claim can be brought either in their own name or on behalf of a corporation.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

Claims launched in summary proceedings by shareholders in relation to mergers or split-ups are usually motivated by a lack of information on the contemplated operation, non-compliance with the rules governing mergers or a challenge to the calculation of the exchange parity. Shareholders are responsible for proving they did not have enough information to be in a position to vote wisely, or that the procedural rules have not been complied with so that there is a risk that the whole procedure may be declared null and void. In practice, French courts do not often grant such claims.

Claims for an independent expert to be appointed can be made either in the scope of summary proceedings or ex parte proceedings. Shareholders must show a legitimate reason to preserve or establish evidence that may be helpful in subsequent litigation. For such claims

to be successful, shareholders will also have to show that they lack information, so that the appointment of an expert is necessary.

Once the merger or split-up has been voted on at the general shareholders' meeting, minority shareholders can still dispute its validity and seek annulment of the operation before a court by proving that the formal requirements for such meetings have not been met at the general meeting, or that the required majority has not been met. In practice, it is extremely rare for a merger to be annulled.

Minority shareholders are also protected against abuses of majority shareholding. To be successful, they will have to prove that the decision that was made goes against the company's interests and was made solely in the interests of the majority shareholders. Abuse of a majority position can lead to the annulment of the decision, the allocation of damages, or both. Given that the criteria are difficult to meet, this is not very often successful in practice.

Shareholders who wish to assert a claim for damages in their own name against a director have to prove three things: a fault, a personal loss and a causal link.

Regarding a director's fault, the French Commercial Code provides for three types of infringements: breach of French legislative or regulatory provisions, violation of a company's articles of incorporation (notably if directors exceed their powers) or mismanagement. The fault is objectively assessed by the courts, meaning that a director's behaviour is assessed in comparison with the standard of a reasonable person acting prudently and diligently. Regarding personal harm and a causal link, shareholders can only bring a claim in their own name if they prove that they are directly and personally affected by a director's fault: in other words, the loss they suffer cannot be a mere consequence of the loss suffered by the company itself. For that reason, claims brought by shareholders in their own name are rarely successful.

Shareholders can also bring a claim in the name and on behalf of a company to get compensation for the loss sustained by the latter (see questions 6 and 8).

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Publicly traded companies must abide by the rules governing the stock market. As such, compared to privately held companies, they must comply with additional rules aimed at affording transparency and information to their shareholders, especially in the case of takeover bids. Main claims usually relate to decisions of the AMF (the French financial markets regulator) clearing a corporate transaction or to the information given by companies involved in a takeover bid to their shareholders.

In the case of a hostile offer, specific mechanisms apply affording additional rights to shareholders (see question 5).

## Form of transaction

### 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Irrespective of the operation at stake, it is always possible for shareholders to initiate proceedings against directors and officers to seek their liability, and to get compensation both for their personal loss and the loss suffered by the company (see question 1).

Any operation that requires modifying a company's articles of incorporation has to be approved by a general shareholders' meeting (the required majority depends on the type of company, and can be 66.6 per cent or 75 per cent of the voting rights, or even a unanimous vote). For such operations, claims based on majority or minority abuses can always be brought, if some shareholders have abused their position, by majority shareholders or minority shareholders.

Additional rules must be followed for some specific transactions such as mergers or split-ups (see questions 1 and 2). In these cases, additional claims may be available to shareholders in cases of non-compliance with these specific rules.

## Negotiated or hostile transaction

### 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

Directors and officers always have to act in the company's best interests, whether they are facing a negotiated transaction or a hostile offer. Failing to do so would trigger their liability towards the company and its shareholders.

This being said, the situations in which claims may be brought by shareholders may differ depending on whether a transaction involves a negotiated transaction as opposed to a hostile offer.

Indeed, since 2014, boards of publicly traded companies receiving a hostile offer can implement defensive measures aimed at frustrating the bid without the prior consent of the general shareholders' meeting, but only to the extent permitted by the company's by-laws and within the limits of corporate interests. Shareholders may have a claim against the directors if they violate the powers granted to them by the by-laws.

## Party suffering loss

### 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

When the loss is suffered by the corporation itself, in principle, it is the corporation's legal representatives who will initiate the action to get compensation. If they fail to do so or if they are personally involved in the damage, then shareholders will launch a derivative action on behalf of the company (see question 8).

Shareholders can always bring actions to claim compensation for the loss they personally suffered, provided they can prove that they suffered a personal loss, which cannot be a mere consequence of the loss sustained by the company (see question 1).

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

#### 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Class actions exist under French law, but they are not applicable to shareholder claims. Therefore, in principle each shareholder must bring

his or her claim in his or her own name and cannot pursue claims on behalf of other shareholders.

This being said, shareholders that have suffered personal losses directly arising from the same conduct of a director or officer can give one or more of the shareholders a proxy to bring claims on their behalf and in their names before civil courts. The proxy must be made in writing, and must mention each shareholder's name and address, the number of shares they have and the amount of money they are claiming.

Affected shareholders may also create an association that will bring the claim on their behalf. This enables several shareholders to share the cost of judicial proceedings.

### Derivative litigation

#### 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

In principle, it is the legal representative of the company who is in charge of protecting the corporation's best interests and bringing claims when necessary. When the loss is suffered by the corporation itself as a result of directors' or officers' behaviour, or when directors fail to take action, shareholders are allowed to bring a claim in the name and on behalf of the corporation. Under French law, this derivative action is called *ut singuli* and can be brought by any shareholder, no matter the number of shares he or she holds. This action is by nature subsidiary: it can only be brought by a shareholder to overcome the directors' inaction.

It should be noted that this right is not often exercised, as shareholders have to bear the litigation costs and, in the event of success, they do not get any compensation, as damages are fully awarded to the corporation.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

#### 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Several procedural tools are available under French law to a party wishing to get interim or injunctive relief in M&A litigation. Such measures can be sought either in the scope of summary proceedings or ex parte proceedings. In this latter case, a plaintiff would have to show a good reason to derogate from the adversarial principle and not to call the other party (for instance, if there would be a risk that the measure may be jeopardised if the other party was informed).

Summary proceedings can be brought before the presiding judge of a commercial court if the plaintiff can prove that there is an emergency situation; and that the requested measure is either not disputable or that such measure is necessary because of the dispute between the parties.

Alternatively, any measures likely to prevent imminent harm can be ordered. In addition, in cases where the existence of the obligation cannot seriously be disputed, the judge can order specific performance of the obligation, even if the obligation at stake is an obligation to do something.

The powers of a judge hearing such cases are quite broad: they will usually consist of protective measures such as appointing an ad hoc agent to chair the general shareholders' meeting instead of the directors; appointing an escrow agent to block shares pending resolution of a dispute; or ordering postponement of a general shareholders' meeting. The judge may also enjoin communication of documents, and if necessary order a daily penalty.

French courts tend not to interfere directly in the conclusion of deals, whether to modify deal terms or enjoin the signing of the deal, as one of the cornerstones of French contract law is the principle of freedom to contract. If one of the parties finally decides not to sign the deal, its civil liability will be triggered as it will be considered to be acting in bad faith – all the more if the negotiations are very advanced – but it will generally not be forced to sign the deal.

### Early dismissal of shareholder complaint

#### 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

There are no discovery or disclosure mechanisms under French law. Defendants cannot seek early dismissal of a shareholder complaint.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

#### 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Shareholders who have suffered a direct and personal loss caused by third-party advisers can bring claims against the advisers if they can prove that they committed a fault that resulted in a loss. The fault could consist in a wrongdoing, a conflict of interest or negligence.

The company itself may also bring a claim against such advisers, either through its legal representatives or, if they fail to act, through a derivative action initiated by shareholders (see question 8).

### Claims against counterparties

#### 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Under French law, directors have a duty of loyalty towards shareholders and their company. They should always act in their company's best interests. Shareholders can bring claims against counterparties provided they can prove that the counterparties directly caused the directors to breach their legal obligations or their obligations deriving from the company's by-laws. Third parties who voluntarily help directors to breach their obligations incur civil liability under general tort law.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

#### 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

The legal provisions on directors' liability are of public policy: they cannot be limited or modified by agreement. The corporation's constituting documents cannot modify the extent of directors' duties towards the shareholders or the company. Provisions aiming to limit the scope of board members' or executives' liability, or provisions aiming to limit or condition a shareholder's right to act against board members or executives, shall be deemed unwritten, and would therefore have no effect. Similarly, no decision of the general shareholders' meeting could extinguish an action seeking directors' or executives' liability.

### Statutory or regulatory limitations on claims

#### 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Any shareholder, no matter the number of shares he or she holds, is entitled to bring a claim against directors and officers in his or her own name or on behalf of the corporation.

Directors and officers can be exonerated from liability if they can prove force majeure, which is defined as an irresistible and unpredictable event. In practice, owing to the strict criteria to be met for it to be successful, such defence is not very common.

Board members and executives should not be held liable for acts that have been approved by the general shareholders' meeting, except if they withheld material information or breached the law.

Directors can also try to be exonerated if they can prove that they formally objected to the decision that the board collectively made.

### Common law limitations on claims

#### 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

With France being a civil law country, case law does not have the same normative value as it does in other jurisdictions such as the United States.

When a shareholder brings a claim against a board member, the central question that courts must answer is whether the board members or executives acted in the corporate interests. The concept of corporate interests is key in French commercial law as it should serve as a guide for the board in all the decisions it has to make. Corporate interests are construed widely as covering not only shareholders' private interests but also the long-term interests of the company itself, its employees and creditors.

The onus of proof lies with the shareholder bringing the lawsuit to establish that the transaction was not in the corporate interests or that board members or executives committed a fault. Courts decide on a case-by-case basis taking into account all the circumstances of a case. There is no such thing in France as the 'business judgement rule'. Board members are not entitled to specific presumptions preventing courts from second-guessing their decisions. However, in practice French courts are reluctant to interfere in the management of companies, except if a breach of corporate interests is obvious.

## STANDARD OF LIABILITY

### General standard

#### 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Board members or executives can only be held liable, either individually or collectively, if they committed a fault. The French Commercial Code provides for three types of infringements likely to trigger their liability towards shareholders or a company: a breach of French legislative or regulatory provisions, a violation of the company's articles of incorporation and mismanagement.

For board members or executives to be found guilty of mismanagement, shareholders must prove that the board or executives did not act in the corporate interests or that they violated their duty of loyalty towards the company or its shareholders. Their behaviour is assessed on an objective basis, by comparison with what a reasonable person,

acting in good faith, prudently and diligently, would have done in a similar situation. The assessment will largely depend on the specific facts of each case (the company's size, the operation at stake, its public or private nature, etc).

### Type of transaction

- 17 | Does the standard vary depending on the type of transaction at issue?

Board members always have to act in the corporation's best interests, regardless of the type of transaction at issue.

This being said, the question of whether board members or executives are guilty of mismanagement very much depends on the facts of each case and the behaviour that would have been expected of a reasonable person placed in a similar situation. To that extent, the assessment of board members' or executives' behaviour will be impacted by the nature of the transaction at issue, the characteristics of the contemplated transaction and the counterparties.

### Type of consideration

- 18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

The type of consideration paid to the seller's shareholders will be taken into account in courts' general assessment of the transaction. However, the standard remains corporate interests.

### Potential conflicts of interest

- 19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

Board members always have to act in the corporation's best interests. This implies that they must refrain from serving their own personal interests.

To prevent potential conflicts of interest, transactions concluded between a corporation and a board member, or between the corporation and another corporation in which a board member has an interest (even an indirect one), have to follow a specific procedure. They are called 'related-party agreements', and have to be agreed by the board and then ratified by the general shareholders' meeting. If a transaction was concluded without the approval of the board or the general shareholders' meeting, it can be annulled if it had harmful consequences for the company.

### Controlling shareholders

- 20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

A transaction concluded between a controlling shareholder and the company falls within the ambit of 'related-party agreements', and as such has to be reviewed and agreed by the board of directors and submitted for approval to the general shareholders' meeting (see question 19).

If a controlling shareholder is receiving consideration in connection with the transaction that is not shared ratably with all shareholders, minority shareholders may launch an action claiming that the controlling shareholder abused its majority position. To be successful, they would have to prove that the decision that was made was contrary to the company's interests and was made solely in the interests of the majority shareholder. The abuse of a majority position can lead either to the annulment of the decision or to the allocation of damages, or to both.

## INDEMNITIES

### Legal restrictions on indemnities

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

In most cases, directors' and officers' insurance is subscribed to by the corporation so that the legal fees of officers or directors named as defendants will be covered by this insurance (see question 24).

If this is not the case, there are no legal restrictions in France on the company advancing or repaying a director or officer the legal fees he or she has incurred given that, until and unless a judgment is handed down, the defendant is presumed not liable. Uncertainty exists as to whether this should be considered as a related-party agreement that would have to be authorised by the board and by the general shareholders' meeting (see question 19). For the sake of prudence and transparency, it is advisable, if the company decides to advance the legal fees, for this decision to be made collectively by the board of directors.

If the director or officer is eventually found liable, the question of whether the company should request repayment of the legal fees will depend on the facts of each case. If the wrongdoing committed by a director or officer was intentional or of a particular gravity (for instance, in the case of a criminal offence or fraudulent behaviour), the company would probably have to ask for repayment of the money it advanced since not doing so may be considered as not being in its corporate interests.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

- 22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

Parties to an M&A transaction have the duty to negotiate in good faith. They can incur civil liability for failing to comply with that duty, for instance if they continue negotiations while knowing that they have no intention to conclude a deal.

Freedom to contract includes freedom to negotiate each clause of a contract. Therefore, as far as privately held companies are concerned, break-up fee, standstill, no-shop, exclusivity or confidentiality clauses are all valid under French law, provided they are negotiated in good faith.

Publicly held companies are subject to stricter rules, especially concerning break-up fees, which are valid only if they do not hinder the concept of the free play of offers and counteroffers by setting an amount that would be too high and would hence deter shareholders from accepting a higher bid. The AMF closely controls such clauses.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

- 23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

If a transaction has to be approved by the general shareholders' meeting, board members cannot theoretically be held liable for such transaction's potentially adverse effects unless it is established that the transaction was approved because of mismanagement by the board or misinformation provided by the shareholders.

Minority shareholders can always challenge the validity of a transaction approved by the general shareholders' meeting if it appears that the formal rules for calling the meeting have been violated or if the majority shareholders have abused their position (see question 2).

It should be noted that the fact that a shareholder voted in favour of a transaction does not preclude him or her from subsequently bringing a claim to challenge its validity.

### Insurance

#### 24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors' and officers' insurance has significantly developed in recent years in France due to the influence of US practice. In the vast majority of cases, the insurance policy is negotiated and paid by the corporation itself and covers any director and officer. The company's de facto managers can also be covered.

The insurance policy covers a director's civil liability towards the shareholders for any loss they personally sustained and towards third parties. Some insurance policies may also cover the loss suffered by the company itself. The insurance policy covers both damages that may be awarded and the fees incurred by the directors and officers to defend themselves (see question 21).

Insurance policies also provide for exclusions, some of which cannot be negotiated as they derive from law. This is notably the case for intentional misconduct and criminal liability, which cannot be covered by the insurance policy.

### Burden of proof

#### 25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The rules applicable in M&A litigation are the same as those applicable in any litigation: the burden of proof lies with the claimant. Therefore, if a shareholder wishes to claim damages against board members or executives, he or she has to prove the fault, the loss and the causal link between the two. The burden of proof does not shift. Although the business judgement rule is not applicable as such in France, French courts tend to avoid interfering in the management of a company unless there is a clear violation of corporate interests (see question 15).

### Pre-litigation tools

#### 26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Shareholders have a general right to be informed of a corporation's commercial and financial situation. They are entitled to obtain at any time the disclosure of several documents, including:

- the annual accounts of the last three financial years;
- the auditor's report;
- the management reports made by directors and officers; and
- the reports and attendance sheets of the last shareholders' meeting.

Additionally, before general meetings, any shareholder can ask questions of the directors and officers in relation to the agenda of such meeting. Twice a year, any shareholder or group of shareholders holding more than 5 per cent of the share capital is entitled to put questions to the president of the board in relation to facts likely to jeopardise the company's activity.

Shareholders can also initiate summary proceedings to have an independent expert appointed, whose mission will consist of assessing the conduct of the board on a specific matter. They can also request seizure of any evidence (reports, emails, hard drives, deliberations) likely to be helpful to ground their claim in potential subsequent litigation (see question 9).

### Forum

#### 27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

In principle, disputes relating to the functioning of commercial companies, their shareholders, and their directors and officers must be brought before the commercial court having jurisdiction over the place where the registered office of the company is located. Shareholders who seek a board member's liability can also bring their claim before the commercial court having jurisdiction over the place where the board member resides.

The articles of incorporation can provide for a forum selection clause covering disputes arising from the conduct of board members or between shareholders. However, these clauses are only valid if every shareholder can be considered as a 'trader' under French commercial law, which will depend on the type of company at stake. Besides, such clause must be very clearly stated in the statutes.

A company's articles of incorporation can also provide that disputes between shareholders, the company, directors and officers will be submitted to arbitration.

### Expedited proceedings and discovery

#### 28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Summary proceedings are widely developed in France. Regarding M&A transactions, they can be a very useful tool for shareholders (see questions 9 and 26).

There is no discovery mechanism in France.

## DAMAGES AND SETTLEMENTS

### Damages

#### 29 | How are damages calculated in M&A litigation in your jurisdiction?

Under French law, the general principle governing the calculation of damages is that the financial compensation awarded must compensate the full loss but nothing except the loss. Loss of chance can be compensated as well as damage to reputation, if applicable. This rule prevents punitive damages from being awarded in France.

Parties can decide to include penalty clauses whereby they determine in advance the amount of damages that will be payable if the obligations arising from the contract are violated. However, a judge can reduce or increase such amount if it is manifestly excessive or ridiculously low.

### Settlements

#### 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

There is no special issue with respect to settlement agreements concluded between a shareholder and a board member for individual claims that a shareholder may have brought against him or her. However, in the case of a derivative action, a shareholder cannot settle on behalf of a corporation for the loss suffered by the latter.

## THIRD PARTIES

### Third parties preventing transactions

- 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

In the case of a merger, the creditors of any company participating in an operation are entitled to challenge the transaction if they prove that a risk exists that they may not recover their debt. In this situation, the court may order the company to reimburse the debt immediately before closing the deal or to provide financial guarantees.

Apart from this specific case, even if the contract concluded with a third party includes an exclusivity clause, a breach of this clause would only allow the third party to claim damages; it would not enable him or her to stop an otherwise-agreed transaction.

### Third parties supporting transactions

- 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Although this would theoretically be possible, we doubt that this would be successful before the French courts because of the freedom to contract, which states that parties are free to decide whether they want to enter into an agreement.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

- 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Since 2014, boards of publicly traded companies receiving a hostile offer can implement defensive measures aimed at frustrating the bid without the prior consent of the general shareholders' meeting, but only to the extent permitted by the company's by-laws and within the limits of corporate interests. Defensive measures can, for instance, consist of:

- looking for a better deal;
- making negative statements to encourage shareholders not to sell;
- selling strategic assets to a friendly third party (the 'crown jewels' defence);
- launching a counter takeover bid to acquire the would-be buyer (the 'Pac-Man' defence); or
- buying business or assets (the 'Fat Man' defence).

Preventive measures such as putting shareholding agreements in place (pre-emption agreements, double voting rights, consultation agreements, etc) can also be implemented.

As an exception to the general rule, shareholders can also decide to expressly remove this right from the board of directors and include in the by-laws what has been referred to as 'a passivity rule'. This way, any measures taken aimed at frustrating a hostile offer would first need to be approved by the general shareholders' meeting.

Should the directors not act in the company's best interests, shareholders may bring a claim to get the measure suspended through summary proceedings. Otherwise, shareholders would have the possibility of bringing an action against the directors to seek their liability.

## COUNTERPARTIES' CLAIMS

### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

Claims are frequently initiated by the buyer in a share deal arguing that the seller breached its representations and warranties because the annual accounts did not give a fair and accurate description of the company's financial situation. In this case, the buyer usually initiates proceedings before the commercial courts on the basis of the liabilities guarantee conceded by the seller. Claims are also frequent between counterparties in relation to the enforcement of earn-out provisions or purchase price adjustment provisions.

To assist them, parties usually resort to private experts (accounting or audit companies) who are in charge of performing an analysis of the company's financial situation and helping parties assess their claims. Parties can also ask the court to appoint an independent expert. This process is long and can be costly, especially if the company at stake uses specific accounting methods (for instance, the on-progress accounting method, which is sometimes used for long-term contracts). For this reason, settlements are not unusual in these types of litigation.

### Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

In France, claims between counterparties to an M&A transaction are by far more common than litigation initiated by shareholders. They tend to be claims on the merits of the case whereby one party claims monetary compensation from the other one. The judicial proceedings are usually lengthy and technical, and can eventually lead to negotiations and a settlement being concluded.

By comparison, litigation brought by shareholders is seen less frequently in France. Litigation can be launched in summary proceedings, and mostly aims at gaining information or having an independent expert or agent appointed to collect documents, review a board's behaviour or replace the board for specific acts such as general shareholders' meetings. Such proceedings rarely end in directors being found liable to pay monetary compensation.

## UPDATE AND TRENDS

### Key developments

- 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

Activism has grown tremendously in the past years in Europe generally and in France, with foreign activist funds aiming at acquiring minority shareholding in major French companies and often threatening to bring lawsuits when they consider that decisions are not made in the company's best interests. The recent strengthening of shareholder activism in France will necessarily imply an expansion of M&A litigation in France.

Another foreseeable cause of development of M&A litigation in France in the future may be due to the emergence in French corporate law of the notion of the 'social interest of the company' beside the classic notion of the 'company's best interest' (which is to generate profits for its shareholders). Indeed, the 'PACTE Bill' (action plan for economic growth and companies' transformation), which is currently (spring 2019) being examined by the French parliament, could authorise shareholders to include, in the company's constituting documents, the

social and environmental goals that are pursued by the company and that will have to govern the conduct of board members and executives.

It is yet to be seen how this will apply in practice. However, it is foreseeable that this notion may trigger debates that may lead to litigation between shareholders and board members or officers regarding the definition and extent of this notion when having to take a position on a transaction that may impact the social interest of the company. One may also foresee debates on the interpretation of the content of the social interest of the company. Some authors already contemplate that this notion of the company's rationale could be used as a new form of defensive measure available to board members of publicly held companies against hostile offers that would not comply with the social interest of the company.

The logo for Hogan Lovells, featuring the name "Hogan Lovells" in a serif font, with "Hogan" on the top line and "Lovells" on the bottom line, set against a dark grey rectangular background.

---

**Christine Gateau**

christine.gateau@hoganlovells.com

**Pauline Faron**

pauline.faron@hoganlovells.com

**Arthur Bœuf**

arthur.boeuf@hoganlovells.com

---

17, avenue Matignon  
75008 Paris  
France  
Tel: +33 1 53 67 47 47  
Fax: +33 1 53 67 47 48  
www.hoganlovells.com



# Germany

Olaf Gärtner and Carla Wiedeck

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

Apart from situations in which shareholders are a party to a transaction (ie, as sellers) and have all the respective rights and duties, shareholders typically assert claims in three types of cases: lack of information or disclosure; violation of stipulations that protect the shareholders; and tortious acts.

In particular, shareholders may assert claims for damages if they have not been duly informed about the transaction. Pursuant to the German Securities Trading Act, the management board of a publicly listed stock company has to publish insider information that directly affects the company. This disclosure obligation applies, in particular, to information that is relevant to the further development of the share price. In the case of an M&A transaction, this notification requirement will be triggered if its realisation is sufficiently probable. Further, the shareholder agreement, the statutes of the entity or the rules of procedure of the management board can stipulate certain requirements for M&A transactions: for example, the involvement and consent of an investment committee or a resolution of the shareholders. Shareholders may assert claims if such stipulations have been violated. Further, in certain events potentially following an M&A transaction, such as the conclusion of a profit transfer agreement, in the event of a squeeze-out or, for example, in the event of a transformation of the target according to the German Transformation Act, shareholders have a claim to appropriate cash compensation.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

To bring a claim for damages for lack of information under the Securities Trading Act, a shareholder must assert that the management board has violated its duty of disclosure. To do this, the shareholder must show that the management board has failed to disclose insider information that directly affects the company. In addition, a claim can be considered if an incorrect ad hoc announcement has been published. However, it is typically difficult to prove in court that the shareholder has suffered a loss, as typically the stock price rises after a transaction.

To assert a claim for a breach of a shareholder agreement, a shareholder must show that the provisions of the shareholder agreement have been violated in an unlawful manner. The shareholder can then try to block the transaction (see question 9) or claim damages in cases where the transaction has already taken place. If the shareholder claims damages, the shareholder has to show he or she suffered a loss.

Further, shareholders have the right to receive appropriate compensation in certain cases (see question 1). In these cases, the shareholder must show that he or she has not been offered compensation or has not been offered such in an orderly manner, or that the cash compensation offered is not appropriate.

A claim for compensation for damages in tortious acts is possible if shareholders are withdrawn from their membership rights. In addition, shareholders are also entitled to a tortious claim for damages if they have been intentionally injured in a manner contrary to good morals. This may be the case, for example, if a member of the management board participates in immoral acts committed by majority shareholders or in connection with the acquisition of shares through deliberately incorrect ad hoc disclosure.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes, there are several stipulations that only apply to listed stock corporations. Some of the above-mentioned main claims – for example, the obligation of the management board to disclose insider information in accordance with the Securities Trading Act (see in detail questions 1 and 2) – only apply to publicly listed stock companies.

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

In general, the form of a transaction has no influence on the type of claim that can be brought. The main exception is the case of a merger: the Transformation Act contains special statutory stipulations for shareholder claims in the event of mergers of companies. For example, shareholders who raised an objection to a merger resolution have a claim to appropriate cash compensation against the acquiring legal entity. Further, the shareholders can challenge a resolution to merge.

### Negotiated or hostile transaction

- 5 Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No.

## Party suffering loss

- 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Shareholders can only assert claims if they themselves have suffered a loss. For example, shareholders can assert claims if the shareholder agreement is violated or if the management board has not fulfilled its notification obligation (see in detail questions 1 and 2). If the corporation has suffered the loss, shareholders usually cannot assert any claims. However, in exceptional cases, shareholders can take legal action for the claims of the corporation (litigation in one's own name on another's behalf; see in detail question 8).

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

- 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

German law does not provide for class actions. A comparable tool is model litigation: the Capital Markets Model Case Act facilitates the enforcement of claims for damages of shareholders in a stock company by enabling model litigation in cases based on false, misleading or omitted public capital market information. If the same factual and legal questions arise in at least 10 individual lawsuits, a model proceeding can be initiated in which these factual and legal questions are decided. After the decision in a model proceeding becomes binding, the individual lawsuits resume and the courts hearing these cases must take the decision into account as binding. Further, shareholders can bundle and enforce claims via a claims vehicle (ie, assign their claims to another entity that brings a lawsuit). In such cases, the assignments have to be in compliance with the Legal Services Act. In practice, this means that they either sell their claims or that the claims vehicle is registered for collection services.

### Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

The German Stock Corporation Act provides that shareholders may bring proceedings in their own name for directors' and officers' (D&O) liability on behalf of the corporation (litigation in one's own name on another's behalf). Shareholders whose shares represent 1 per cent of the share capital or a pro rata amount of €100,000 may apply to the district court responsible for the corporation for approval of such an action. The action can only be approved if the facts provide a reason to suspect that the company has suffered a loss as a result of improprieties or gross breaches of the law or articles of association, and no overriding interests of the company exist that would prevent the assertion of such damage claim. Apart from this, shareholder activism for claims of the stock company is not permissible.

In a limited company, shareholders can bring legal action in their own name on behalf of the corporation in accordance with the general principles of an *actio pro socio*. This requires that claims of the corporation against its shareholders resulting from membership (eg, breaches of trust) exist. Furthermore, an *actio pro socio* is subsidiary, and therefore inadmissible if the corporation itself asserts its claims. It shall only be admissible if the competent body refuses to pursue legal action.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Injunctive or other interim relief can only be awarded if a shareholder can prove that he or she has a certain right or claim and that, without interim relief, the realisation of such right or claim would be thwarted or made significantly more difficult. In particular, an M&A transaction can theoretically be blocked, if, for example, a shareholder resolution is required. In such cases, a court could block the execution of the resolution if the resolution was unlawful, against the corporate by-laws, etc (note that courts are rather reluctant to block the decision-making process itself). Another example would be that third parties that have a pre-emptive right can seek interim relief.

German courts cannot generally enjoin M&A transactions or modify deal terms. However, in cases where the contract has already been concluded and the seller is unwilling to transfer the shares, the buyer can sue the seller for the transfer of the shares (performance) or for damages.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

No, early dismissal and discovery only exist in very limited cases, and M&A transactions are not covered by such special relief.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

In general, only the corporation itself can assert claims against advisers on the basis of its contractual relationship. Individual shareholders are not party to this contract. However, shareholders may assert claims if the contract has some protective effect to the benefit of third parties. This can either be explicitly set out in the contract or can be a matter of interpretation. For example, a contract with a tax consultant advising on the best legal form regarding the tax law implications of a transaction or the corporate structure can have a protective effect to the benefit of shareholders, who then can bring a claim against the consultant. Further, claims based on tortious acts can also be brought by the shareholders.

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

No, with the exception of claims based on tortious acts.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

According to the Stock Corporation Act, a stock company may not waive or compromise a claim for damages that it may have against a board

member in advance: it can only do so after the expiry of three years after the claim has arisen. The stock company can of course stipulate duties of the board members that go beyond the statutory law. In a German limited company, the parties can go both ways: that is, either limit or extend the liability.

#### Statutory or regulatory limitations on claims

14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

No.

#### Common law limitations on claims

15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

German law provides for a 'business judgement rule', which states that a board member or managing director acts in a dutiful manner if he or she holds sufficient information prior to making a business decision, does not have a conflict of interest and may be trusted to act in the best interests of the company.

### STANDARD OF LIABILITY

#### General standard

16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

There are no specific standards in connection with an M&A transaction. As the transaction itself is a business decision, the business judgement rule (see in detail question 15) applies. However, the management board or director has to respect all statutory duties, as well as all obligations laid down in the shareholder's agreement, statutes, etc. Regarding liability for tortious acts, a board member or director must have intentionally and immorally harmed the shareholders, and have also intended that the shareholders suffered a loss.

#### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

No.

#### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

#### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

The business judgement rule (see in detail question 15) does not apply if there is a conflict of interest. A prerequisite for the application of the business judgement rule is that the manager's decision is based exclusively on the interests of the company. The managing director must not allow him or herself to be guided by irrelevant aspects (ie, his or her

own interests) when choosing between the various alternative courses of action.

#### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

The standard does not vary. However, if a board member agrees on terms with the controlling shareholder that are not at arm's length, or if the board member grants benefits only to a controlling shareholder, the board member can usually be held liable. Further, there might be tax implications (ie, hidden distribution of profits).

### INDEMNITIES

#### Legal restrictions on indemnities

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Usually, D&O insurance covers legal and extrajudicial defence costs, and in particular the legal consultancy costs. D&O insurance is usually paid for by the company.

### M&A CLAUSES AND TERMS

#### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

Shareholders can at most challenge the conclusion of the contract unless they are a contracting party.

### PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

#### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

A resolution of the shareholders' meeting is binding for the management board.

However, there are only a few cases in which shareholders are required to give their consent, such as:

- in cases of the transfer of registered shares with restricted transferability;
- if the transaction results in a permanent change in the corporate purpose of the stock company;
- if the seller stock company undertakes to transfer the entire assets of the company by way of transfer of individual rights; and
- if a merger is associated with the company transaction in accordance with the Transformation Act.

In addition, the management board can theoretically obtain the approval of the shareholders' meeting for corporate transactions on a voluntary basis. In practice, however, this hardly ever happens.

## Insurance

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

D&O insurance is usually involved in litigation against management. Most policies stipulate that either the board member or director has the obligation to follow any instructions under the insurance policy or that the insurance can directly lead the defence. Further, the board member or director can assign a claim for cover to the company, which then can initiate proceedings directly against the insurance.

## Burden of proof

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The burden of proof varies depending on a shareholder's claim. As the claimant, the shareholder bears the burden of proof for all facts that are favourable to him or her.

For example, in the event of a shareholder's action for deficiency in a resolution, the shareholder must prove that he or she is entitled to challenge the resolution, ie, that he or she is a shareholder, and that the resolution violates the law or the company's articles of association.

In the case of a claim arising from torts law, the injured party, that is, the shareholder, bears the burden of proof for all liability conditions: in particular, he or she must prove intent on the part of a board member or director, as well as the occurrence of a pecuniary loss. In the more common case of a lawsuit brought by a corporation against its board members or directors, the board members or directors have to prove that they did not violate their duties and that they acted without fault. On the other hand, the corporation must provide evidence of the damaging act, the damage caused by it and the loss.

## Pre-litigation tools

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Shareholders have a statutory right to information and inspection rights regarding the company. This right includes all information related to the management and the economic situation of the company, and to the company's relations with third parties, and therefore also includes acquisitions and disposals. In addition, shareholders have the right to inspect the company's books and records (eg, all documents, files, films, computer records). The right of access to information and inspection has limitations: for example, a shareholder has to observe the principles of proportionality, and a board member or director does not have to disclose information if he or she would make him or herself liable to prosecution by providing information.

## Forum

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

In the event of an action for deficiency in a resolution, the district court in whose district the corporation has its registered office is competent. In all other respects, the general rules of local jurisdiction apply. Forum selection clauses are generally admissible in contracts between companies.

## Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

No.

## DAMAGES AND SETTLEMENTS

### Damages

29 | How are damages calculated in M&A litigation in your jurisdiction?

The object of damages is to place the party to whom they are awarded in the same pecuniary position that they would have been in if the breach triggering liability had not occurred. The usual ways in which experts calculate damages are normally used in M&A litigation.

However, in particular regarding the value of a company, the following method is applied:

- in the case of non-delivery or non-acceptance of the target company, the target's enterprise value is usually derived from future surpluses by means of the usual valuation procedures; and
- in the case of non-fulfilment, the damage incurred is calculated by deducting the purchase price from this determined enterprise value.

A business valuation is also made in cases of the delivery of a company with an impairment of its value. Consequential damages and loss of profits are also compensated.

Further, if the parties are in dispute as to whether damage has occurred and how much the damage amounts to, the court can estimate the damage. To do so, it is necessary that the plaintiff has presented sufficient facts for the court to have a basis for an estimate.

### Settlements

30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

As there are no class actions in Germany, it can be more difficult for shareholders to assert their claims in court. Except for a few exceptions (see in detail question 7), each shareholder must assert his or her own claim and assume the risk of litigation. Likewise, there are no class settlements in Germany, ie, the company or board member has to settle individually with each shareholder. In the case of a settlement, the parties should reach an agreement regarding the costs, particularly in cases in which a claim already has been filed. Otherwise, the party that, following a settlement, withdraws the claim would have to bear the costs of the proceedings.

## THIRD PARTIES

### Third parties preventing transactions

31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

This is possible in special cases, such as if a third party has a pre-emptive right.

### Third parties supporting transactions

32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No, unless the M&A transaction had already been agreed upon and the third party sues for transfer of the shares.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

- 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

In such cases, several duties may arise out of the loyalty obligations towards the shareholders: for example, they have to be informed about the offer.

In addition, there are several statutory provisions in the case of takeover bids regarding stock companies. To mention a few, the management board and the supervisory board have to render a reasoned opinion on the bid; and after the publication of the decision to make a takeover bid and until publication of the result, the management board of the target company may not take any actions that could prevent the success of the offer. This does not apply to actions that a prudent and conscientious manager of a company not affected by a takeover bid would have taken, to endeavours to find a competing offer or to actions consented to by the supervisory board of the target company.

Further, duties and responsibilities of board members and directors are usually defined in the respective articles of association of the company, the employment contract or the shareholders' agreement.

## COUNTERPARTIES' CLAIMS

### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

In Germany, disputes between the parties to an M&A transaction are far more common than shareholder claims.

The most common reasons for disputes are impairments of a company. The buyer often tries to assert his or her claims in particular from guarantees, violations of pre-contractual obligations and liability for defects (claims based on tort are possible, but less common). Regarding guarantees, owing to the great importance of disclosures in the annual financial statements for the valuation of the target company, accounts warranties are often the subject of post-M&A disputes, and are therefore a possibility for the purchaser to claim damages. Usually, accounts warranties require that the annual financial statements of the target company provide a true and fair view of the assets, liabilities, financial position, and profit or loss of the target company. Further, the liability system for M&A transactions is usually structured by guarantees; hence, claims based on liability for defects are usually also claims based on breach of a guarantee. In addition to claims arising from guarantees, the buyer often asserts claims arising from a breach of pre-contractual obligations. The pre-contractual information obligations of the seller are particularly relevant. A claim for damages due to pre-contractual breaches of the duty of disclosure is generally only considered if the buyer can prove that the seller has acted with knowledge and will. In the case of a claim arising from a pre-contractual breach of duty, the buyer must state that there was a duty to inform. In addition, he or she must prove that the information provided was incorrect and that the seller was aware of it. It must have been apparent to the seller that the relevant information was essential for the signing of the contract by the buyer (causality). For example, a claim may exist if the seller has not informed the buyer about the company's substantial debts, if the seller has provided false information about the sales made by the company or if the seller has violated the rules of proper accounting.

Further, disputes regarding the calculation of the final purchase price are very common. The parties often agree on a basic purchase price



#### Olaf Gärtner

olaf.gaertner@hoganlovells.com

#### Carla Wiedeck

carla.wiedeck@hoganlovells.com

Karl-Scharnagl-Ring 5  
80539 Munich  
Germany  
Tel: +49 89 290 12 0  
Fax: +49 89 290 12 222  
www.hoganlovells.com

of the company, which is then adjusted on the basis of a fixed purchase price calculation method. For this reason, the purchase price is often not fixed at the time of signing the purchase contract. In most cases, the parties still have to fulfil conditions between signing and closing of the purchase contract. After signing the purchase contract, however, the company often develops further. This means that the purchase price is adjusted and may be higher than expected by the buyer. This in turn leads to the fact that the buyer often accuses the seller of having consciously caused this increase in the purchase price.

Finally, the parties to an M&A transaction often argue about the effectiveness of M&A contracts. In particular, a buyer can assert claims based on fraudulent misrepresentation on the part of the seller. In this regard, it is particularly relevant that the right to challenge a contract on the grounds of fraudulent deception cannot be effectively excluded from the contract.

### Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Disputes between the parties to an M&A transaction are usually contract-based and solved by arbitration (as most M&A contracts contain arbitration clauses). Litigation brought by shareholders is in most cases based on tort and – owing to the lack of a contractual basis, and therefore a lack of an arbitration clause – brought in public courts.

## UPDATE AND TRENDS

### Key developments

- 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

The most remarkable trend over the past 12 to 24 months is the increased number of D&O liability cases stemming from insolvency situations. In these situations the insolvency administrator is suing former board members for negligent or intentional violation of their duties. Although this is a general trend without specific focus on M&A transactions, it also encompasses the latter in that respective violations in M&A transactions (eg, selling a company below its value) can also be pursued.

# Hong Kong

Chris Dobby and Grace Zhu

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The main types of claims shareholders may assert against companies, officers and directors in connection with M&A transactions include:

- statutory (section 725(1)(b) or (2) of the Companies Ordinance) and common law unfair prejudice claims;
- statutory claims for breach of fiduciary duty by a director (section 728(4)(b) of the Companies Ordinance); and
- common law claims against directors for acting in excess of their powers or acting unfairly to the members.

Shareholders may have claims in their own names (personal actions) or in the name of the company (derivative actions). Section 732 of the Companies Ordinance allows a member of a company, with leave of the court, to bring derivative proceedings on behalf of the company in respect of any 'misconduct' committed against the company.

Other common causes of action vary from common law claims for breach of contract (including in relation to rights set out in the company's articles of association, which may also be pursued under section 728(4)(c) of the Companies Ordinance); and claims against third parties for aiding and abetting a default of the Companies Ordinance, or breach of a fiduciary duty and breach of a fiduciary duty by a party other than a director of the company (section 728(4)(a) of the Companies Ordinance).

### Requirements for successful claims

2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

For unfair prejudice actions, a shareholder must satisfy the court that the company's affairs are being or have been conducted in a manner unfairly prejudicial to the interests of the members generally or of one or more members; or an actual or proposed act or omission of the company (including one done or made on behalf of the company) is or would be so prejudicial.

For breach of fiduciary duty actions, a shareholder must show that a director has failed to act honestly, in good faith and in the best interests of the company as a whole; or a director has failed to exercise his or her powers for the proper purposes for which those powers have been conferred on him or her.

The directors of a company must exercise reasonable care, skill and diligence that would be exercised by a reasonably diligent person with the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions of the director, and in relation to the company (section 465(2)(a) of the Companies Ordinance);

or the general knowledge, skill and experience that the director has (section 465(2)(b) of the Companies Ordinance).

A registered shareholder of the company or a shareholder of an associated company (ie, a subsidiary or holding company of the first company) may bring a derivative claim under section 732 of the Companies Ordinance if it can satisfy the court that:

- on the face of the application, it appears to be in the company's interests that leave should be granted;
- there is a serious question to be tried;
- the company has not itself brought the proceedings; and
- the shareholder has served a written notice on the company of his or her intention to apply for leave.

If leave of the court is obtained, the shareholder must prove on the balance of probability the company's entitlement to the relief sought at the full trial.

### Publicly traded or privately held corporations

3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

The basic principles for a shareholder to bring a claim against directors, officers or third parties in M&A transactions between privately held companies and publicly traded companies are generally the same. However, there might be additional regulations on public companies (particularly publicly listed companies).

In Hong Kong, the Companies Ordinance defines that a company is a 'private company' if its articles of association restrict the right to transfer shares, limit the number of its members to no more than 50, and prohibit any invitation to the public to subscribe for shares in, or debentures of, the company. The term 'public companies' is defined in the Companies Ordinance as companies other than private companies and companies limited by guarantee.

Public companies listed in Hong Kong are subject to:

- the Securities and Futures Ordinance (SFO);
- the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited or the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (Listing Rules); and
- the Codes on Takeovers and Mergers and Share Buy-Backs (Takeovers Code).

Publicly listed companies have various disclosure and reporting obligations under part XV of the SFO, the Listing Rules and the Takeovers Code to ensure a fair market and to protect investors' interests.

The Securities and Futures Commission of Hong Kong can bring a civil action before the Market Misconduct Tribunal (MMT) for suspected market misconduct or other infringements of the SFO.

Shareholders also have separate statutory rights of action under the SFO through the civil courts (section 281 of the SFO) if the shareholders have suffered financial loss caused by any form of market misconduct. The MMT's findings in relation to market misconduct will be admissible in evidence in a private civil action (section 281 (7) of the SFO). For a shareholder's civil claim to be successful, the court has to be satisfied that it is 'fair, just and reasonable' that compensation should be paid in the circumstances of the case (section 281 (2) of the SFO).

For publicly traded companies, the grounds for shareholders' claims for unfairly prejudicial conduct in an M&A transaction are limited to conduct that is in breach of their legal or equitable rights, or universal expectations of shareholders. However, for privately held companies, in addition to the legal, equitable and universal expectation of shareholders, personal expectations arising from personal relationships or dealings between parties with mutual trust and confidence are generally protected under the Companies Ordinance.

#### Form of transaction

4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

No.

#### Negotiated or hostile transaction

5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No. However, in the case of a hostile or unsolicited takeover offer, under the Companies Ordinance, minority shareholders who do not accept the offer may under certain circumstances have the right to be bought out by the purchaser.

#### Party suffering loss

6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes.

If the loss is suffered by a shareholder, the types of claims available would mostly be unfair prejudice claims or contractual claims for breach of the company's constitutional documents.

Claims for losses suffered by the company itself may be brought by a shareholder in the form of derivative actions, for example, against the directors for breach of their fiduciary duties.

### COLLECTIVE AND DERIVATION LITIGATION

#### Class or collective actions

7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

There is no class or collective action regime in Hong Kong. The only multiparty proceedings regime is the procedure for representative proceedings provided under order 15, rule 12 of the Rules of the High Court, which allows one or more persons to start or continue proceedings as representatives of other persons who have the 'same interest' in the proceedings. However, this mechanism has limited application due to the strict interpretation of the 'same interest' requirement in the Hong Kong Court of Appeal case, *Markt & Co Ltd v Knight Steamship Co Ltd (Markt & Knight)*. In particular, the plaintiffs must prove the existence of the same contract between all plaintiff class members and the defendant; the same defence (if any) pleaded by the defendant

against all the plaintiff class members; and the same relief claimed by the plaintiff class members.

Although some piecemeal judicial initiatives have been taken to relax such requirements, *Markt & Knight* has never been expressly overruled, and it is still the leading case in Hong Kong.

It is also worth noting that a shareholder, when making an unfair prejudice petition, can join other shareholders as respondents.

#### Derivative litigation

8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes.

Shareholders of a company or of an associated company may bring derivative actions under section 732 of the Companies Ordinance if there has been 'misconduct' committed against the company. 'Misconduct' is widely defined under the Companies Ordinance as fraud, negligence, breach of duty or default in compliance with any ordinance or rule of law.

In addition, common law derivative actions can be brought by shareholders where a loss is suffered by the company under circumstances where the company has engaged in conduct that is ultra vires or illegal; or parties that are in control of the company commit a fraud on the company.

### INTERIM RELIEF AND EARLY DISMISSAL

#### Injunctive or other interim relief

9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

The court has a wide discretion under the Companies Ordinance and the Companies (Winding Up and Miscellaneous Provisions) Ordinance to award injunctive or other interim relief on such terms as the court deems appropriate. This extends to M&A transactions.

For example, sections 728 to 729 permit certain persons, including shareholders of a company, to seek an injunction to restrain breaches of the Companies Ordinance, breaches of fiduciary duties by directors or breaches of the company's articles.

The court also has a general power under section 21L of the High Court Ordinance to grant an injunction in all cases where it is 'just and convenient' to do so.

#### Early dismissal of shareholder complaint

10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Yes. There is no distinction between M&A litigation and the usual situations in which summary judgment or strike out may be awarded, albeit a personal shareholder claim could be struck out where the loss being claimed has been suffered by the company rather than the individual shareholder (where the proper procedure would be a derivative action), and vice versa.

Other common grounds for strike out of a shareholder's claim include that the pleading discloses no reasonable cause of action, is scandalous, frivolous or vexatious, or is an abuse of process.

In addition, under section 736 of the Companies Ordinance, in circumstances where statutory derivative proceedings are on foot and the same shareholder or shareholders initiate a common law derivative action in respect of the same cause or matter, the court has the power

to strike out part or the whole of the pleading in relation to the common law claim or to award summary judgment dismissing it.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Yes, shareholders can bring derivative actions, on behalf of the company, against third-party advisers that assist in M&A transactions if the third-party advisers have committed a wrong against the company.

### Claims against counterparties

12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Yes. For example, section 728 of the Companies Ordinance permits claims against parties other than directors in circumstances where:

- a person has engaged in, is engaging in or is proposing to engage in conduct that constituted, constitutes or would constitute:
  - a contravention of the Companies Ordinance;
  - a default relating to a contravention of the Companies Ordinance; or
  - a breach specified in subsection (4) of section 728 of the Companies Ordinance; or
- a person has refused or failed, is refusing or failing, or is proposing to refuse or fail, to do an act or thing that the person is required by the Companies Ordinance to do.

A default for the purposes of this section of the Companies Ordinance is defined as:

- an attempt to contravene the Companies Ordinance;
- aiding, abetting, counselling or procuring another person to contravene the Companies Ordinance;
- inducing or attempting to induce, whether by threats, promises or otherwise, another person to contravene the Companies Ordinance;
- being in any way, directly or indirectly, knowingly concerned in or a party to a contravention of the Companies Ordinance by another person; or
- conspiring with others to contravene the Companies Ordinance.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

It depends on the terms of the relevant constitutional documents. Various versions of model articles are set out in the Companies (Model Articles) Notice.

Under section 468 of the Companies Ordinance, any provision, whether contained in the articles of a company, or in any contract with a company or otherwise, for exempting a director of the company from any liability to the company or an associated company that by virtue of any rule of law would otherwise attach to him or her in respect of any negligence, default, breach of duty or breach of trust of which he or she may be guilty, is void.

### Statutory or regulatory limitations on claims

14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Not specifically, but under the Companies Ordinance, the court may refuse to grant a shareholder leave to bring a derivative claim or to intervene if it is satisfied that:

- in the case of an application for leave to bring proceedings under section 732(1) or (2), the member has, in the exercise of any common law right, brought proceedings on behalf of the company in respect of the same cause or matter; or
- in the case of an application for leave to intervene in proceedings under section 732(3), the member has, in the exercise of any common law right, intervened in the proceedings in question to which the company is a party.

### Common law limitations on claims

15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Yes. The rules laid down in the English case of *Foss v Harbottle* apply in Hong Kong, which impose restrictions on the ability of shareholders to bring claims against board members or executives who committed a wrong to the company. The rules include the proper plaintiff principle and the irregularity principle.

Under the proper plaintiff principle, where directors have breached their duties owed to the company or any person has committed a wrong to the company, the proper plaintiff to bring an action against the wrongdoer is the company save in circumstances where the criteria to bring a derivative action are satisfied.

Under the irregularity principle, shareholders cannot sue to complain of a mere irregularity that can be cured by a vote of the company in a general meeting and where the intention of the majority shareholders is clear.

Apart from the above principles, if shareholders bring a common law derivative claim, the shareholders are also subject to certain restrictions as follows:

- the shareholders must show they have a claim for illegal conduct or acts that are ultra vires, or that there has been a fraud on the company or, less commonly, that it is in the interests of justice;
- only current registered shareholders can bring an action;
- the shareholders must not have engaged in inequitable or unjust conduct; and
- where the majority shareholders acting independently of the wrongdoers and without collateral purpose ratify the wrongdoers' actions, such ratification can effectively prevent a derivative action being brought.

There is, at present, no statutory equivalent in Hong Kong to the US-style 'business judgement rule'.

## STANDARD OF LIABILITY

### General standard

16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

For a director or an executive to be held liable to shareholders in connection with an M&A transaction, the shareholders must prove that on the



balance of probabilities, the director's or executive's conduct infringes the shareholders' personal rights. Shareholders' personal rights can arise pursuant to the company's constitution, common law, a contract or statute. In cases where the conduct of the director or the executive infringes both the company's rights and the shareholders' personal rights, the shareholders' loss should be separate and distinct and not properly regarded as being reflective of the company's loss. In determining whether the shareholders' loss is reflective of the company's loss, the test is whether the loss would be made good if the company was able to recover for its own loss.

If a shareholder wishes to seek remedies under an unfair prejudice action (section 724 of the Companies Ordinance), it must prove that the company's affairs are managed by the wrongdoer in a way that is unfairly prejudicial to the shareholders. The concept of the 'company's affairs' is given wide interpretation, and includes contracts, assets, goodwill, profits and loss, business or trade matters, capital structure, dividend policy, voting rights, and other external activities and internal management.

### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

No. However, infringements of the shareholders' personal rights that can be caused by a director or executive differ based on the specific circumstances of the transaction.

### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

No. A director has a duty in common law to avoid conflicts between his or her personal interests and those of the company. Section 536 of the Companies Ordinance states that if a director of a company has a material interest in a transaction, arrangement or contract, or a proposed transaction, arrangement or contract, with the company, that is significant in relation to the company's business, the director must declare the nature and extent of his or her interest to the other directors.

### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

No. There is no equivalent in Hong Kong to the US-style 'entire fairness rule'.

## INDEMNITIES

### Legal restrictions on indemnities

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Yes. Under section 468 of the Companies Ordinance, if a provision in a company's constitutional documents purports to exempt a director of the company from any liability that would otherwise attach to the director in connection with any negligence, default, breach of duty or breach of trust in relation to the company, the provision is void.

In addition, if, by a provision of a company's constitutional documents the company directly or indirectly provides an indemnity for a director of the company, or a director of an associated company, against any liability attaching to the director in connection with any negligence, default, breach of duty or breach of trust in relation to the company or associated company (as the case may be), the provision is void.

Section 469 of the Companies Ordinance permits a company to indemnify a director against liability incurred by the director to a third party if specified conditions are met. Certain liabilities and costs must not be covered by the indemnity, such as:

- criminal fines;
- penalties imposed by regulatory bodies;
- the defence costs of criminal proceedings where the director is found guilty; and
- the defence costs of civil proceedings brought against the director by or on behalf of the company or an associated company in which the judgment is given against the director.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

Assuming the M&A transaction documents are governed by Hong Kong law and subject to the exclusive jurisdiction of the Hong Kong court, shareholders can challenge particular clauses in the signed transaction documents if the shareholders believe that the execution of the particular clauses is, for example, unfairly prejudicial to the shareholders.

In privately negotiated M&A transactions in Hong Kong, it is not common to see a shareholder challenge particular clauses that, for example, preclude third-party bidders.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

Under the Companies Ordinance, a special resolution (a resolution that is passed by a majority of at least 75 per cent of the shareholders who attend and vote, in person or by proxy, (section 564(1)) is required for important matters such as, but not limited to:

- alteration of the articles of association (section 88(2)(3) of the Companies Ordinance);
- change of the company's name (section 107(1) of the Companies Ordinance);
- reduction of a company's share capital (section 215(1) of the Companies Ordinance);
- an unlisted company buying back its shares (section 244(1)(2) of the Companies Ordinance); and

- pay out of a company's capital in respect of the redemption or buy-back of shares (section 258(1) of the Companies Ordinance).

Furthermore, under section 473 of the Companies Ordinance, shareholders may vote to ratify conduct by a director involving negligence, default, breach of duty or breach of trust in relation to the company.

However, pursuant to section 734 of the Companies Ordinance, this does not prevent a shareholder bringing a derivative action in relation to the ratified conduct, and when considering the derivative action, the court will take into account:

- whether the members were acting for proper purposes, having regard to the company's interests, when they approved or ratified the conduct;
- to what extent those members were connected with the conduct when they approved or ratified the conduct; and
- how well informed about the conduct those members were when they decided whether to approve or ratify the conduct.

**Insurance**

**24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?**

Under section 468(4) of the Companies Ordinance, a company is permitted to take out insurance for its directors for:

- any liability to any person attaching to the director in connection with any negligence, default, breach of duty or breach of trust (except for fraud) in relation to the company or associated company (as the case may be); or
- any liability incurred by the director in defending any proceedings (whether civil or criminal) taken against the director for any negligence, default, breach of duty or breach of trust (including fraud) in relation to the company or associated company (as the case may be).

**Burden of proof**

**25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?**

It depends on who brings the litigation and what remedy is sought. If directors commence the litigation on behalf of the company, the directors have the burden to prove the company's claim. If the shareholders bring a derivative action on behalf of the company or bring a claim for infringement of their personal rights, the shareholders have the burden of proof.

**Pre-litigation tools**

**26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?**

Yes. For example, under section 740 of the Companies Ordinance, upon application to the court by members representing at least 2.5 per cent of the voting rights of all the members who are entitled to vote at the company's general meeting or at least five members of the company, the court may make an order to authorise a person to inspect any record or document of the company if the court satisfies that the application is made in good faith and the inspection is for a proper purpose.

However, according to section 741 of the Companies Ordinance, the authorised person is not allowed to disclose the information obtained to anyone that is not the applicant, without the company's prior written consent, unless stated otherwise by section 741 (3) of the Companies Ordinance (eg, for the purpose of criminal proceedings or for any other requirement under the law).

Under section 41 of the High Court Ordinance and Order 24, Rule 7A of the Rules of the High Court, a shareholder may apply for a pre-action disclosure order against board members or executives of the company, if the shareholder can prove that: (i) the shareholder is likely to be a party to subsequent proceedings; (ii) the person against whom the order is sought is likely to be a party to subsequent proceedings; and (iii) such person is likely to have or to have had in his or her possession, custody or power any relevant documents.

**Forum**

**27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?**

No.

**Expedited proceedings and discovery**

**28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?**

A court may expedite proceedings to resolve certain issues quickly, and particularly in the context where an injunction is granted to delay closing, in the same way as it would with any type of civil claim.

Common discovery issues arise in relation to access to the transactional documents and due diligence as to the parties to the transactions and relevant third parties.

**DAMAGES AND SETTLEMENTS**

**Damages**

**29 | How are damages calculated in M&A litigation in your jurisdiction?**

There are no special rules in Hong Kong regarding calculation of damages in M&A litigation. The normal rules as to the calculation of damages apply, including the principles of remoteness.

However, there are various mechanisms, in relation to post-closing claims, for quantifying adjustments to the purchase price based on value, such as discounted cash flow or net asset value.

**Settlements**

**30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?**

There are no special issues in Hong Kong with respect to settling shareholder M&A litigation.

**THIRD PARTIES**

**Third parties preventing transactions**

**31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?**

Third parties may seek injunctive relief to break up or stop agreed M&A transactions prior to closing if they have an underlying cause of action either in tort or contract, or pursuant to statute.

However, litigation without a cause of action issued for the sole purpose of creating pressure would be at risk of being struck out for abuse of process.

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Specific performance is an available remedy in Hong Kong and can be used to compel parties to perform their obligations, including proceeding with a transaction.

However, as above, litigation without a cause of action issued for the sole purpose of creating pressure would be at risk of being struck out for abuse of process.

### UNSOLICITED OR UNWANTED PROPOSALS

#### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

In Hong Kong, directors' fiduciary duties mainly arise from common law, which include the following duties:

- to act in good faith in the interests of the company;
- to exercise powers for proper purposes;
- to avoid conflicts of interests;
- not to make secret profits; and
- not to misappropriate company assets.

In addition, the directors also have a statutory duty to exercise due care, skill and diligence under section 465 of the Companies Ordinance.

Therefore, when directors consider an unsolicited or unwanted proposal, the directors must comply with their fiduciary duties.

There are situations where directors attempt to defeat takeover offers by entering into agreements that are triggered upon a takeover offer and that might make it prohibitively expensive or otherwise unattractive for an offeror to proceed (the 'poison pill' arrangement), or an agreement involving the disposal of the company's major assets (the 'sale of the crown jewels'). In such case, whether the directors have breached their fiduciary duties depends on the specific circumstances. If, for example, it is clear that the directors' purpose of refusing an unsolicited M&A proposal is simply to preserve their positions in the company, then it may amount to a breach of duty.

For public companies, the directors must also comply with the Takeovers Code. Under general principle 9, directors of a target company cannot, without general meeting approval, take action in relation to the affairs of the company that could effectively result in any bona fide offer being frustrated or shareholders being denied a chance to decide its merit. However, for private companies, as the articles must impose restrictions on the right of shareholders to transfer shares, the directors are justified to ensure that the identities of shareholders are consistent with the company's interests. As such, the directors of private companies may be given more latitude in determining whether an M&A proposal should be carried forward or defeated.

### COUNTERPARTIES' CLAIMS

#### Common types of claim

#### 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

The claims differ depending on the stage of the M&A transaction.

Before the M&A agreement has been signed, disputes that concern the behaviour of contractual parties could include breaches of pre-signing confidentiality or exclusivity provisions; or breaches of letters



#### Chris Dobby

chris.dobby@hoganlovells.com

#### Grace Zhu

grace.zhu@hoganlovells.com

11th Floor, One Pacific Place  
88 Queensway  
Hong Kong  
Tel: +852 2840 5629/5605  
Fax: +852 2219 0222  
www.hoganlovells.com

of intention (LOIs) (these often involve the issue of whether and to what extent the LOI is binding, and if the LOI is not binding, whether there are any pre-contractual obligations deriving from the LOI).

After signing the M&A agreement, most of the claims are based on the terms and conditions of the agreement, which include:

- conditions precedent not being met before closing;
- breaches of covenants;
- breaches of representations and warranties;
- disputes regarding due diligence and the disclosure letter;
- disputes regarding post-closing price adjustments; or
- disagreements regarding the earn-out adjustments.

#### Differences from litigation brought by shareholders

#### 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between parties to M&A transactions most commonly occurs post-closing. This includes claims for breach of the transactional documents and misrepresentation claims.

Litigation brought by shareholders is usually pre-closing, and aimed at protecting shareholder interests either through direct claims or claims in the name of the company.

# India

Naresh Thacker and Bhavin Gada

Economic Laws Practice

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

Shareholders can make the following claims and seek remedies in the following situations.

#### Oppression, mismanagement and prejudicial conduct

Shareholders may proceed against other shareholders (usually majority shareholders or promoters), directors and officers in default to seek to establish that the affairs of the company are being conducted in a manner prejudicial or oppressive to the aggrieved shareholders, or prejudicial to the company or public interest, or to both.

#### Class or derivative actions

A prescribed number of members can initiate an action on behalf of the members if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members.

#### Breaches of contract

Contractual relationships between the shareholders arise either out of separate agreements or through the articles of association, which in themselves are considered to be a contract between the company and the shareholders. In the case of unlisted companies, a company may enter into contracts under which certain special rights are given to the shareholders (usually private equity investors):

- affirmative voting rights;
- shareholder lock-in rights;
- pre-emptive rights;
- rights of first offer or refusal; or
- any similar or other rights.

In the alternative, rights can be enshrined in the articles of association (which can be in addition to any separate contractual arrangement that such companies have). Violation of these rights gives rise to breach of contract, and the aggrieved party may claim damages. Additionally, if the contractual arrangement specifically records indemnity provisions, the aggrieved party can also claim the said indemnity.

#### Acts of misconduct

Where an M&A transaction involves misconduct on the part of directors or officers – for example, where directors have not complied with their fiduciary duties, or such M&A transaction is the result of a director's conflict of interest or fraudulent act – the Companies Act, 2013 (Companies Act) has specifically provided for various statutory duties

upon the directors, the breach of which could lead to action being initiated against them under the relevant provisions of the Companies Act.

#### Breaches of statutory duties and obligations

Where an M&A transaction results in breach of statutory duties and obligations by corporations, officers and directors, it could take the form of non-compliance with the statutory prerequisites, resulting in action being initiated against them under the relevant provisions of the Companies Act. For example:

- mergers and amalgamations require the approval of the shareholders (including creditors, debenture holders and statutory authorities, as may be applicable) under the Companies Act: that is, 75 per cent of the shareholders in value involved in a company are required to approve actions such as a merger of a company. The Companies Act has statutorily recognised that any objection to a compromise or arrangement shall be made only by persons holding not less than 10 per cent of the shareholding; and
- for the sale of substantial assets of a public company, whether listed or unlisted, the board of directors cannot exercise such power unless it has the approval of the shareholders of the company by passing a special resolution, that is, by a 75 per cent majority.

#### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

#### Applicable thresholds

An application for relief of oppression and mismanagement can be made in the case of a company having a share capital, not less than 100 members of the company or not less than one-tenth of the total number of its members, whichever is less, or any member or members holding not less than one-tenth of the issued share capital of the company. In the case of a company not having a share capital, then not less than one-fifth of the total number of its members are required to maintain such an action. An action for relief of oppression and mismanagement is required to be filed before the relevant national company law tribunal (NCLT). An NCLT, in its discretion as per the facts and circumstances of a case, is also empowered to waive such threshold if an application is made to it in this behalf, so as to enable the members to apply.

For the initiation of a class action, in the case of a company having a share capital, there should be at least 100 members of the company or not less than such percentage of the total number of its members as may be prescribed (as on date there is no such number prescribed), whichever is less, or any member or members holding not less than such percentage of the issued share capital of the company as may be prescribed (as on date there is no such number prescribed). In the case of a company not having a share capital, not less than one-fifth of the total number of its members is entitled to initiate class action.

## Grounds

Depending on the nature of the claim, the grounds of the claim would need to be established in the following manner:

- for making a case of oppression and mismanagement, it is essential to show that the affairs of the company have been or are being conducted in a manner:
  - prejudicial to the public interest;
  - prejudicial or oppressive to the aggrieved shareholders or any other member or members; or
  - prejudicial to the interests of the company;
- that there has occurred a material change in the management or control of the company that is not a change brought about by or in the interests of any creditors, including debenture holders or any class of shareholders of the company; and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests, or to its members or any class of members; and
- in a class action claim, it is essential to show that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members.

## Non-compliance with statutory duties and obligations

Facts establishing the non-compliance would be required. Where the shareholders are proceeding against directors or officers, depending on statutes, and where an act or omission was caused by the consent or connivance of the relevant directors or officers, this would entitle the shareholders to proceed against specific directors or officers. The Companies Act recognises that the officers in default (which includes various categories of persons, such as key managerial personnel and the de facto controller of the company) could be held liable for acts or omissions committed therein.

## Remedies in contractual disputes

The shareholders would have to establish the breach complained of, and the damages or losses they may suffer by reason of such breach of contract. For injunctions as an interim remedy, the shareholders would have to establish that they have a prima facie case against the company or other shareholders, that their rights would be irrevocably prejudiced if the action complained of is allowed to take place and that the balance of convenience lies in their favour. In the case of a claim for indemnity, the terms of the indemnity provision will govern such claim.

## Publicly traded or privately held corporations

- 3 | Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes. In addition to claims (as mentioned in question 1) with respect to publicly traded corporations, the Securities and Exchange Board of India (SEBI), the Indian securities regulator, has issued several regulations for listed companies the breach of which could result in statutory actions being initiated by the regulator itself or by the aggrieved party. These regulations include:

- the SEBI (Prohibition of Insider Trading) Regulations, 2015, which, inter alia, prohibit the sharing of unpublished price-sensitive information (whether or not in conjunction with the trading of shares) and are geared towards levelling information asymmetry in the market;
- the SEBI (Substantial Acquisitions and Takeovers) Regulations 2011, which require shareholders acquiring a certain percentage of shares or control in a listed company to make an open offer to acquire the shares of other shareholders who are not party to such arrangement due to which the open offer was triggered;

- where the acquisition would result in delisting, the dissenting shareholders have the right to seek an exit from the promoters of the company in accordance with the provisions of the SEBI (Delisting of Equity Shares) Regulations 2009; and
- additionally, the SEBI has also mandated that listed companies making disclosures in relation to their material transactions follow certain corporate governance norms and obtain relevant approvals under the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015. These norms include the formation of a stakeholders' grievance committee that is required to address shareholders' grievances in a time-bound manner, failing which the shareholders may approach the SEBI or the stock exchange where the shares of such companies are listed.

In view of the above, shareholders (or any other stakeholders) may approach or file complaints with the SEBI or a stock exchange in the event that the company, or promoters, directors or other officers, have not complied with the aforementioned legislation.

## Form of transaction

- 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

See questions 1 to 3. Remedies before the NCLT or the civil courts may arise depending upon the nature of a transaction, as per the provisions explained above.

## Negotiated or hostile transaction

- 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

In a negotiated transaction, counterparties to the M&A transaction can bring claims for breach of contract and for breach of covenants or representations and warranties, and can seek indemnities (if provided for).

In the case of a hostile or unsolicited offer, in the event of non-compliance with the various regulations mentioned in question 3, an aggrieved shareholder of a listed company can seek remedy as mentioned therein.

## Party suffering loss

- 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes, different claims will lie depending upon who has suffered the loss. For further details, see questions 1 and 2.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

- 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Yes, a class or derivate action claim can be pursued. The requirements with respect to these are explained in question 1.

### Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

No. There is no provision under the Companies Act that entitles a shareholder to bring derivative actions on behalf of or in the name of the

company. The Companies Act permits a shareholder to initiate class action proceedings only on behalf of the members or depositors of the company.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Courts in India have the discretion to award injunctive relief to prevent the closing of an M&A transaction if the company or its shareholders are able to establish that the proposed M&A transaction affects the rights of the company or its shareholders. For an interim injunction, the shareholders would need to establish that there is a prima facie case in their favour, that they would suffer irreparable harm if the transaction went through without deciding their rights and that the balance of convenience lies in their favour. While courts can prevent an M&A transaction from closing if it affects the rights of the company or its shareholders, a court cannot rewrite a contract, and therefore cannot interfere with or modify deal terms.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Yes. The grounds on which an early dismissal may be sought are non-compliance with the minimum applicable threshold for filing the proceedings; the applicability of a period of limitations to initiate the action; and the existence and availability of an alternative remedy.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

### Claims in a class or derivative action

Shareholders can bring a class action seeking damages or compensation or another other suitable action from or against:

- the auditor, including the audit firm of the company, for any improper or misleading statement of particulars made in its audit report, or for any fraudulent, unlawful or wrongful act or conduct; or
- any expert, adviser, consultant or any other person for any incorrect or misleading statement made to the company, or for any fraudulent, unlawful or wrongful act or conduct, or any likely act or conduct on his or her part.

### Claims before governing bodies

Shareholders may also make complaints to the bodies that govern such advisers (such as the Bar Council in the case of legal advisers or the Institute of Chartered Accountants India).

### Claims in the case of listed companies

Shareholders may complain to the SEBI or a stock exchange that merchant bankers and other intermediaries have not followed the requisite code of conduct.

## Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Unless there is a privity of contract between such parties, no proceedings can be initiated in relation to an M&A transaction.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

The Companies Act imposes various duties on directors and key managerial personnel breach of which could result in an action being initiated against an officer in default under the relevant provisions of the Companies Act.

### Statutory or regulatory limitations on claims

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

As per the provisions of the Companies Act, any objection to a compromise or arrangement shall be made only by persons holding not less than 10 per cent of the shareholding. In addition to this, a shareholder can initiate proceedings for oppression or mismanagement subject to the condition that the applicant has paid all calls and other sums due on his or her shares.

### Common law limitations on claims

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

There is no such common law rule impairing the rights of shareholders to bring such claims.

## STANDARD OF LIABILITY

### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Depending upon the remedy being sought, a board member or executive could be held liable if his or her involvement in the said wrong is demonstrated. For example, in a case of oppression and mismanagement, an NCLT is empowered to terminate, set aside or modify any agreement, howsoever arrived at, between the company and the managing director, any other director or manager, if in the opinion of the NCLT it is just and equitable in the circumstances of the case. Similarly, in the case of a class action, regarding the role and involvement of a director, a claim could be made for damages or compensation, or any other suitable action from or against the company or its directors, for any fraudulent, unlawful or wrongful act or omission or conduct, or any likely act or omission or conduct on their part.

**Type of transaction**

17 | Does the standard vary depending on the type of transaction at issue?

No, the standard does not vary depending on the type of transaction.

**Type of consideration**

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No, the standard does not vary depending on the type of consideration being paid to the seller's shareholders.

**Potential conflicts of interest**

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

**Statutory duty**

The Companies Act sets out the duties of directors, under which a director of a company is prohibited from involving him or herself in a situation in which he or she may have a direct or indirect interest that conflicts with the interest of the company.

**Director's interest**

If a director who holds more than a 2 per cent shareholding in another company with which the company seeks to enter into a transaction fails to so disclose his or her interest, the transaction is voidable at the option of the company, and such director is liable to pay a fine as well as imprisonment.

**Controlling shareholders**

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared ratably with all shareholders?

The standard does not vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared ratably with all shareholders.

**INDEMNITIES****Legal restrictions on indemnities**

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Under the Companies Act, there is no restriction on the company's ability to indemnify its officers and directors. A company may procure directors' and officers' insurance cover to indemnify them against any liability in respect of any negligence, default, misfeasance, breach of duty or breach of trust for which they may be guilty in relation to the company.

**M&A CLAUSES AND TERMS****Challenges to particular terms**

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

If a shareholder had a right pursuant to which his or her prior consent or approval had to be sought for any agreement that a company may

enter into, and if such consent or approval has not been obtained, the aggrieved shareholder may challenge the terms of an M&A document.

**PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION****Shareholder vote**

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

Under the Companies Act, there is no provision enabling a shareholder to vote on M&A litigation. Any such power of a shareholder to cast a vote would have to be contained in the constitution documents of the company pursuant to a shareholders' agreement (the breach of which would entitle the shareholders to sue or initiate arbitration for breach of contract). Decisions with respect to the initiation and defence of an M&A litigation would typically be made by the directors of the company.

**Insurance**

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

As discussed above, such insurance is common, and usually covers the liability of the directors and officers in question, including in relation to M&A transactions.

**Burden of proof**

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The burden of proof lies on the party asserting a claim. Therefore, initially such burden of proof would lie with the person initiating proceedings or making a claim, and if there are any counterclaims or defences specifically taken up by the counterparty, then such counterparty would be required to establish the same.

**Pre-litigation tools**

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

There is a statutory right to inspect:

- annual returns;
- registers of members;
- the minutes of shareholders' meetings;
- financial statements;
- the register of directors and key managerial personnel;
- the register of loans and guarantees;
- the register of contracts and arrangements in which directors are interested; and
- the contracts of employment of the managing director and full-time directors.

**Forum**

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Under the Companies Act, the following, inter alia, are required to be heard by the NCLT in whose jurisdiction the registered office of the company is located:

- legal proceedings concerning mergers;
- demergers;

- amalgamations;
- windings-up;
- reductions of capital;
- oppression and mismanagement; and
- class actions.

For example, NCLT Mumbai will have jurisdiction to hear proceedings against a company that is registered within the state of Maharashtra and NCLT Ahmedabad will have jurisdiction over a company that is registered within the state of Gujarat.

With respect to legal proceedings arising out of a breach of contract, the jurisdiction of the civil court may be determined, inter alia, on the basis of where the cause of action has arisen. If the contract in respect of which a breach is alleged contains an arbitration clause, then the same will have to be heard by an arbitral tribunal, with the seat of the arbitral tribunal being determined by the terms of the contract.

### Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

There is no such provision for expedited proceedings and discovery in M&A litigation.

The Companies Act requires NCLTs to endeavour to dispose of matters within three months from the date of their being filed. In the event that an NCLT is unable to conclude the hearings within the aforesaid time frame, the president or chairperson of the NCLT is empowered to grant an extension of a further period not exceeding 90 days.

With respect to shareholder disputes, the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act 2015, requires the high courts to endeavour to dispose of the proceedings in a far more efficient manner by providing strict time-lines to ensure expeditious disposal of the proceedings. For example, defendants are now required to file their statement of defence or written statement within 120 days, after which the said right is forfeited.

When dealing with the stage of discovery of documents, the Code of Civil Procedure 1908, requires the parties to ensure that a list of all documents and photocopies thereof are filed at the stage of the filing of the plaint or the written statement itself. In this regard, one of the most common issues faced by parties in discovery is the requirement to obtain the leave of the court to produce a document that was not originally filed at the time of instituting the suit. Grant of such leave is entirely discretionary in nature and is subject to costs.

## DAMAGES AND SETTLEMENTS

### Damages

29 | How are damages calculated in M&A litigation in your jurisdiction?

The grant of damages for breach of contractual obligations is, inter alia, governed by the Indian Contract Act 1872 (the Contract Act).

Parties may contractually provide for the payment of damages in the event of a breach of contract. Such damages are granted only if the courts find the sum in question (not exceeding the amount of liquidated damages mentioned in the contract) to be a genuine pre-estimate of the damages. If not then the court will only grant reasonable compensation. In making a claim for liquidated damages, proof of loss or damage is imperative, except in circumstances when damage or loss is difficult or impossible to prove.

### Settlements

30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

The settlement of disputes arising out of a contract is a matter of private negotiation between the parties. On reaching a settlement, the parties are required to record the terms of their settlement and produce the same before the civil court. While doing so, the parties provide undertakings to the court with respect to their compliance with their respective obligations under the consent terms. These undertakings are recorded by the court and the proceedings are accordingly disposed of in terms of a settlement arrived at between the parties.

With respect to any proceedings filed before the NCLT, if the parties amicably settle the same before the first hearing of the matter, then the NCLT Rules, 2016, require the applicant to seek permission from the NCLT for withdrawal of the case. Such withdrawal may be granted, subject to the payment of costs, at the discretion of the NCLT.

## THIRD PARTIES

### Third parties preventing transactions

31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

### Interest in property

Third parties can bring litigation to break up or stop an agreed M&A transaction if such third party's interest is adversely affected.

### Contractual breach

If there is any contract with such third party that is being breached by such M&A transaction, the third party can intervene.

### Regulatory proceedings

If the acquisition involves regulatory proceedings, for example at the NCLT for a merger (which requires public notice) or the Competition Commission of India for combinations, third parties can intervene by objecting to the transfer.

### Third parties supporting transactions

32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Unless there is a specific contract, third parties cannot pressure a company to enter into an M&A transaction. Where there is a contract, a suit for specific performance could arise from this.

Further, where the government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the government may, by order, provide for the amalgamation of those companies into a single company with such constitution, such property, powers, rights, interests, authorities and privileges, and such liabilities, duties and obligations as may be specified in the order.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

The Companies Act imposes various duties on directors. For example, they should exercise their duties with due and reasonable care, and skill and diligence, and they shall exercise independent judgment. Similarly, they should not be involved in a situation in which they may have a



direct or indirect interest that conflicts, or that possibly may conflict, with the interests of the company. Such duties may require them to proactively disclose any unsolicited or unwanted proposals to the board of directors.

## COUNTERPARTIES' CLAIMS

### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

Commonly, counterparties to an M&A transaction assert claims for breach of statutory provisions, breach of representations and warranties, indemnities and purchase price adjustments, depending on the criteria set out in the contract.

### Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between parties to an M&A transaction usually arises from the contract entered into between the parties (ie, breach of contract, breach of representations and warranties). Parties to an M&A transaction would have to institute a suit or an arbitration for damages or specific performance.

On the other hand, litigation brought by shareholders would be in the nature of oppression and mismanagement or a class action on the ground that the affairs of the company are being conducted in a manner prejudicial to the company, its shareholders, or both. Remedies may also be sought against the management.



Naresh Thacker  
nareshthacker@elp-in.com

Bhavin Gada  
bhavingada@elp-in.com

109A, 1st Floor  
Dalamal Towers, A Wing  
Free Press Journal Road  
Nariman Point  
Mumbai 400 021  
India  
Tel: +91 22 6636 7000/+91 90 0467 5224  
Fax: +91 22 6636 7172  
www.elplaw.in

# Italy

Andrea Atteritano, Francesca Rolla and Emanuele Ferrara

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The main claims that shareholders can bring in connection with M&A transactions are as follows:

- Shareholders are entitled to challenge the resolutions of the shareholders' meeting and the board of directors resolving on the relevant transaction, provided that the resolution is in breach of the law or by-laws and, as far as a resolution of the shareholders' meeting is concerned, the shareholders have not voted in favour (or, under certain limited conditions, independently from their consent). Under certain circumstances, shareholders are entitled to challenge resolutions only if they possess a certain amount of the corporate capital. In the absence of such requirement, shareholders are entitled only to seek compensation.
- With regard to merger transactions, shareholders are entitled to challenge the merger, by no later than the filing of the deed of merger with the companies' register, if the merger causes them damages. After filing, pursuant to article 2504-bis and 2504-quater Italian Civil Code (ICC), the merger is effective, and shareholders, as well as other possibly injured third parties, can only seek compensation for losses deriving from the merger. In this latter case, the corporation is directly responsible for the losses suffered by the shareholders (or by third parties).
- Shareholders, individually or on behalf of the company, are entitled to claim liability of directors, statutory auditors, or both, for violation of their duties arising from the law or by-laws.

In more general terms, shareholders can also activate control procedures over directors' acts or omissions that are possibly unlawful as follows: internally, by referring the same acts or omissions to the statutory auditors; or externally, by referring the same acts or omissions to the competent state court, which can, inter alia, appoint a judicial director also having the power to bring liability claims against directors (article 2409 ICC).

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

For each of the claims outlined in question 1, the shareholders shall demonstrate the following elements.

### Challenge to resolutions

Shareholders shall demonstrate that the resolution is invalid (in violation of the law or by-laws) and, as far as a resolution of the shareholders' meeting is concerned, that they have not voted in favour. For joint-stock companies, shareholders shall also demonstrate pursuant to article 2378 ICC that they possess shares representing at least 1/1,000 of the corporate capital for publicly traded companies, or 5/100 for privately held companies.

### Challenge to mergers

This requires the occurrence (and satisfactory evidence) of one of the following circumstances:

- violation of the ICC rules governing the merger (articles 2501 et seq ICC);
- invalidity of a shareholders' or board of directors' resolution of one of the companies involved in the merger (eg, violation of shareholders' voting rights; breach of the shareholders' right to be fully informed; or an unreasonable share exchange ratio); or
- invalidity of the deed of merger.

After filing the deed of merger with the companies' register, the merger can no longer be challenged, but, pursuant to 2504-quater (2) ICC, shareholders can still bring compensation claims against the company, which, according to some case law, is directly liable for all acts and omissions of its corporate bodies. In this case, shareholders shall essentially:

- allege the occurrence of one of the circumstances above (the company is indeed burdened to prove that no violation of the ICC rules, or invalidity of the shareholders' or board of directors' resolution or of the deed of merger occurred); and
- prove the damage individually suffered in connection with the merger (ie, independently from the possible damage that the company that they are shareholders in has possibly suffered).

According to the same case law, since the company is directly liable for its corporate bodies, the shareholders are not required to specifically demonstrate the negligence or wilful misconduct of its directors.

### Directors' liability

Irrespective of, and independently from, any action against the company, the directors may still be held liable by shareholders for their wilful misconduct or negligence pursuant to article 2395 ICC. In this respect, to bring a successful claim, shareholders shall demonstrate: the negligence or wilful misconduct of the directors; the damage individually suffered (ie, not as a consequence of the loss suffered by the company); and causation between the directors' unlawful behaviour and the shareholders' loss.

The claim may be brought against directors who are still in office, as well as against those who are no longer in office. Third parties (for instance, former shareholders) can waive their right to start legal action against the directors of a company.

### Publicly traded or privately held corporations

- 3 | Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

In general terms, publicly traded corporations are subject to specific rules and disclosure obligations on price-sensitive information (material acquisition, capital increases, mergers and demergers, divestment of material assets, etc). The National Commission for Companies and the Stock Exchange (CONSOB) is the regulatory authority that supervises transactions (including tender offers and mergers) involving Italian publicly traded companies.

For instance, in the case of merger, the expert who is responsible for rendering its opinion on the fairness of the exchange ratio of shares and quotas has to be chosen and appointed among audit firms that are subject to the supervision of CONSOB. Violation of such specific rules may entail invalidity of the resolutions and deeds underlying the transaction and, to this extent, these rules may be relevant to claims that shareholders can bring.

As for tender offers, Italian law is detailed, and further types of claims may be raised under the relevant law provisions. For instance, Italian Financial Law (TUF) provides, inter alia, that an entity which becomes the owner of certain thresholds of voting shares of an Italian listed company shall launch a mandatory tender offer; and shareholders have the right to sell their shares if a bidder, as a result of a mandatory or voluntary tender offer, ends up owning certain thresholds of voting shares.

Violation of such provisions may entitle relevant shareholders to raise further claims.

### Form of transaction

- 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

The types of claims that shareholders can bring may differ depending on the form of the transaction.

While certain claims may be relevant to any transaction (such as the challenge of resolutions or liability claims against directors and officers), others may be brought only in the context of specific transactions, such as the challenge of a merger or a liability claim against experts who rendered a fairness opinion in the context of a merger (see further question 11).

### Negotiated or hostile transaction

- 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

The types of claims that shareholders can bring may vary on the basis of the nature of the transaction (ie, a negotiated transaction versus a hostile or unsolicited offer).

While, in a negotiated transaction, the claims shareholders may raise are those already outlined in question 1, further types of claims may be brought in connection with hostile or unsolicited offers. The specific discipline concerning these additional claims is set out within the TUF and is mainly focused on the 'passivity rule', whereby directors of Italian companies that are target of an unsolicited offer shall refrain from undertaking strategies that would jeopardise the action of the bidder unless such defensive strategies are expressly authorised by the shareholders' meeting or provided by the company by-laws or articles of association.

The responsibility of directors towards the company is provided for in cases of non-compliance with such duty.

### Party suffering loss

- 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

With regard to liability claims against directors, the nature of such liability – contractual or tortious – depends on whether the loss is suffered by the corporation or the shareholders. The different nature of the responsibility entails significant differences in the allocation of the burden of proof and different statutes of limitations apply.

Indeed, when the corporation seeks directors' liability, the liability is contractual in nature, and this means that the plaintiff (the company or, for instance, shareholders acting on its behalf) is required to:

- allege that directors have breached the duties established by the law or by-laws, including the duties of loyalty, fairness and diligence (the directors have the burden to demonstrate that they fulfilled their duties);
- prove the damage suffered by the company; and
- demonstrate the causal nexus between such violation and the damage.

The claim can be raised within five years of the termination of the director's mandate.

However, when the shareholders individually seek directors' liability, according to certain case law, the liability is tortious in nature and, as a consequence, the plaintiff is required to prove the directors' negligence or wilful misconduct; the damage individually suffered (not as a consequence of the loss suffered by the company); and causation between the directors' unlawful behaviour and the shareholders' loss. The claim for damages can be raised within five years of the moment in which the unlawful behaviour occurred.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

- 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Pursuant to article 140-bis Legislative Decree No. 206/2005, class actions can be initiated only by consumers, and shareholders are not included in that definition. It follows that it is upon each individual shareholder to raise a claim for damage compensation.

Nevertheless, to some limited extent and under certain circumstances, shareholders may raise claims collectively. For instance, if corporate by-laws provide for the issuance of saving shares, the representative of the holders of such kind of shares may challenge resolutions of the shareholders' meeting and request the judge to ascertain and declare that shareholders have suffered a loss. In any case, even if it is ascertained and declared that damage occurred, the shareholders will have to then individually seek compensation.

### Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Shareholders are entitled to pursue compensation claims on behalf of the company in cases where the damage suffered by the company is attributable to the negligence or wilful misconduct of the directors in the management of the company and, therefore, also in the context of an M&A transaction.

Shareholders' right to bring liability claims against directors is provided for by the ICC both for joint-stock corporations (article 2393

ICC) and limited liability companies (article 2476 ICC), and has to be exercised within five years from the termination of the manager's mandate.

More specifically, for limited liability companies, the action can also be brought by a single shareholder.

As for joint-stock corporations, the claim can be raised by:

- (i) the shareholders' meeting;
- (ii) the statutory auditors (resolving with a majority of two-thirds of all statutory auditors);
- (iii) one-fifth of shareholders (but the minimum threshold can be differently set up to one-third by corporate by-laws) in the case of private companies; or
- (iv) one-fortieth of shareholders (but corporate by-laws can provide for a lower threshold) if the company is publicly held.

In cases (i) and (ii), board members, executives or directors involved are automatically removed from their role if the action is resolved by at least one-fifth of the shareholders.

In addition, the liability claim against directors can be initiated by the director appointed by the court pursuant to the procedure provided for by article 2409 ICC (see question 1).

If the claim is upheld by the judicial authority or is amicably settled, any damage compensation shall be paid to the company. Legal costs shall be reimbursed to the shareholders, up to the amount of legal costs awarded or agreed.

With reference to a situation where a claim is brought by one company against another company that is a party to an M&A transaction, such action may be initiated only by the company's representatives, and shareholders may only subsequently intervene in the proceedings should they wish to support or object to the company's claim.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Article 2378 ICC establishes that shareholders may challenge resolutions (possibly resolving on an M&A transaction) in breach of the law or corporate by-laws. Resolutions can be challenged by shareholders who own shares with voting rights representing, on aggregate, at least 1 per 1,000 of the share capital for companies resorting to risk capital; and 5 per cent in other cases.

The by-laws may reduce or exclude such a requirement.

Together with the claim, plaintiffs can also request the judge to issue an interim order suspending the effectiveness of the resolution, which could also be sought (and granted) *ante causam*. In such a case, plaintiffs need to prove that their claim is *prima facie* grounded and that there is a risk of damage in case the interim relief is not granted. In any case, the order of suspension may be revoked by the court during the merit proceedings relating to the validity of the resolution.

Under article 2504-quater ICC, a merger cannot be challenged once the deed of merger is filed with the companies' register. However, shareholders may in principle ask the judge to issue a temporary order preventing the shareholders' meeting or the board of directors from resolving upon the merger. Pursuant to article 700 Italian Code of Civil Procedure (ICCP), the shareholders shall demonstrate the risk that irreparable damage will occur in the case of a merger and the *prima facie* groundedness of the claim.

Regarding the possibility for third parties to prevent the closing of M&A transactions, see question 31.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

No disclosure or discovery applies under Italian procedural law.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Pursuant to article 2501-sexies ICC, if the shareholders are not unanimously resolved to the contrary, each of the companies involved in a merger transaction is compelled to seek a third-party adviser (registered in a dedicated public roster) to provide a report on the fairness of the exchange ratio of shares and quotas and the criterion adopted for its calculation. Article 2501-sexies(6) ICC also establishes the liability of advisers in relation to companies, shareholders and third parties for damage caused in connection with the report. Shareholders will have to prove, *inter alia*, that in preparing the report, the advisers acted contrary to the duties of care and due diligence. The advisers, on the other hand, will have to provide evidence, *inter alia*, that any misstatement cannot be attributed to their work of audit. Under certain circumstances, misstatements may be qualified as criminal offences.

Any other consultancy provided to any of the parties that falls outwith the scope of article 2501-sexies is subject to the ordinary rules governing professional services contracts.

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

No specific provisions under Italian law confer upon shareholders the power to sue the counterparties to M&A transactions. Generally speaking, such an action would be probably dismissed for lack of shareholders' standing, given that the parties to the transaction are the only ones entitled to raise a claim for non-compliance.

In any case, under general rules for civil liability, it cannot be excluded that one party may be found liable for having contributed to the breach of a contractual obligation binding another party or to the causation of damages. To this limited extent, the possibility that shareholders bring claims against the counterparties to M&A transactions could in principle be envisaged.

As an example, pursuant to article 2395 ICC, directors are personally responsible towards shareholders for their harmful conducts (see question 6): shareholders could bring claims against counterparties if they prove counterparties directly caused the directors to act with negligence or wilful misconduct.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

First, corporation documents (articles of association, by-laws, etc) are subject to the general rules applicable to contracts. Specifically, article 1229 ICC provides that any agreement aimed at limiting or excluding (in advance) liability for wilful misconduct and gross negligence, or in relation to acts amounting to violations of public policy, is null and void.

Second, the board of directors or by-laws may confer upon one or more of its directors, or upon a managing board, the power to perform certain functions. In this case, the other members of the board of directors are not liable for acts committed by the delegated members unless they are aware of the possible damage and fail to take any countermeasure. Furthermore, directors are not liable if, in the absence of any fault attributable to them, their dissent is recorded in the minutes of the board of directors and they have informed statutory auditors of the relevant facts.

### Statutory or regulatory limitations on claims

- 14 Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Italian law does not provide for any statutory or regulatory limit to shareholders' ability to bring claims against directors and officers in connection with M&A transactions.

### Common law limitations on claims

- 15 Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Italian scholars and case law accept and uphold the 'business judgement rule' (recently, Supreme Court, 22 June 2017, No. 15470). Accordingly, courts can potentially only assess whether members of the board of directors complied with the applicable law, by-laws and obligations of due diligence and fair dealing, and that no conflict of interests occurred (see question 16); they cannot assess the economic opportunity and convenience of management's choices as discretionary in nature, provided that they do not contravene the above-mentioned provisions and duties.

## STANDARD OF LIABILITY

### General standard

- 16 What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Board members and executives must act in the best interest of the company, in compliance with all the obligations set out by the law and the company's by-laws, which shall be carried out 'with the diligence required by the nature of the office and their specific competences'. Such general duty of diligence and care applies to M&A transactions as well.

In the case of a failure to fulfil their duties, directors may be held liable for the damage resulting from their actions or omissions towards the company, the company's creditors, and shareholders or third parties.

The extent of directors' responsibilities and the standard of care required for each director may vary depending on the director's specific expertise. In general terms, however, to bring a successful claim, a damaged party shall demonstrate that the director did not perform his or her duties in good faith; undertake all the proper procedural steps before taking the business decision; and handle the situation with the care that an ordinarily prudent person in a similar position would have used under comparable circumstances.

The above-mentioned duties apply also when an insolvency procedure is opened: directors are open to criminal liability if they commit offences either during insolvency proceedings or in the period before a company is declared insolvent, under certain specific circumstances.

### Type of transaction

- 17 Does the standard vary depending on the type of transaction at issue?

The nature of the relevant transaction does not affect the standard for determining whether a board member or executive may be held liable to shareholders.

The business judgement rule mentioned in question 15 is a flexible standard that applies to any transaction (and, more generally, to any business decision) undertaken by directors, who will be held liable only in cases of failure to meet their duty of care and diligence.

### Type of consideration

- 18 Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

The consideration being paid to the seller does not affect the standard for determining whether a board member or executive may be held liable to shareholders.

The business judgement rule applies to any transaction (and, more generally, to any business decision) undertaken by directors (see questions 15, 16 and 17).

### Potential conflicts of interest

- 19 Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

In general terms, boards of directors have to act in the company's best interests. Therefore, a director must inform other directors and statutory auditors of any interest he or she has on his or her own behalf (or on behalf of third parties) in a transaction, specifying its nature, terms, origin and relevance; in the case of a managing director, he or she shall abstain from such transaction, informing the board of the interest or reporting it to the shareholders' meeting (in the case of a sole director). A potential conflict of interest does not prevent the director with this interest from voting in favour of the transaction, but it requires the entire board of directors to adequately specify the reasons for the transaction and the advantages for the company deriving from the relevant transaction.

In the event of non-compliance with the above, the resolution – if adopted with the determining vote of the director in a conflict of interest situation, and if prejudicial to the company – can only be challenged by directors and the board of statutory auditors within 90 days of the date of its adoption. In any case, rights acquired in good faith by third parties on the basis of acts carried out in execution of the resolution shall remain unaffected.

Shareholders would in any event be entitled to pursue the liability of directors for violation of their duties on behalf of the company provided that the conditions outlined in question 2 are met.

In addition, directors will be liable for damage that may be caused to the company from any use for their own benefit (or that of third parties) of data, information and business opportunities obtained in connection with their appointment.

### Controlling shareholders

- 20 Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

Italian law does not provide for any specific duty upon controlling shareholders in the case of M&A transactions.

More generally, however, specific rules and liabilities apply to legal entities exercising direction and coordination towards other companies. Those legal entities will be liable towards shareholders of the controlled companies (for damage caused to the value of their shares); and creditors of the controlled companies (for damage caused to the latter's assets) when acting in their own interest (or in the interest of third parties) in breach of the principles of fair management of the controlled company.

No liability shall arise where shareholders or creditors of the controlled companies suffered no damage, taking into account the overall outcome of the activity of direction and coordination; or where damage has been completely eliminated by a specific action carried out for this purpose.

To bring a successful claim against the directors of a controlling or controlled company, minority shareholders shall demonstrate the directing and coordinating power of the controlling entity; the existence of conducts against the principles of proper management; and the damage suffered.

As for listed companies, CONSOB sets out a specific discipline concerning related-party transactions.

## INDEMNITIES

### Legal restrictions on indemnities

**21** | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Companies are in principle allowed to indemnify or advance the legal fees of their officers and directors sued for alleged breach of their duties.

This is not, however, common practice since, as explained in question 24, companies usually opt instead to pay for insurance policies covering directors' and officers' liability. This practice is also due to the fact that it is debated in the Italian courts the nature of the relationship between the directors and the company and the existence of an effective obligation for companies to keep their directors and officers indemnified.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

**22** | Can shareholders challenge particular clauses or terms in M&A transaction documents?

This possibility is not specifically provided for under Italian law.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

**23** | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

Shareholders who expressed their favourable vote to a resolution approving a transaction cannot challenge it.

As regards joint-stock corporations, shareholders' resolutions that are not in compliance with the law or company by-laws may be challenged only by those shareholders who were not present at the relevant shareholders' meeting or that dissented or abstained from the vote (as well as by directors, supervisory board members or statutory auditors). As explained in question 9, resolutions can be challenged by shareholders who own shares with voting rights representing, on aggregate, at least one per 1,000 of the share capital, for companies recurring to risk capital and 5 per cent in other cases.

The by-laws may reduce or exclude such a requirement. Shareholders who do not represent the required share capital (and those who are not entitled to challenge the resolution) are entitled to seek damages suffered by the non-compliance of the resolution with the law or with the by-laws.

As to limited liability companies, quotaholders' resolutions that are not in compliance with the law or by-laws may be only challenged by those quotaholders who were not present at the relevant quotaholders' meeting or that dissented or abstained from the vote (as well as by directors, supervisory board members or auditors). The corporate capital quota needed to challenge the resolution is provided by the by-laws of the company.

## Insurance

**24** | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors and officers are commonly insured (companies also often sign insurance policies covering directors and officers as part of their directors' and officers' insurance policy) against damage claims deriving from breaches of duties set out in the law or by-laws, as long as these do not derive from gross negligence or wilful misconduct.

It is therefore common that, when a director or officer is sued, he or she seeks indemnification from the insurance company. This is usually sought by filing a request for joinder upon the insurance company. Traditionally, insurance companies present pleadings that are twofold and aimed at denying that an obligation to indemnify the director or officer exists, and dismissing claims raised against the director or officer.

## Burden of proof

**25** | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

As a general rule, article 2697 ICC establishes that the burden of proof is upon the party making the relevant allegation.

However, in the context of liability claims against directors and officers, the burden of proof depends on whether the shareholders claim losses suffered by the company or individually.

In the first case, the claim is grounded on a contractual breach, and the claimant or injured party is exonerated from demonstrating that a breach occurred as it has to be only alleged, while the defendant or injuring party has the burden to prove that it has complied with the relevant contractual obligation (Supreme Court 30 October 2001, No. 13533). The claimant or injured party shall, in any case, demonstrate the existence of the contract, the occurrence of a loss (as well as its quantification) and causation between the breach and the loss. Accordingly, when shareholders file a claim for damages on behalf of the company, ie, grounded on the failure of the board members or officers to comply with their duties, the shareholders (more correctly, the company) shall prove the existence of the contractual relationship between the parties and the damage, along with its quantification. On the other hand, the members of the board or officers shall prove that they complied with their duties or that the alleged damage cannot be attributed to their behaviour.

If the shareholders act personally and in their own interest against the board members or officers, the general rule under article 2043 ICC will apply, and the plaintiff or injured party shall provide evidence of the unlawful act or omission committed by the director or officer, the causation between the breach and the loss and the wilful misconduct or negligence of the director or officer.

## Pre-litigation tools

### 26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

As for limited liability companies, pursuant to article 2476 ICC, quota-holders who are not directors or members of the board have the right to obtain from the directors updates regarding the status of operations; and to examine the corporate books and records, even with the assistance of a professional adviser.

As for joint-stock companies, shareholders' right to examine and make copies is restricted to certain corporate books (article 2422 ICC), as the control regarding correct management generally lies with the statutory auditors. Pursuant to article 2409 ICC, when there is a reasonable ground to deem that directors have committed a serious breach relating to management, possibly causing losses to the company or controlled companies, a certain number of shareholders (minimum thresholds can be modified by corporate laws) can refer the relevant facts to the competent court. The court may, *inter alia*, order an inspection or even appoint a judicial director.

In the framework of mergers, a copy of the following documents, *inter alia*, shall be shared with the shareholders (30 days before the meeting resolving upon the transaction): the merger plan; the financial reports of the last three years of the companies taking part to the transaction, along with the reports of the board of directors and auditing firm; and the up-to-date financial status of the companies taking part in the transaction (article 2501-septies ICC).

Each shareholder can inspect said documents and obtain a free copy of them.

## Forum

### 27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Provided that the company is sued, the general rule under Italian law is that proceedings shall take place where the company has its headquarters or its registered offices (article 19 ICCP).

While by-laws can derogate from such provision and provide that claims shall be brought before a different court (articles 28 to 29 ICCP), that option is not applicable, *inter alia*, to claims raised by shareholders to challenge the validity of any resolution, including the one that authorises the merger or acquisition, pursuant to article 2378 ICC (this rule was confirmed by the Supreme Court in judgment No. 19039 of 11 September 2007), as well as to disputes between shareholders.

Further limitations are provided by law in relation to, *inter alia*, interim proceedings, enforcement proceedings and insolvency proceedings.

Furthermore, it is common that companies' by-laws provide that any dispute among the company, shareholders and directors shall be settled through arbitration. Under Italian law, arbitrators are generally prevented from ordering interim measures, with very limited exceptions relating to the order of suspension of the effectiveness of resolutions.

## Expedited proceedings and discovery

### 28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Discovery does not apply to Italian judicial proceedings, and each party to the proceedings is free to file (or not to file) with the court the documents and evidence that it deems necessary to support its allegations. However, pursuant to article 210 ICCP, each party is able to request the court to order the other party or a third party to exhibit a certain

document if relevant requirements are met (eg, the exact identification of the relevant document, the indication of the reasons why exhibition is sought and the relevance of the – alleged – content of the document to the case). The party against which exhibition is sought may object, *inter alia*, that the exhibition of the document would be prejudicial to itself or a third party (eg, in the case of a confidential document).

The Italian civil procedural system provides for a simplified trial governed by articles 702-bis et seq ICCP. Such simplified procedure can be used when collection of evidence is presumed to be easy. If the complexity of the matter requires a more articulated examination, the court can order the case to be decided through ordinary proceedings. This kind of proceeding cannot be used when the dispute, pursuant to article 50-bis ICCP, has to be decided by a panel of three judges. A panel of three judges is required, for instance, where specialised court divisions have jurisdiction over the matter (eg, court divisions having jurisdiction over a wide number of disputes possibly involving corporations, including without limitation liability claims against directors and officers, and disputes relating to any transfer of participation interests) or in the case of proceedings for challenges of resolutions of a shareholders' meeting or of the board.

In any case, given the complexity of post-M&A litigation, it is highly unlikely that even residual claims (ie, those not falling under the cases reported above) will be initiated or decided through summary proceedings.

## DAMAGES AND SETTLEMENTS

### Damages

#### 29 | How are damages calculated in M&A litigation in your jurisdiction?

The most common issues in M&A litigation concerning damages are related to the difference between the value attributed to the shares during and after the transaction, and the value that the same would have had if the alleged unlawful behaviour did not occur. It is upon the claimant to provide an estimate of the damages and to provide supporting evidence. Given the complexity of the calculation, courts generally appoint an expert to evaluate the correct value of the disputed amount. In such case, the parties will have the right to appoint their own experts.

### Settlements

#### 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

In general terms, settlement agreements are regulated by articles 1965 et seq, ICC. Nonetheless, when the object of the settlement agreement is a liability claim against directors and officers brought, or possibly to be brought, by a shareholders' meeting on behalf of the company (pursuant to article 2393 ICC), the settlement can take place only upon approval by the majority of the shareholders' meeting, provided that no objection is raised by shareholders who represent (at least) one-fifth of the corporate capital or 1/40th for companies recursing to risk capital (or any other majority the corporate by-laws provide for). According to article 2393-bis ICC, the liability claim can also be brought by shareholders who represent at least one-fifth of the shareholders on behalf of the company (or any other majority the corporate by-laws provide for but not exceeding one-third), and in this case the settlement must be approved by the same shareholders who initiated the claim. In this latter case, if the shareholders' claim proves successful, shareholders are reimbursed for any legal expenses. In both cases, any damages compensation awarded shall be paid to the company.

## THIRD PARTIES

### Third parties preventing transactions

#### 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

M&A transactions may be delayed or stopped if the shareholders' meeting resolutions approving the transaction are challenged for breach of the law or the by-laws (also on procedural basis) and, in such a context, temporarily suspended (see question 9). In addition, pursuant to article 2503 ICC, a merger cannot be completed until 60 days after the filing of the resolution resolving the merger with the companies' register.

In this time frame, creditors and bondholders of either company have the right to object to the merger pursuant to articles 2503 and 2503-bis ICC should they consider that the operation may prejudice the company's compliance with outstanding obligations. Upon request of the company, the competent court may issue a temporary decision authorising the transaction, if it considers prima facie that the claim is ungrounded or that the company has provided sufficient guarantees.

Alternatively and in any case, the 60-day term does not apply if:

- all the creditors and bondholders have previously consented;
- the company fulfils its obligations towards the creditors objecting to the merger;
- the company deposits the claimed amounts in a dedicated bank account; or
- a single firm of auditors is in charge of drafting both companies' report regarding the share exchange ratio, pursuant to article 2501-sexies ICC, and it certifies under its own responsibility that the transaction will not damage the position of creditors and bondholders.

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No specific actions are provided under the law. Of course, anyone can start litigation to put pressure on the defendants. However, if the litigation is frivolous, plaintiffs can be ordered to pay damages in addition to legal costs.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

The general rules regarding the duties and responsibilities of directors apply.

In addition, further specific duties may arise, inter alia, from rules laid down in the TUF and CONSOB Regulation No. 11971 of 1999.

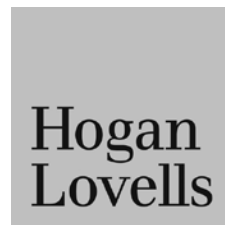
## COUNTERPARTIES' CLAIMS

### Common types of claim

#### 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

The most common types of claims that may arise from an M&A transaction include:

- breach of contract;
- breach of representations and warranties;



#### Andrea Atteritano

andrea.atteritano@hoganlovells.com

#### Francesca Rolla

francesca.rolla@hoganlovells.com

#### Emanuele Ferrara

emanuele.ferrara@hoganlovells.com

Via Marche, 1-3  
Rome 00187  
Italy  
Tel: +39 06 6758231  
Fax: +39 06 67582323

Via Santa Maria alla Porta, 2  
Milan 20123  
Italy  
Tel: +39 02 7202521  
Fax: +39 02 72025252

www.hoganlovells.com

- purchase price adjustments;
- earn-out claims;
- lack of disclosure in the negotiation phase and pre-contractual liability; and
- breach of good faith obligations.

### Differences from litigation brought by shareholders

#### 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

The rationale behind these two types of litigation is completely different, and the impact on the way litigation is conducted – which changes also based on the content of claims and the relief sought – is so wide, that it cannot be summarised in few lines. In general terms, however, it should be highlighted that in Italy:

- claims between parties to an M&A transaction are by far more common than litigation initiated by shareholders;
- disputes between parties to an M&A transaction are mainly focused on the transaction documents, while shareholders' litigation focuses on the actions taken by the corporate bodies and their consequences for the company; and
- disputes between the parties to an M&A transaction are usually contract-based and solved by arbitration (as most M&A contracts contain arbitration clauses), while litigation brought by shareholders can also be based on tort and is usually brought in public courts.



**UPDATE AND TRENDS****Key developments****36 | What are the most current trends and developments in M&A litigation in your jurisdiction?**

Following the recent better performance of Italian economy, the country experienced in the past two years a progressive growth of foreign and internal investments. This resulted in an indirect increase of M&A transactions and, consequently, of post-M&A litigation.

The most common claims in this respect concern the breach of representations and warranties, and price adjustment. On the other hand, while in the past parties did not commonly seek the annulment of the transaction, we are experiencing an increase of such claims in recent years, especially when environmental issues are involved or when part of the purchase price is to be paid by means of earn-out consideration.

# Japan

Kenichi Sekiguchi

Mori Hamada & Matsumoto

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

There has been an increased number of appraisal cases in which shareholders who were not satisfied with the consideration offered in a transaction have requested the court to determine the fair value of the shares. In some cases, shareholders also claimed a breach of fiduciary duty of directors of the seller (for selling shares at a discounted price), the buyer (for buying shares at a price higher than the fair value) or the target company (for accepting, and recommending its shareholders to accept, a tender offer despite the tender offer price being lower than the fair value of its shares). However, as proving a breach of fiduciary duty is challenging for shareholders without comprehensive discovery, appraisal claims are currently the most common claims. When shareholders claim a breach of directors' fiduciary duty, they tend to claim against directors in tort at the same time.

While, in theory, the Companies Act of Japan (Companies Act) permits claims for injunctive relief to suspend a transaction, shareholders generally do not attempt this because the grounds for injunctive relief are limited. Shareholders may also bring a claim to nullify a transaction, but as doing so would affect a large number of interested parties and the courts tend not to nullify transactions in the absence of extraordinary circumstances, such successful claims are quite rare.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

Appraisal cases are treated as non-contentious cases in which the court has reasonable discretion to determine the fair value of shares without regard to the burden of proof of the parties. However, in recent cases the court has presumed the consideration offered in a transaction is fair if it was determined through fair procedures and without any coercion. Therefore, as in many cases the company can show the fairness of the procedures to a certain extent, shareholders are normally required to rebut this presumption, for example by showing there were factors preventing the shareholders from approving the transaction fairly (eg, the company's false disclosure of material facts, or shareholders being threatened with a squeeze-out at a lower price in the future) or that the independence of the target's board was jeopardised.

For a derivative claim in which shareholders pursue damages sustained by the company for breach of fiduciary duty, shareholders must prove the existence of the fiduciary relationship, the contents of the directors' duties, their breach and the quantum of damages arising.

Directors could then refute the claimed negligence, as it is not a strict liability. On the other hand, to pursue directors for damage directly sustained by shareholders, the Companies Act requires shareholders to prove, in addition to the foregoing, malicious intent or gross negligence on the part of the directors.

In both cases, as mentioned in question 15, except in the case of directors of the target company breaching their fiduciary duty in management buyouts (or transactions involving conflicts of interests), the business judgement rule would apply to the decision of directors with respect to M&A transactions. Therefore, shareholders would be required to show that the directors were prevented from making an informed decision, or that their decision or decision-making process was extremely unreasonable (see question 15 for further explanation).

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

The actual claims that shareholders tend to bring differ depending on whether the companies involved in the M&A transactions are publicly traded or privately held, but under the Companies Act, there is no major difference in the types of claims they can bring.

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Shareholders can bring a derivative suit or direct claim in all types of M&A transactions if losses are sustained by the company or the shareholders (see question 6).

A claim for injunction under the Companies Act is only available (and in a limited manner) for mergers and other statutory reorganisations, and not in the case of tender offers, share purchases or asset sales, although the Companies Act generally allows injunctions by shareholders if directors conducted or are likely to conduct actions that are outside the scope of the company's purpose or that otherwise are in violation of the law or the company's articles of incorporation, and the company will likely sustain substantial damages.

In addition, appraisal rights are available in mergers and other statutory reorganisations and business transfers, except for simplified mergers or other reorganisations or for shareholders of the acquiring company in short-form mergers or other reorganisations. Shareholders do not have appraisal rights in the case of tender offer, share purchase and asset purchase transactions.

### Negotiated or hostile transaction

- 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No.

### Party suffering loss

- 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes, shareholders can bring a derivative suit if the company itself sustains losses. Subject to directors' malicious intent or gross negligence, if shareholders themselves directly sustain damages arising out of a breach of directors' fiduciary duty, they may bring a direct claim against directors. The question arises as to whether shareholders can claim diminution of value of their shares due to directors' failure to exercise their fiduciary duty with respect to M&A transactions, which resulted in losses to the company as damages in a direct claim. The majority view is that diminution of value of their shares is an indirect damage, and that the remedy should be through bringing a derivative action if the loss is sustained by the company and is recoverable through the derivative action. For instance, in a cash-out merger, the surviving company would sustain losses if the merger ratio was improper and the surviving company paid excessive consideration to the shareholders of the absorbed company, in which case shareholders of the surviving company should bring a derivative action.

If the consideration in the merger was shares of the surviving company, all the assets and liabilities of the absorbed company are succeeded to the surviving entity without any cash-out and, therefore, the surviving company arguably does not sustain any losses. In this case, while a derivative action would likely be dismissed due to the lack of losses sustained by the surviving company, shareholders of the surviving company may bring a direct claim as their shares were diluted in a manner disproportionate to a fair merger ratio. In this case, one would argue that issuing new shares based on an improper merger ratio itself should be considered damage to the issuer (ie, the surviving company), but whether the courts will accept such argument or not remains to be seen.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

- 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Japanese law does not permit class or collective actions (except for collective actions that may be brought by certified consumer protection agencies under special laws for protection of consumers' interests, which are not relevant here). This said, there have been cases in which a lead shareholder made a campaign through a website or other means to solicit other shareholders or similarly situated parties to be co-plaintiffs in a claim.

### Derivative litigation

- 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes, shareholders can bring derivative litigation on behalf of or in the name of the company.

Any shareholder holding one or more shares in a company (for at least six months or such shorter period as prescribed in the articles of

incorporation in the case of a public company) may demand that the company bring a claim against its directors and other officers. After receipt of the demand, the company will have 60 days to determine whether it will bring a claim against the named directors and other officers. If the company does not file such claim within the 60-day period, the demanding shareholder may bring derivative litigation on behalf of the company. When the company decides not to bring the claim, upon request of the demanding shareholder it must notify the demanding shareholder, and provide a description of any investigation it conducted, the conclusion and justifying reasons for such decision.

The 60-day period does not apply, and shareholders can immediately bring derivative litigation if the waiting period would result in the company sustaining irrecoverable damages.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Under the Companies Act, for mergers or other M&A transactions involving corporate reorganisations such as spin-off, the court may enjoin the transaction if there is a violation of the law or the articles of incorporation, and the shareholders are likely to be prejudiced by the transaction. In the case of short-form mergers or other short-form reorganisations that do not require approval of the shareholders, if the consideration of the transaction is extremely unfair that would also form the basis of an injunction. A breach of fiduciary duty or the insufficiency of consideration in the transaction (except for short-form mergers or other short reorganisation) is not generally considered a violation of law. As mentioned in question 1, injunctive or other interim relief to prevent the closing of an M&A transaction is extremely rare in Japan.

The court does not have any authority to modify deal terms.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

This is not relevant in Japan as there is no comprehensive discovery.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

In theory, shareholders can bring such claims if, for example, advisers had been involved in some wrongdoing or there were other extraordinary circumstances that would constitute a tort, but in practice such claims are extremely rare.

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

In theory, shareholders of a party can bring claims against the counterparty to the M&A transactions for aiding and abetting a breach of fiduciary duty based on the joint-tort theory, but we are not aware of any such cases. As the directors and officers of the counterparty do not owe any fiduciary duty to the shareholders of the first party, bringing a successful claim would be extremely difficult. Note that a controlling

shareholder is not construed as owing fiduciary duties to other minority shareholders, so the foregoing is also true for M&A transactions between a company and its controlling shareholder.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

A company may include provisions in its articles of incorporation that allow the board to discharge directors' or officers' liabilities or permit non-executive directors or officers to enter into contracts limiting their liabilities, in both cases in excess of certain statutory minimum liabilities. For details, see question 21.

### Statutory or regulatory limitations on claims

14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

To deter abusive derivative litigation, shareholders are not entitled to demand the company to bring a claim against its directors, or to bring a derivative claim if the claim is for the personal benefit of the shareholders or other third parties or causes damage to the company. Otherwise, there are no statutory or regulatory provisions that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions.

### Common law limitations on claims

15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Japan is not a common law jurisdiction. However, the Japanese courts generally apply a 'business judgement rule' when questions arise with respect to a managerial decision. While there is no concrete specification of the business judgement rule and the effect thereof, where the business judgement rule applies, the court normally respects the decision of the director unless the director made a mistake in gathering or analysing the information necessary to recognise the underlying facts that formed the basis of his or her decision; or the director's decision or the decision-making process was extremely unreasonable.

How and to what extent the business judgement rule applies to a decision of board members in connection with M&A transactions is not entirely clear. However, except for a decision of board members of a publicly traded target company with respect to management buyouts or other transactions that involve conflicts of interests (see refer question 17), the business judgement rule would be widely applied.

## STANDARD OF LIABILITY

### General standard

16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

As mentioned above, the court would normally apply the business judgement rule in some form in determining the liability of directors with respect to M&A transactions; therefore, unless exceptional circumstances are found, it is not easy for shareholders to prove a breach of a

board member's or executive's fiduciary duty. For instance, with respect to an integration of two publicly traded non-life insurance companies by way of a joint share swap, a shareholder filed a claim for breach of fiduciary duty and asserted that the representative director of the company failed to exercise the duty to determine a fair consideration (ie, the stock swap ratio). However, the Tokyo District Court applied the business judgement rule and dismissed the claim.

In doing so, the Tokyo District Court reasoned that:

- the company engaged an independent third party to conduct financial due diligence;
- the parties agreed on the stock swap ratio in reference to the result of multiple third-party valuation reports;
- the agreed stock swap ratio was within a range of the valuation reports; and
- the multiple independent third parties expressed a fairness opinion.

### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

It is not entirely clear whether the court applies a different standard of review depending on the type of transaction, consideration being paid, potential conflict or involvement of a controlling shareholder.

In 2013, the Tokyo High Court held in a breach of fiduciary duty claim with respect to a management buyout of Rex Holdings that the decision to conduct the management buyout itself should be respected under the business judgement rule unless there were circumstances that rendered such decision or the decision-making process extremely unreasonable. Nonetheless, the court stated that, even if the decision for conducting the management buy-out itself is respected under the business judgement rule, the directors must perform their fiduciary duties to ensure that the fair value is transferred among shareholders; and to disclose the information necessary for the shareholders to determine whether to tender their shares in a tender offer.

There are divided views as to whether this decision imposes a stricter standard of review or merely clarifies duties of directors in management buy-outs. It is also not clear whether this decision applies only to management buy-outs, or whether it could extend to transactions involving conflicts of interests or further to transactions in which a transfer of value among shareholders would be disputed.

### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

See question 17.

### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

See question 17.

### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

See question 17.

## INDEMNITIES

### Legal restrictions on indemnities

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

With respect to indemnification of directors' or officers' liabilities against the company itself, the Companies Act provides specific rules for the company to discharge such liabilities. As a general rule, discharging directors' or officers' liabilities against the company requires unanimous approval of the shareholders. However, if the director or officer acted in good faith and without gross negligence, the liability in excess of the statutory minimum (ie, six years' salary for representative directors and four years' salary for other directors) could be discharged by approval of the shareholders or, if the articles of incorporation of the company have a provision expressly allowing it, by the board. Non-executive directors or officers, if there is a provision in the articles of incorporation expressly allowing it, may enter into contracts with the company limiting their liabilities to the statutory minimum or any amount determined by the company within the range stipulated in the articles of incorporation, whichever is the higher.

Apart from those statutory provisions, officers and directors are generally considered as fiduciaries of the company and, in accordance with the Civil Code of Japan, may request that the company reimburse or advance expenses required to perform their duties as fiduciaries. In addition, they may request that the company indemnify them for any liability incurred in performing their duties as fiduciaries not attributable to their fault. While the Civil Code of Japan requires officers and directors not to be at fault, in practice, companies from time to time voluntarily indemnify officers and directors in the absence of gross negligence. Therefore, it is generally understood that companies may indemnify, or advance the legal fees of, its officers and directors named as defendants in M&A-related litigation so long as such indemnification or advancement is necessary for them to perform their duties as officers or directors.

The Companies Act does not clearly set out rules concerning companies' ability to indemnify, or advance the legal fees of, their officers and directors named as defendants. Depending on the circumstances, it is possible that the indemnification or advancement of legal fees could be considered compensation, in which case other requirements would apply (eg, obtaining shareholder approval). Hence, there was ambiguity about whether companies could take such actions.

In recognition of this, a study group organised by the Ministry of Economy, Trade and Industry published a report in July 2015 on the practice of corporate governance, and clarified the requirements and procedures for indemnification, or advancement of legal fees or other damages, to enable directors to take necessary risks when managing companies without fear of personal liability. In January 2019, the Legislative Council Companies Act Subcommittee published a Proposal for the Companies Act Revision, which addresses these issues, and relevant amendments are expected to come into force soon.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

- 22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

It is not clear whether shareholders can challenge particular clauses or terms in M&A transaction documents such as termination fees, standstills, 'no shop' or 'no talk' clauses, or other terms that tend to preclude third-party bidders. Agreeing on deal protection clauses without proper

fiduciary-out exceptions might deprive shareholders of opportunities to receive more favourable offers from other bidders and would constitute a breach of directors' fiduciary duty. If this is the case and shareholders sustain losses as a result, shareholders can bring a claim for breach of fiduciary duty. However, proving damage arising out of such breach would normally be difficult, unless a favourable competing offer was actually made but prevented due to the deal protection clauses. Injunctions based on improper deal protection clauses are even more difficult, as the grounds for injunctions are limited (see question 9).

As such, it is not practicable for shareholders to challenge particular deal protection clauses.

Having said this, in subsequent appraisal proceedings shareholders may use the improper deal protection clauses in support of the claim that the entire transaction process was unfair (and thus, the court should not presume the agreed consideration to be fair).

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

- 23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

While the shareholder vote itself is not the decisive factor, the court normally respects the informed decision of shareholders. In an appraisal proceeding concerning an M&A transaction between independent listed companies, the Supreme Court judged that, if the transaction was implemented through procedures generally considered fair (such as the approval of the shareholders based on proper disclosure of relevant information) then, unless there were special circumstances that prevented shareholders from making a reasonable decision, the consideration of the transaction will be considered fair.

### Insurance

- 24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors' and officers' (D&O) insurance plays a substantial role in shareholder litigation.

Standard D&O insurance in Japan would normally cover a wide range of liabilities that directors or officers could incur in performing their duties, except for matters arising from receipt of unlawful private benefits, criminal acts or wilful breaches of the law. Whether a company can pay the insurance premium corresponding to special coverage for cases where a director loses in a shareholders' derivative suit had long been subject to discussion, as it would have been construed as payment of compensation without obtaining shareholder approval or a discharge of directors' liabilities without taking proper procedures. In practice, to be conservative, directors themselves have paid the insurance premium corresponding to such special coverage. However, as this differed from other developed countries, in the report of the study group organised by the Ministry of Economy, Trade and Industry (see question 21), it was clarified that the company can pay such insurance premiums for directors by taking certain procedures required, and the Proposal for the Companies Act also contains relevant proposals.

### Burden of proof

- 25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

For appraisal cases there is no precise burden of proof, while for a breach of a fiduciary duty claim shareholders have the burden of proof. For further details, see question 2.

There are no clear rules as to when and to what extent the burden shifts.

### Pre-litigation tools

**26** | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Any shareholder may, during the normal business hours of the company, review or obtain copies of minutes of shareholders' meetings.

Similarly, if it is necessary to exercise this right as a shareholder, a shareholder may request the company to make available for review, or provide copies of, minutes of board meetings. However, for the board minutes, if the company is a company with statutory auditors or a company with an audit or nominating committee, the request requires court approval.

Class actions are not possible under Japanese law; however, shareholders are entitled to review or copy the shareholders' register, and sometimes a plaintiff shareholder exercises this right to solicit other shareholders who would be potential plaintiffs. The company may refuse such a request only if it was made:

- (i) for purposes other than securing or exercising rights as a shareholder;
- (ii) for disturbing the business of the company or otherwise impairing the common interests of shareholders;
- (iii) for providing to third parties the facts ascertainable from the shareholders' register for consideration; or
- (iv) by an applicant who has provided to third parties the facts ascertainable from the shareholders' register for consideration in the past two years.

Shareholders holding at least 3 per cent of the total voting rights of a company (or such lower threshold as prescribed in the articles of incorporation) may request the company to make available for review, or provide copies of, the accounting books and records at any time during normal business hours. However, the company may refuse to do so based on the grounds equivalent to items (i) to (iv) above and also if the requesting shareholder engages in a competing business.

In addition, when a shareholder anticipates a dispute with respect to an M&A transaction that requires shareholders' approval, any shareholder holding at least 1 per cent of the total voting rights (or such lower threshold as prescribed in the articles of incorporation) (in the case of a public company, for a consecutive period of six months) may request the court to appoint an inspector to investigate the convocation procedures and the manner of the resolution of the shareholders' meeting.

### Forum

**27** | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Under the Companies Act, with some minor exceptions, the court located in the area of the headquarters of the defendant company or the company for which the defendant directors or officers serve has exclusive jurisdiction over any litigation concerning the validity of an M&A transaction or a breach of fiduciary duty claim. Forum selection clauses in corporate by-laws are not permitted.

### Expedited proceedings and discovery

**28** | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

There are no expedited proceedings or comprehensive discovery under Japanese law. However, under the Code of Civil Procedure, a party may request the court to order the other party or any third party to produce a document to the court. The party requesting such order must specify a description, the purpose and the holder of the document, the facts to be proven by the document and why it is necessary. Documents typically requested by plaintiff shareholders would include negotiation materials, internal evaluation documents, third-party valuation reports and minutes of material internal meetings, including those in draft form.

The statute imposes a general obligation on relevant parties for submission of documents with some exceptions. In M&A litigation, defendants could contest a plaintiff shareholders' request in reliance on:

- the lack of necessity of producing a document;
- the specification of the documents requested to be disclosed; or
- the exceptions for document production related to professional secrecy or to documents prepared solely for the use of the party holding the documents.

The court once ordered a company to produce various documents with respect to an attempted management buyout that was not successful due to improper involvement of the management who participated in the buyer; it was an extraordinary case that came about mainly because of a series of reports from whistle-blowers. The lack of comprehensive discovery in M&A litigation is probably a major factor in M&A litigation being less common in Japan than in some other jurisdictions such as the US.

## DAMAGES AND SETTLEMENTS

### Damages

**29** | How are damages calculated in M&A litigation in your jurisdiction?

There are no clear guidelines as to how damages should be calculated in M&A litigation in Japan.

As a general rule, Japanese courts do not award punitive damages. While the position of the courts is far from settled, shareholders tend to assert that the difference between the actual price paid in the transaction and the fair value of the shares is the damage they sustained from the transaction. Calculation of damages based on a multiple would not likely be accepted by the court.

### Settlements

**30** | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

In a derivative M&A litigation brought by a shareholder, if the company is not a party to the litigation, the settlement does not have an immediate final and binding effect on the company unless the company affirms the settlement. In such cases, the court must notify the company of the description of the settlement and request the company to make any objection within two weeks. If the company does not object to the settlement in writing within two weeks, the company is deemed to have affirmed the settlement, and the settlement will be final and binding on the company.

## THIRD PARTIES

### Third parties preventing transactions

#### 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Under the Companies Act, only shareholders of the company are entitled to bring claims for injunctions in M&A transactions. Therefore, in the absence of contractual or other specific grounds that would form the basis of an injunction under the Civil Preservation Act, third parties cannot bring litigation to break up or stop agreed M&A transactions prior to closing.

One such exceptional case was the merger between the Mitsubishi Tokyo Financial Group (MTFG) and the UFJ Holdings Group (UFJHD) together with some of their affiliates. In this case, UFJHD had entered into a memorandum of understanding (MOU) with Sumitomo Trust Bank (STB) regarding the disposal of its shares in UFJ Trust Bank that included exclusivity provisions, but UFJHD had later decided to unilaterally terminate the MOU to enter into discussions with MTFG regarding the integration of the entire UFJHD group with the MTFG group. STB brought an injunction based on the exclusivity provision. While the Tokyo District Court granted injunctive relief to prohibit negotiations between UFJHD and MTFG, the Tokyo High Court and the Supreme Court denied the injunction. In doing so, the Supreme Court stated that, as the MOU itself did not oblige either party to enter into definitive agreements for a transaction, the damage the claimant would sustain from the breach of the MOU should not include the profit they would have received if the transaction was completed. If that were the case, such damage could be recovered by a subsequent damages claim, and thus there is no significant damage or imminent danger that forms the basis of injunctive relief.

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

It is not common in Japan for third parties to use litigation to force or pressure companies to enter into M&A transactions. As mentioned in question 31, in the absence of contractual or other specific grounds that would form the basis of an injunction under the Civil Preservation Act, third parties cannot bring claims for injunction.

It is of course possible for third parties to acquire substantial shares in companies and pressure them to enter into M&A transactions, but here again, initiating litigation to force or pressure companies to enter into M&A transactions is not practicable.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Unsolicited or unwanted offers are quite rare in Japan, and there is no judicial precedent in which directors' duties in the face of an unsolicited or unwanted offer were directly at issue.

When the validity of defensive measures has been disputed, courts have normally upheld the defensive measures adopted by boards if the purpose is to obtain information and the time required to ensure the informed decision of shareholders. On the other hand, if the board takes a more aggressive measure such as the issuance of stock options to a friendly third party with the aim of diluting the shareholding of the hostile offeror, as determined in the Tokyo High Court's decision in the

*Livedoor v Nippon Broadcasting* case, unless exceptional circumstances justify the taking of such a measure to protect the common interest of shareholders (eg, there is a greenmailer or other abusive offeror), taking such measures is presumed to be for the purpose of maintaining the control of the incumbent management and would not be permissible.

With regard to defensive measures approved by the shareholders, however, the Supreme Court held in the *Steel Partners Japan Strategic Fund v Bull-Dog Sauce* case in 2007 that it was permissible under the principle of equal treatment of shareholders for a company to allot stock options to all shareholders that are only exercisable by shareholders other than the hostile offeror as long as such allotment is necessary and appropriate to protect the common interests of shareholders from the probable damage to be caused by the hostile offeror.

## COUNTERPARTIES' CLAIMS

### Common types of claim

#### 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

In private M&A transactions, we have seen an increased number of disputes regarding breach of representations and warranties. From time to time, parties to M&A transactions dispute purchase price adjustments or earn-out payments, but these are less common. This said, while there have been some cases in which the court determined whether a breach of representations and warranties occurred and, if so, the amount of damage arising, owing to the limited number of such precedents there remains a number of issues with respect to which the court's position is unclear.

### Differences from litigation brought by shareholders

#### 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

In litigation brought by shareholders, shareholders would have difficulties obtaining the evidence necessary to prove their case. In litigation between the parties to an M&A transaction, asymmetry of information would not normally be a critical issue.

## UPDATE AND TRENDS

### Key developments

#### 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

Since the enactment of the Companies Act in 2005, there has been a significant increase in the number of appraisal cases in which minority shareholders have demanded that the courts determine the fair value of their shares in M&A transactions, mainly because the Companies Act entitles dissenting shareholders to the fair value of the shares taking into consideration the synergies arising out of the transaction or the value the shares would have had in the absence of the M&A transaction. In some of these appraisal cases, the courts looked in detail at the appropriate value of the shares and determined the fair value on its own without specifically relying on any third-party expert's opinion. Such cases encouraged arbitrary actions by shareholders to a certain extent, creating uncertainty in M&A transactions involving publicly listed companies, and have been criticised by practitioners. The Supreme Court removed such uncertainty in its decision involving the appraisal of shares of Jupiter Telecommunication, the largest Japanese cable TV operator, in its going-private transaction by its major shareholders, KDDI and Sumitomo Corporation, who collectively held more than 70 per cent

of the shares in Jupiter Telecommunication prior to the transaction. The Supreme Court stated that, even in the case of a two-step going-private transaction consisting of a tender offer and a subsequent squeeze-out procedure that involves conflicts of interest, the court should respect the price determined by the parties to the transaction if:

- measures to ensure the decision-making process was not arbitrary due to conflicts of interests such as obtaining an opinion from an independent committee or third-party experts were taken; and
- the tender offer was conducted through procedures generally considered fair, such as disclosing the offeror's intent to acquire the remaining shares in the subsequent squeeze-out process at the same price as the tender offer price (to reduce coerciveness).

To put it simply, the Supreme Court stressed that courts should focus on procedural fairness before looking deeply into the substance (ie, valuation of the shares) because judges are not valuation experts. How and to what extent the courts should review procedural fairness are remaining issues about which further clarification is awaited. In any event, we expect to see fewer arbitral appraisal cases going forward, but at the same time the courts will review procedural fairness more carefully, so practitioners should continue to pay attention to how they ensure procedural fairness.

In this regard, the Ministry of Economy, Trade and Industry has established a study group regarding fairness in M&A transactions and it is expected that the study group will clarify some of those issues.

Apart from the appraisal proceedings, we have seen an increased number of disputes regarding breach of representations and warranties between private sellers and buyers. As mentioned earlier, the courts' position on a number of issues relating to M&A litigation are far from settled, but judicial precedent that can guide M&A practitioners has gradually accumulated through a series of court decisions, including Supreme Court decisions, in recent years.

## MORI HAMADA & MATSUMOTO

---

### **Kenichi Sekiguchi**

kenichi.sekiguchi@mhmjapan.com

---

16th Floor, Marunouchi Park Building  
2-6-1 Marunouchi, Chiyoda-ku  
Tokyo 100-8222  
Japan  
Tel: +81 3 6266 8562  
Fax: +81 3 6266 8462  
www.mhmjapan.com



# Netherlands

Manon Cordewener, Carlijn van Rest and Bas Keizers

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

Under Dutch law, shareholders can bring various types of claims in connection with M&A transactions.

Litigation by shareholders (in publicly traded companies) often takes place in inquiry proceedings before the Enterprise Court of the Amsterdam Court of Appeal. A recent example of such proceedings is the case of *Elliott Advisors v AkzoNobel*, initiated in 2017. Inquiry proceedings are often used to protect the interests of minority shareholders.

This type of proceedings entails three steps:

- a request for an inquiry into the policies and course of affairs of the company;
- the actual inquiry (in which there is room for disclosure and discovery); and
- an assessment on the basis of an inquiry by the Enterprise Court as to whether the company has been mismanaged.

If the Enterprise Court rules that the company has been mismanaged, it can take a number of measures based on the request of the shareholder (who initiated the proceedings). Inquiry proceedings are based on article 2:345–2:359 Dutch Civil Code (DCC). It is only possible to start inquiry proceedings against a company, and not against individual officers or directors. There are also certain requirements (a group of) shareholders have to meet to qualify as a shareholder eligible to bring this type of claim. These requirements can be found in article 2:346 (b) and (c) DCC. In this respect, it must be noted that the shareholders are required to bring forward their objections to the board of directors and the supervisory board and provide the company a period to investigate and remedy the objections raised in order to have a cause of action. Furthermore, inquiry proceedings can only be brought against companies established under Dutch law and thus companies with its statutory seat in the Netherlands.

In addition, shareholders can bring unlawful act claims against companies, officers and directors on the basis of article 6:162 DCC read in conjunction with the special provision contained in article 2:8 DCC. In these types of claims, the shareholder will have to argue that the conduct of the company or the officers or directors constituted a tort against the claimant. If the district court at which the claim has to be filed rules that such tortious behaviour did indeed happen, damages can be awarded, and in very rare cases the M&A transaction itself can be challenged.

Finally, the shareholders can request the court to declare decisions taken by the board of directors to engage in an M&A transaction null and void. In addition, a shareholder could claim that management decisions are subject to annulment. The legal basis for such a claim is article 2:15 DCC. These kinds of actions are possible with regard to companies that

have been established under Dutch law and thus have their statutory seat in the Netherlands. A claim can be asserted either before or after the acts necessary to implement this decision are taken by the board of directors. The implementing acts in situations concerning M&A transactions include, for example, negotiations with a third party and entering into an agreement with this third party.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

For inquiry proceedings, the shareholders have to meet certain thresholds of equity interests in order to have a cause of action before the Enterprise Court. The Supreme Court has ruled that a foreign (indirect) shareholder also has the right of inquiry as long as it meets these thresholds and it is the (economic) beneficiary (Dutch Supreme Court, *Chinese Workers*). As applicants, the shareholders will have to make a sufficiently plausible showing that there are reasonable grounds to believe that the company in which the shareholders hold shares has been mismanaged.

The standard for liability of a corporation based on a wrongful act is set by the standard of due care following from article 6:162 DCC interpreted in light of the requirements set out by the principles of reasonableness and fairness described in article 2:8 DCC (Dutch Supreme Court, *Tuin Beheer*). These principles are dependent on the circumstances of each case (Dutch Supreme Court, *Zwagerman Beheer*).

With regard to requests to declare decisions taken by the board of directors to engage in a type of M&A transaction null and void, such decision has to be in conflict with the law (article 2:14 DCC). A management decision could be subject to annulment on the basis of one of the following three grounds:

- the decision has been taken in violation of the statutory provisions or rules in the company's articles of incorporation that govern the ways in which decisions have to be taken;
- the (method of formation of the) decision is contrary to the principles of reasonableness and fairness that all corporate bodies need to take into account in their relationship with each other (article 2:8 DCC); and
- the decision was taken in violation of any by-laws of the corporation.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

No. Both publicly traded companies (NVs) and privately held companies (BVs) are subject to inquiry proceedings based on article 2:346 DCC. The same applies to the possibility to claim damages on the basis of the general tort provision of article 6:162 DCC read in conjunction with

article 2:8 DCC. The validity of management decisions is subject to the same statutory provisions.

### Form of transaction

#### 4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

No, the types of claims shareholders can bring do not differ depending on the form of the transaction. Needless to say, however, the question of whether a shareholder will be successful in initiating proceedings towards a corporation, its directors or its officers highly depends on the circumstances of the case, which will differ depending on the form of the transaction.

### Negotiated or hostile transaction

#### 5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No.

### Party suffering loss

#### 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes, the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder.

A derivative action, on the basis of which an individual shareholder claims damages in its own name, instead of a claim by the company, does not exist under Dutch law. Under Dutch law, it is not considered appropriate that both the company and the individual shareholders would have the possibility to claim the same kind of damages. For damage suffered by the company, in principle only the company itself is able to start liability claims against directors or officers and third parties.

Therefore, under Dutch law, shareholders are unable to claim damages on the sole ground that the value of the shares has depreciated. Derivative losses do not qualify for compensation. Thus, in the Netherlands there is no such thing as the derivative suit as applied in the United States, or the *action sociale* as applied in Germany and France.

Only under specific circumstances is a shareholder able to claim damages directly from a third party. The Supreme Court held in the *Poot v ABP* judgment that a shareholder is able to claim damages from a third party (including the management of the company in which the shareholder holds shares) if such person did not act in accordance with a specific standard of due care to be observed towards the individual shareholder. In such case, the individual shareholder must prove that he or she has suffered a personal loss. In addition, the shareholder's damage must have become final (eg, the company in which the shares are held will not take legal action itself) (*Dutch Supreme Court, Kip/Rabo and Kessock/SFT*). Only these specific circumstances might give an individual shareholder the possibility to claim damages from the third party or director directly.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

#### 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Dutch law provides for a collective action based on article 3:305a DCC. This article stipulates that a collective action can be instituted by a foundation or association whose statutory goal is to represent the interests

of groups of injured parties having similar damage claims and having a similar interest in holding a third party liable for the damage suffered by such group of injured parties. This means that a shareholder itself cannot pursue a claim on behalf of similarly situated shareholders.

The collective action can (currently) be used to seek a declaratory judgment against the third party that the third party acted wrongfully, so it is not possible to claim damages. Despite the fact that no damages can be claimed through an action based on article 3:305a DCC, such collective actions have been employed successfully to obtain declaratory judgments in which it is confirmed that one or more defendants acted wrongfully and are liable to pay damages. Although individual victims still need to (individually) file follow-on suits to obtain damages (or enter into a settlement with (former) defendants), they can rely on the findings of the court that heard the collective action on common issues such as wrongfulness and the duty of care.

It must be noted that the Dutch Senate approved the legislative bill introducing the collective damages action in the Netherlands on 19 March 2019. The adopted legislation introduces an option to claim monetary damages in a collective action on an opt-out basis. Consequently, it lifts the current prohibition on representative organisations claiming monetary damages in a collective action. The proposed action can either result in a judgment in which the court will award damages or in a collective settlement held to be binding by the court. The date on which the new legislation will enter into force has not been determined yet. The legislation will apply to harmful events that took place on or after 15 November 2016.

### Derivative litigation

#### 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

No. Derivative actions do not exist under Dutch law.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

#### 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

The Enterprise Court may at any time during the inquiry proceedings order interim measures upon the request of the applicant. In takeover situations, these interim measures play an important (often decisive) role in the outcome of the matter. The Enterprise Court can take (inter alia) the following measures: suspending executive or supervisory board members, appointing interim executive or supervisory board members, and suspending shareholders' voting rights.

It is worth noting that it is possible in civil proceedings initiated by the shareholder that the preliminary relief judge of the district court will only grant interim relief measures for the time the Enterprise Court has not decided on the question of interim measures. Such interim relief measures only apply for the time the Enterprise Court has not decided on the question of interim measures. From then on, to avoid contradictory judgments, the measures granted by the Enterprise Court will take precedence.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Only in inquiry proceedings are there grounds upon which the company can seek early dismissal of a shareholder's request to start an inquiry. The request for an inquiry will not be handled by the Enterprise Court if the shareholders have not communicated their concerns about the policies or course of affairs of the company to the board of directors and the supervisory board in written form (prior to initiating inquiry proceedings). The shareholders have to allow the boards reasonable time to respond and to take measures themselves before initiating inquiry proceedings.

### ADVISERS AND COUNTERPARTIES

#### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Shareholders can indeed bring claims against third-party advisers that assist in M&A transactions on the basis of the general tort provision of article 6:162 DCC.

#### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

A shareholder can bring a claim against the counterparty to an M&A transaction. To do so, it will have to demonstrate that the counterparty to the M&A transaction has breached the standard of due care when concluding the contract or the transaction. An example of such a breach by a counterparty to an M&A transaction is continuing to conclude and execute the transaction agreement while knowing that approval from the shareholders' meeting was required but not given (Dutch Supreme Court, *Bibolini*). Such action could result in the annulment of the transaction.

### LIMITATIONS ON CLAIMS

#### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

A director can be discharged by the shareholders from internal liability against the company during the adoption and approval of the annual accounts (articles 2:101 and 2:210 DCC). Such discharge has to be adopted in a shareholders' resolution, and is limited to the information presented in the annual accounts or otherwise provided to the shareholders prior to the discharge. The company can also indemnify its director or officers, although such indemnification is not unlimited (see question 21).

To some extent, the company can indemnify the director against external liability (ie, claims of third parties). Such indemnity could be included in the articles of association or the management or employment contract concluded with the director. Along the same line as regards internal liability, indemnity for external liability may not apply in the event the director's liability is based on intent or deliberate recklessness, or if serious blame can be attributed to the director.

### Statutory or regulatory limitations on claims

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

There are no statutory or regulatory provisions under Dutch law that expressly limit the ability of shareholders to bring claims against directors and officers in connection with M&A transactions. Shareholders have to rely on the general tort provision of article 6:162 DCC to bring their claims. As explained in question 6, the ability of shareholders to bring claims against directors and officers of a company in connection with M&A transactions is limited, because Dutch law does not facilitate derivative actions.

### Common law limitations on claims

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

The Netherlands is a civil law jurisdiction, and it has no common law rules. However, in line with the business judgement rule, the discretionary power of board members is to some extent safeguarded owing to the fact that the Supreme Court has ruled that the board of directors, or directors individually, can be held liable in cases where they are to blame for serious instances of mismanagement (Dutch Supreme Court, *Willemsen/NOM*). As a result, the threshold for liability of board members is higher than it is in other cases of liability, and this offers board members the opportunity to take commercial risks to some extent.

In cases where the conduct of board members or supervisory board members is challenged in inquiry proceedings or proceedings based on article 2:15 DCC, the Dutch Corporate Governance Code and the principles of reasonableness and fairness play a role.

### STANDARD OF LIABILITY

#### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Under Dutch law, shareholders are unable to claim damages against a director on the sole ground that the value of the shares has depreciated. These damages are considered to be derivative losses, which do not qualify for compensation (see question 6). Thus, in the Netherlands there is no such thing as the 'derivative suit' as applied in the United States or the *action sociale* as applied in Germany and France. For a shareholder to successfully bring an action against a director, it is required that a specific rule to be observed towards such shareholder has been breached.

Individual shareholders can initiate a claim against one or more directors or officers arising from a wrongful act (article 6:162 DCC). The Supreme Court has ruled that the board of directors, or directors individually, can be held liable in cases where they can be blamed for serious instances of mismanagement (Dutch Supreme Court, *Willemsen/NOM*). The requirement of a serious imputable act also applies in relation to the 'internal liability' of directors against the company itself (article 2:9 DCC). A claim initiated by an individual shareholder is regarded as the 'external liability' of the directors. The standards of reasonableness and fairness as stipulated in article 2:8 DCC imply that the high threshold of internal liability (ie, the requirement of a serious imputable act) also applies to a claim from an individual shareholder against a director.

In the event it is established that the director has breached a specific rule protecting the shareholder (eg, a rule incorporated in the articles of association), this results – in principle – in the liability of the director against the shareholder.

By establishing a high threshold of directors' liability, the company's interest is served as it prevents directors from being too defensive in their decision-making.

### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

No, the standard does not vary depending on the type of transaction at issue, except for the fact that, as explained in question 6, there will always be regard for the specific circumstances of the case.

### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No, the standard does not vary depending on the type of consideration at issue, except for the fact that, as explained in question 6, there will always be regard for the specific circumstances of the case.

### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

No, the standard does not vary in cases where the directors have a (potential) conflict of interest. It should be noted, however, that articles 2:129(6) and 2:239(6) DCC stipulate that a director shall not participate in the deliberation and adoption of resolutions if he or she has a direct or indirect personal interest that is in conflict with the interests of the company. Should the director – in disregard of these statutory provisions – participate in the adoption of a resolution, such resolution is subject to annulment (article 15(1)(a) DCC). However, the annulment does not affect the authority of the directors to represent the company, unless the third party was aware of the conflict of interest. The directors can be held liable by the shareholders in cases of breaching the decision-making rule on conflicts of interest on the basis of article 6:162 DCC (wrongful act).

Furthermore, the existence of a potential conflict of interest and the failure of a director or officer to address this in a correct way is a violation of the Corporate Governance Code (article 2:391(5) DCC).

### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

The standard does not vary if one or more directors or officers have potential conflicts of interest in relation to the receipt of any consideration in connection with an M&A transaction. It should be noted that the directors shall be guided in the performance of their duties by the best interests of the company and the undertaking connected with it (articles 2:129(5) and 2:239(5) DCC).

## INDEMNITIES

### Legal restrictions on indemnities

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

It is considered to be unacceptable for the company to indemnify the director for any internal liability against the company due to serious mismanagement. This would be in contradiction of article 2:9 DCC as the statutory basis of internal liability against the company. This provision is of a mandatory nature (article 2:25 DCC). However, the director can be discharged by the shareholders from internal liability against the company during the adoption and approval of the annual accounts (articles 2:101 and 2:210 DCC). Such discharge is limited to the information presented in the annual accounts or otherwise provided to the shareholders prior to the discharge.

The company can indemnify the director against external liability (ie, claims of third parties). Such indemnity could be included in the articles of association or the management or employment contract concluded with the director. Along the same lines as regards internal liability, indemnity for external liability may not apply in the event the director's liability is based on intent or deliberate recklessness, or if serious blame can be attributed to the director.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

No, shareholders cannot challenge particular clauses or terms in M&A transaction documents.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

In inquiry proceedings, the Enterprise Court determines whether the company has been mismanaged. The Enterprise Court also assesses the conduct of the shareholders' meeting. In the event that the shareholders (collectively) refuse to vote in favour of a plan in the interest of the company and its continued existence, this may cause the Enterprise Court to decide that the company has been mismanaged.

In relation to publicly traded companies, some resolutions of the board of directors require approval at the general shareholders' meeting when they relate to an important change in the identity or character of the company or the undertaking (article 2:107a DCC). For example, such approval is required in the event of a transfer of the undertaking or virtually the entire undertaking to a third party, or the acquisition or divestment by it or a subsidiary of a participating interest in the capital of a company having a value of at least one-third of the amount of its assets. It could be argued by a defendant that the shareholders in hindsight cannot dispute a decision of the board in connection with an M&A transaction if such decision has been approved by the shareholders.

## Insurance

### 24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

There is an increasing role for directors' and officers' (D&O) insurance. Such D&O insurance can be taken out in relation to both internal liability (against the company) and external liability (eg, against third parties). Possible damages and legal fees can be covered by D&O insurance. Generally, there are different degrees in coverage, such as coverage for personal liability of the director, corporate reimbursement covering indemnities provided by the company and corporate entity coverage, which also protects the company from direct claims.

## Burden of proof

### 25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

Pursuant to Dutch procedural law, in principle, the burden of proof is on the party relying on the legal consequences of certain facts (article 150 Dutch Code of Civil Procedures (DCCP)). An exception to this general principle may apply in cases where the requirement of such proof would be contrary to the standards of reasonableness and fairness (eg, in the event of an unreasonably difficult case caused by the other party).

As a result of this general rule, the burden of proof is often on the shareholders claiming damages from directors or officers on the basis of a wrongful act (article 6:162 DCC). To substantiate their claim, shareholders will have to furnish the facts. If such facts have been contested (with reasons) by the defendants, a claiming shareholder will have the burden of proof as regards the facts that result in the wrongful act. After the submission of evidence by the shareholder, the defendants are allowed to submit counter-evidence.

A 'reversal rule' may mitigate the burden of proof in liability cases. The reversal rule does not result in a shift of the burden of proof. Instead, the causal link between the act and the damage is presumed if the damage results from a breach of a specific rule (eg, in the articles of association) serving the purpose to prevent the occurrence of specific harm to the shareholders, and if the violation of this rule increased the materialisation of the risk the rule envisions to prevent. If so, the directors as defendants have the right to submit counter-evidence in relation to the causal link between the act and the damage.

Inquiry proceedings have their own specific investigative provisions. The inquiry into the management of the company is conducted by experts appointed by the Enterprise Court (article 2:351 DCC). The outcome of the inquiry is an investigative report (2:353 DCC). The decision of the Enterprise Court on whether there has been mismanagement is based on this investigative report.

## Pre-litigation tools

### 26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Under Dutch law, there are various pre-litigation tools that can be used to investigate potential claims. There are no pre-litigation tools specifically available for M&A litigation only.

There is one exception. Shareholders are entitled to request information from the board of directors and the supervisory board. The board of directors and the supervisory board are obliged to provide such information, unless there are compelling reasons not to comply with such request (articles 107(2) and 217(2) DCC). The entitlement of shareholders to information from the company also gives rise to inquiry proceedings before the Enterprise Court (Enterprise Court, *Fortuna*).

The following pre-litigation tools apply to various disputes, including M&A litigation. Pursuant to article 843a DCCP, a party has a right to request documents when the following criteria are met:

- the party making the request has a legitimate interest;
- the party making the request has specified the relevant documents; and
- the documents relate to a legal relationship to which the requesting party or its legal predecessor was a party.

Such a request can be made by submitting a motion during the proceedings or in separate preliminary relief proceedings, and will be assessed by the court. Prior to proceedings, it is possible to order a provisional examination of witnesses or a preliminary expert opinion, or to seize evidence. However, when evidence is seized, this does not automatically give the attaching party the right of inspection. Subsequently, a request on the basis of article 843a DCCP will have to be made.

## Forum

### 27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Unless otherwise provided by the articles of association or shareholders' agreements, there are no specific rules limiting the jurisdiction. It should be noted that the general rule is that the court where the defendant is domiciled has jurisdiction.

## Expedited proceedings and discovery

### 28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

In the Netherlands, it is possible to initiate preliminary relief proceedings. In preliminary relief proceedings, it is possible to obtain a provisional remedy in urgent matters only. A claimant in preliminary relief proceedings could request the judge of the competent district court to order the defendant to comply with a mandatory injunction or a prohibitory injunction subject to a penalty in cases of non-compliance. Such injunctions provide an alternative to the immediate reliefs that can be imposed by the Enterprise Court in inquiry proceedings. It should be noted that a judgment in interim relief proceedings does not prejudice the consideration of the case in proceedings on the merits of the case.

The concept of document discovery or disclosure does not exist under Dutch law. There is, however, the possibility to demand the production of exhibits as explained in question 26 (article 843a DCCP).

## DAMAGES AND SETTLEMENTS

## Damages

### 29 | How are damages calculated in M&A litigation in your jurisdiction?

Pursuant to article 6:95 DCC, damage must be compensated in the event of a statutory ground leading to an obligation to compensate financial loss. Financial loss is further specified in article 6:96 DCC, which states that financial loss comprises both losses suffered and profits lost. In addition, reasonable costs to prevent or mitigate damage, reasonable costs incurred in assessing damage and liability, and reasonable costs incurred in obtaining extrajudicial payment are considered to be included in financial damages.

The main principle under Dutch law is that the aggrieved party should be placed as much as possible in the situation in which it would have been in the event that the damage had not been caused. From

this principle, it follows that only damage actually suffered must be compensated, and that this damage must be fully compensated.

## Settlements

### 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

One special issue under Dutch law with respect to the settling of M&A litigation initiated by shareholders is the possibility to have a collective settlement that can be declared binding for all injured parties in the same situation by the Court of Appeals of Amsterdam (article 7:907 DCC). In this respect, such collective settlement seems only to be of use in cases where many shareholders have suffered (similar) damage. For a settlement to be declared generally binding, a petition has to be submitted to the Amsterdam Court of Appeal. The Court of Appeal will have to determine whether the settlement is reasonable. After the declaration of the Court of Appeal, the injured parties have (at least) three months to choose to opt out of the collective settlement. If it chooses to opt out, an injured party is able to initiate proceedings individually.

## THIRD PARTIES

### Third parties preventing transactions

#### 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Under Dutch law, there are no specific provisions that enable third parties unrelated to the company to initiate legal proceedings to break up or stop a potential M&A transaction. However, in the event such M&A transaction implies a wrongful act against a third party (potentially) resulting in damages, the third party could try to obtain a provisional injunction in preliminary relief proceedings. Subsequently, proceedings on the merits of the case will have to be initiated.

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Under Dutch law, there are no specific provisions that enable third parties unrelated to a company to initiate legal proceedings to enter into an M&A transaction. In addition, the same possibility of initiating (preliminary relief) proceedings applies as described in question 31.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

The board of directors is responsible for determining the strategy of the company, which is supervised by the supervisory board. This means, in general, that the board of directors may decide on a proposal to enter into an M&A transaction without consulting the shareholders. However, the board of directors has to report (afterwards) its strategy to the shareholders in relation to an M&A proposal (Enterprise Court, *Elliott/AkzoNobel*).

By determining the strategy of the company, the board of directors shall be guided in the performance of their duties by the best interests of the company and the undertaking connected with it (articles 2:129(5) and 2:239(5) DCC). The interest of the company lies most often in the advancing of the success of the company. Based on the standards of

reasonableness and fairness that apply to all the parties involved with the company (article 2:8 DCC), the directors have to prevent the interests of other interested parties from being disproportionately harmed owing to pursuing the best interests of the company (Dutch Supreme Court, *Cancun*).

According to the Enterprise Court in the *Elliott/AkzoNobel* decision, directors are generally not obliged to actually enter into negotiations for the purpose of an M&A transaction. Such obligation to enter into negotiations may exist depending on the circumstances of a specific case. The board of directors has no obligation to enter into negotiations against a bidder (in the case of a hostile takeover). The directors of a target company are obliged, however, to respect the justified interests of a bidder, and they are not allowed to disproportionately harm the interests of the bidder by frustrating a (potential) offer (Dutch Supreme Court, *ABN AMRO*).

## COUNTERPARTIES' CLAIMS

### Common types of claim

#### 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

The most common types of claims following M&A transactions result from an alleged breach of the representations and warranties in the share purchase agreement.

### Differences from litigation brought by shareholders

#### 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between the parties to an M&A transaction differs from litigation brought by shareholders as follows.

- The debate in legal proceedings between parties to an M&A transaction is focused on the transaction documents and their clauses. The interpretation and the performance of the contractual provisions will be the main focus of the debate, which often results in claims on the basis of a breach of contract.
- Shareholder litigation is of a very different nature: shareholders only have the ability to bring claims on the basis of mismanagement of the company (inquiry proceedings) or the tortious conduct of the board of directors (either collectively or individually). At the centre of that debate are the actions taken by the corporate bodies and the consequences of these actions for the company. Shareholders find themselves in a difficult position particularly as derivative losses are not eligible for compensation under Dutch law: such damages may be successfully claimed only in cases where a specific standard of due care to be observed towards such shareholder has been breached.

## UPDATE AND TRENDS

### Key developments

#### 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

Owing to the *Poot/ABP*-doctrine in principle the shareholder cannot claim damages from a third party consisting of the depreciation of its shares if the company itself has a claim. As outlined above, a shareholder can claim derivative damages if a third party (i) breached a specific standard of due care towards the individual shareholder and (ii) if the shareholder's damages have become final. Although this doctrine still applies in all its aspects, a tendency in case law is visible showing

that the boundaries of this doctrine are being explored. For example, the Court of Appeal Arnhem-Leeuwarden ruled that two shareholders breached a specific standard of due care towards another shareholder, Barinov. In addition, the court of appeal ruled that the damage suffered by Barinov – the depreciation of the shares' value – was final as there was only a theoretical possibility that the liquidation of the company would result in proceeds for Barinov (Court of Appeal Arnhem-Leeuwarden, *Barinov*).

In disputes arising from M&A contracts, the Supreme Court held that the depreciation of shares is not to be considered derivative damages – and is therefore not covered by the *Poot/ABP*-doctrine – if the share purchase agreement provides that such damage is considered to be direct damage, for example, on the basis of warranties provided in the share purchase agreement (Dutch Supreme Court, *Licorne Holding*).

Another development worth mentioning is that in the Netherlands legislation has entered into force as per 1 January 2019 regarding the introduction of the Netherlands Commercial Court (NCC). Following in the footsteps of some other EU countries, the Netherlands will be the next country in Europe with a special court for international commercial disputes, which facilitates legal proceedings in English. For example, the parties to an M&A transaction could agree on a choice-of-forum clause for the NCC to have jurisdiction on disputes deriving from the M&A contracts. Also, claims against directors could be brought before the NCC upon express agreement by the parties that the proceedings will be held before the NCC in the English language. The NCC does not hear cases within the jurisdiction of the Enterprise Court of the Amsterdam Court of Appeal (eg, inquiry proceedings). The NCC will have its seat in Amsterdam and will operate at a first instance level (as part of the District Court) and at the appeal level (as part of the Court of Appeal).

The logo for Hogan Lovells, featuring the name "Hogan Lovells" in a serif font, with "Hogan" on the top line and "Lovells" on the bottom line, set against a dark grey square background.

---

**Manon Cordewener**

manon.cordewener@hoganlovells.com

**Carlijn van Rest**

carlijn.vanrest@hoganlovells.com

**Bas Keizers**

bas.keizers@hoganlovells.com

---

Atrium - North Tower  
Strawinskylaan 4129  
1077 ZX Amsterdam  
Netherlands  
Tel: +31 20 55 33 600  
Fax: +31 20 55 33 796  
www.hoganlovells.com

# Spain

Jon Aurrecoechea, Eugenio Vazquez and Manuel Martínez

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

There are four claims that shareholders can file in connection with M&A transactions (claims 2 and 3 relate to directors' responsibility).

#### Action 1

The most common claims in shareholder-initiated litigation deriving from M&A transactions are claims between the parties to the M&A transaction, generally based on breach of contract.

The action is usually a damage compensation claim deriving from (mainly) a breach of the representation and warranties of a sale and purchase agreement, or from discussions regarding price-adjustment clauses, although it could relate to other contractual breaches.

There are two types of claims: in a share deal, the buyer or the shareholders (as sellers), or both, can generally claim against the counterparty based on a breach of contract; and in an asset deal, the buyer and/or the company (as seller) can claim against the counterparty based on a breach of contract.

#### Action 2

Social liability action: the company (through an agreement of the general shareholders' meeting), shareholders (holding a minimum capital percentage) and creditors are entitled to claim directors' liability. The purpose of the social liability action is having the liable directors compensate the company for any damage caused.

#### Action 3

Individual liability action: shareholders and creditors individually damaged by directors' actions or omissions (ie, when the damage is not caused to the company itself) can request compensation from the liable directors. The purpose of the individual liability action is having the liable directors directly compensate the shareholders or creditors (as the case may be) for any damage caused.

#### Action 4

The fourth action related to M&A transactions arises mainly in the context of tenders and initial public offerings. Should there be a misrepresentation or inaccurate information in the prospectus (or in the periodic information that should be disclosed by issuing companies), shareholders may assert claims against the corporation, or against the directors or other personnel legally liable for the accuracy of the prospectus, further to sections 38 and 124 of the Capital Markets Act. Section 38 establishes the liability for information (ie, false information or omissions) disclosed in the prospectus, whereas section 124 sets

forth the liability regarding periodic information disclosed by issuing companies. Further to these sections, shareholders are entitled to claim damage suffered.

These four actions are referred to by their corresponding numberings throughout this chapter.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

#### Action 1

In the case of a breach of contract claim, claimants need to prove the breach, the damages suffered and a cause-and-effect relationship between the breach and the damages.

#### Actions 2 and 3

Regarding directors' liability claims (both for social and individual liability actions), claimants must prove that directors acted wilfully or negligently contrary to the law, the company's by-laws or the legal duties deriving from their position. Shareholders must also prove that the corporation (in the case of a social liability action) or the shareholder or creditor (in the case of an individual liability action) suffered actual damage. Finally, it must be proven by the claimant that there is a cause-and-effect relationship between the wilful or negligent behaviour of the director and the damage suffered.

#### Action 4

In the event of claims further to the Capital Markets Act (Action 4), shareholders need to prove the existence of false information or omissions, the damage suffered and a cause-and-effect relationship.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

They apply to both publicly traded and privately held corporations, except in the case of claims further to the Capital Markets Act (Action 4). Actions further to the Capital Markets Act can only be brought against issuing companies (ie, companies subject to the capital market regulations).

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Yes.



In the case of tender offers, Actions 2 and 3 (directors' liability), and Action 4 (claim further to the capital markets regulation), would be available.

In a share deal, Action 1 will be available to the contracting parties.

In an asset deal, the contracting company will have legal standing for a breach of contract claim (Action 1) and shareholders could bring Actions 2 and 3.

In the case of a merger, Actions 2 and 3 would be available for shareholders.

### Negotiated or hostile transaction

5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No.

### Party suffering loss

6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Regarding Action 1, the loss is suffered by the contractual party (a buyer, a shareholder or the company, as the case may be). The damaged party will be the one with legal standing.

In Actions 2 and 3, if the loss is suffered by the corporation, the appropriate way to seek compensation would be a social liability action, whereas if the loss is suffered by a shareholder, compensation would have to be requested through an individual liability action.

In Action 4, shareholders are the individually damaged parties.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

In the case of a social liability action, shareholders (if the general shareholders' meeting does not pass a resolution favourable to suing corporate directors) can file the claim against directors to the benefit of the company (and, indirectly, of the remaining shareholders).

In an individual liability action, shareholders cannot pursue claims on behalf of other similarly situated shareholders.

In claims further to the capital markets regulation, shareholders cannot pursue claims on behalf of other similarly situated shareholders. However, consumer associations can bring collective claims on behalf of consumers that have accepted being part of such claim.

### Derivative litigation

8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Only regarding social liability actions, shareholders holding minimum capital stakes can file actions requesting a director's liability deriving from M&A transactions on behalf of the corporation when the corporation itself (through an agreement of the shareholders meeting) has refused to initiate said actions.

As a way of exception, if a social liability action is based on a breach of the duty of loyalty, shareholders are entitled to directly file a claim against corporate directors, without a previous refusal of the general shareholders' meeting.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

There are three requirements under Spanish law to get interim relief:

- (i) *fumus boni iuris*: the claim must be justifiable on the merits, that is, the requesting party shall be likely to receive a favourable ruling on the merits;
- (ii) *periculum in mora*: there is a real risk that the enforcement of the claim would be frustrated if the petition is not guaranteed during the proceedings; and
- (iii) posting a bond or security to cover potential damage caused to the counterparty.

Even if a claimant could evidence the fulfilment of requirement (i) and offer a bond (requirement (iii)), the *periculum in mora* is hardly ever met in interim relief aimed at preventing the closing of M&A transactions, as the potential damage caused to the shareholders could, in the vast majority of cases, be compensated through a monetary reward.

Spanish courts cannot generally enjoin M&A transactions or modify deal terms.

### Early dismissal of shareholder complaint

10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

This is not applicable. Early dismissal and discovery do not exist under Spanish law (ie, discovery is only available in antitrust damage action claims).

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Technically speaking, shareholders could arguably bring tort claims against third-party advisers that assisted the company in M&A transactions. However, it would be much more natural that these claims against third-party advisers are brought by the corporation itself rather than by the shareholders. Otherwise, directors' liability may arise, and shareholders could file Actions 2 and 3.

### Claims against counterparties

12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Shareholders bringing claims against the counterparties to M&A transactions is far from being usual. There may be very particular circumstances in which shareholders may bring tort liability claims against the counterparties to M&A transactions, but this is not at all common. Claims deriving from M&A transactions are almost always brought by the affected corporation.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

The corporation's constituting documents are a key element regarding Actions 2 and 3. Shareholders may bring claims against directors if it is proven that they failed, wilfully or negligently, to comply, inter alia, with the provisions included in the corporate by-laws, in the regulation of the general shareholders' meeting or in the regulation of the board of directors.

Regarding liability limitation provisions that may be included in the corporation's constituting documents, any limitation provision would be considered null and void.

Directors' and officers' (D&O) insurance, for instance, would be a way to limit the personal exposure of company directors.

### Statutory or regulatory limitations on claims

14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

Shareholders' ability to bring claims against directors cannot be limited by statutory or regulatory provisions.

Indeed, if the company by-laws include any kind of clause limiting shareholders' ability to bring claims against directors and officers, such stipulations would not be accepted by the commercial registry and therefore would not apply. In the very unlikely scenario that a clause like that is accepted (due to the inattention of the registry) it would be null and void.

### Common law limitations on claims

15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Section 226 of the Spanish Corporations Act provides for the protection of directors through the business judgement rule.

Regarding strategic and business decisions subject to the business judgement rule, the standard of diligence of an orderly business person is understood to have been fulfilled when the director acted in good faith, without personal interest in the matter being decided, with sufficient information and further to a proper decision-making process.

## STANDARD OF LIABILITY

### General standard

16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

A general standard is the above-mentioned standard of diligence of an orderly business person.

Additionally, there are differences for determining whether directors may be held liable to shareholders:

- in actions of company directors contrary to the law or the corporate by-laws, there is a presumption of guilty behaviour by the directors. That provision means that the burden of proving the non-existence of guilt lies on the directors; and

- in actions of company directors breaching their legal duties (eg, the duty of diligence, duty of loyalty), there is no presumption of directors' liability. The burden of proof lies on the claimant, who must prove that the director acted wilfully or negligently and that such actions caused damage.

### Type of transaction

17 | Does the standard vary depending on the type of transaction at issue?

Generally not, although regarding Action 4 the standard would be reasonable care and diligence.

### Type of consideration

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

### Potential conflicts of interest

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

The duty to avoid conflicts of interest is included within the broad concept of the loyalty duty of corporate directors. The Corporations Act provides for the regulation regarding conflicts of interests, and sets forth the circumstances in which a director has the obligation to avoid conflict of interest situations.

A violation of such provisions would be considered a breach of the loyalty duty.

Therefore, further to our answer in question 16, the applicable standard in cases of conflicts of interest, as it is technically a breach of a legal duty, is that there is no presumption of directors' liability. Therefore, the claimant will need to prove a breach of the loyalty duty, a damage arising thereof and a cause-and-effect relationship.

### Controlling shareholders

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

Yes, it does.

If a shareholder is part of the M&A transaction, it could file Action 1 (eg, a damage claim for breach of contract).

To the contrary, if the shareholder is a person legally responsible for the accuracy of a prospectus (eg, a corporate director), such shareholder could not arguably bring Action 4 (a claim based on the capital markets regulation).

Regarding Actions 2 and 3 (directors' liability), the ability of shareholders to bring actions would depend on their degree of knowledge and participation on the relevant transaction.

## INDEMNITIES

### Legal restrictions on indemnities

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

This question should not apply to Action 1, as the party to the M&A transaction is generally the company itself.

In Actions 2, 3 and 4, a company cannot indemnify corporate directors (it would arguably be a kind of invalid limitation of liability), and the approving director could face liability.

Regarding advancing legal fees, in Actions 2 and 3, the claiming party is always the company itself (either through an agreement of the general shareholders' meeting, or an agreement by shareholders or creditors on behalf of the company). It would not make sense for the claimant (ie, the company) to advance the legal costs to the defendant (ie, the defendant directors).

In Action 4, any decision to indemnify corporate directors or to advance legal costs could represent a decision under a conflict of interest, because the directors (eg, the board) would be the ones approving such decisions to their own benefit.

Generally, legal costs in this type of claim are initially covered by D&O insurance.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

No, they cannot, if they are not directly part of the transactional documents.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

In an asset deal (Action 1), the decision would be on the board except if the transaction involves assets exceeding 25 per cent of the company's value. In that case, the transaction must be approved by the general shareholders' meeting. Shareholders approving the transaction could have limited possibilities of filing actions against corporate directors, except in cases of concealment of information, or when inaccurate or incomplete information was provided.

Regarding Action 2, the general shareholders' meeting has to approve the filing of a social liability action. However, if the resolution is not favourable, shareholders holding a determined percentage of shares can file a social liability action in the name and on behalf of the company.

Regarding Actions 1 (share deal), 3 and 4, whether to file an action is a personal decision of each shareholder. Therefore, voting is unnecessary.

### Insurance

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

D&O insurance plays an essential role within shareholder litigation arising from M&A transactions. It covers damage caused by directors and officers, normally except in cases of wilful behaviour. It also generally provides for an advance of legal costs to the defendant director.

### Burden of proof

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

Regarding actions or omissions of company directors contrary to the law or the corporate by-laws, there is a presumption of guilty behaviour

by the directors. That provision means that the burden of proving the inexistence of guilt lies on the directors.

Regarding actions or omissions of company directors breaching their legal duties, there is no presumption of directors' liability. The burden of proof lies on the claimant, who must prove that the director acted wilfully or negligently and that such actions caused damages.

### Pre-litigation tools

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Yes, but they are very limited. To prepare a statement of claim, shareholders can request the company to provide very limited types of documents and accounts.

Additionally, shareholders have a limited right to information regarding the matters to be discussed with a general shareholders' meeting.

### Forum

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Regarding Action 1 (share deals and asset deals), the parties are generally allowed to include forum clauses in the relevant contracts, including arbitration clauses.

Regarding Actions 2 and 3, companies can submit their internal disputes to arbitration. Including an arbitration clause in the corporate by-laws requires the favourable vote by two-thirds of the shares. The challenge of corporate decisions by shareholders or directors can also be submitted to arbitration, provided that the proceedings are administered by an institution and that such institution also appoints all the arbitrators.

If no arbitration clause is included in the corporate by-laws, Actions 2 and 3 must be filed in the court of the domicile of the defendant directors. If several directors with different domiciles are sued, the claimant can choose the court that will handle the case.

In connection with Action 4, the claim must normally be filed in the court of the domicile of the defendant. If there is more than one defendant, the claimant can choose the court that will handle the case. However, if the claim derives from a public offering or the claimant is a consumer (eg, a minority shareholder legally qualifying as a consumer), it could file the claim in the courts of his or her domicile.

### Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

No.

## DAMAGES AND SETTLEMENTS

### Damages

29 | How are damages calculated in M&A litigation in your jurisdiction?

Claimants are only entitled to claim actual damage caused to the company by directors' actions or omissions that are duly proven.

The methodology to calculate damages depend on the action filed and the type of damage caused. The usual ways in which experts calculate damages are normally also used in M&A litigation.

## Settlements

30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

There are no special issues regarding settlements.

## THIRD PARTIES

### Third parties preventing transactions

31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

This is not common, but it could happen in very special circumstances (eg, if there is a priority right or a previous transaction by a third party regarding the same assets or shares).

### Third parties supporting transactions

32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Directors must issue a report regarding the proposal stating whether they support the tender offer. They also need to disclose whether there is any agreement between the company or its directors or shareholders and the offeror. Any conflict of interest situation also needs to be disclosed.

Likewise, corporate directors are obliged to request the authorisation of the general shareholders' meeting before executing any action that could jeopardise an unsolicited proposal (eg, selling the company's assets, paying dividends), including approval for the issuance of securities in order to avoid the offeror from gaining control of the company. By way of exception, directors are entitled to look for competing offers.

If an action that could jeopardise the proposal was already approved before the offer was known, directors are also obliged to request confirmation at the general shareholders' meeting.

Directors are further obliged to notify the Capital Markets Commission of any defensive measure approved by the general shareholders' meeting. Before defensive measures are approved, corporate directors must issue a report justifying the proposed measures.

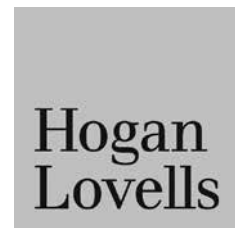
## COUNTERPARTIES' CLAIMS

### Common types of claim

34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

In share deals and asset deals (Action 1), the most common claims are based on a breach of contract. Such claims normally relate to, inter alia:

- a breach of representations and warranties;
- purchase price adjustments;
- contract interpretation;
- material adverse change provisions;
- specific indemnities;
- limitations of liability clauses; and
- a breach of non-compete obligations.



#### Jon Aurrecoechea

jon.aurrecoechea@hoganlovells.com

#### Eugenio Vazquez

eugenio.vazquez@hoganlovells.com

#### Manuel Martínez

manuel.martinez@hoganlovells.com

Paseo de la Castellana, 36-38  
Planta 9  
Madrid 28046  
Spain  
Tel: +34 91 349 82 00  
Fax: +34 91 349 82 01  
www.hoganlovells.com

## Differences from litigation brought by shareholders

35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Actions 1 (in cases of a share deal where shareholders are sellers), 2, 3 and 4 are litigation types brought by shareholders.

Action 1 (asset deals) would be the usual claim deriving from M&A transactions, but shareholders do not normally have legal standing (ie, the asset deal has to be filed by the contracting party, which is normally the company).

That said, whereas litigation involving M&A transactions (asset deals) and shareholder litigation in a share deal are contractual claims based (normally) on a breach of contract, shareholder litigation (Actions 2, 3 and 4) are damage claims against corporate directors or the company (in the case of Action 4).

## UPDATE AND TRENDS

### Key developments

36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

We are seeing quite an intense M&A litigation activity between co-founders and financial entities taking a stake in the share capital of start-ups during financial rounds. In many cases the business plan provided to the investors was not accurate or the co-founders fail to manage the company successfully. Hence, the financial institutions are initiating litigation trying to recover the amounts invested.

# Switzerland

Harold Frey and Dominique Müller

Lenz & Staehelin

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The main claims that shareholders may assert against corporations, officers and directors under Swiss law in connection with M&A transactions are the following:

- challenges of shareholder resolutions and of certain board resolutions;
- liability claims against officers, directors, founders, auditors or any person involved in a merger, demerger, capital increase, conversion of legal form or transfer of assets, or the review thereof; and
- claims for the review and determination of adequate compensation by a court.

These claims are available under the Swiss Merger Act (MA) and/or Swiss corporate law as set forth in the Swiss Code of Obligations (CO).

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

Challenge actions against shareholder or certain board resolutions require the plaintiff shareholders to show that the resolutions violate the corporation's articles of association, provisions or principles of Swiss corporate law, and/or provisions of the MA (board resolutions can be challenged only in the latter case). It is further required that the challenged resolutions affect the plaintiff shareholder's legal position and that he or she did not approve the resolutions. Challenge actions must be directed against the corporation and filed within two months of the adoption of the resolution (in the case of a challenge under Swiss corporate law) or of the publication of the resolution (in the case of a challenge under the MA), respectively, after which the respective claims will be forfeited.

Liability claims against officers, directors, founders or auditors or any person involved in a merger, demerger, capital increase, conversion or transfer of assets, or the review thereof, require the plaintiff shareholder to show that the defendant intentionally or negligently breached a legal duty under Swiss corporate law or the MA; that such breach caused loss or damage to the corporation(s) involved or to the plaintiff shareholder; and that there is an adequate causal nexus between the breach of duty and such loss or damage. Whether the plaintiff shareholder must also establish fault of the defendant or whether fault is presumed (and the defendant must prove he or she was not at fault to escape liability) depends on the specific claims in question and is controversial.

Claims for review and determination of adequate compensation by the court in the context of a merger, demerger or conversion of legal form require the plaintiff shareholder to show that his or her shares or membership rights are not adequately safeguarded, or that the compensation offered is not adequate. Such claims must be filed within two months of the publication of the merger, demerger or conversion resolution, after which the respective claims will be forfeited.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

No. Under Swiss law, the types of claims shareholders can assert do not depend upon whether the corporations involved in the M&A transaction are publicly traded or privately held. Note, however, that in the case of public tender offers, the stock exchange law and regulations apply, and shareholders may resort to the competent authorities in the case of violations of these provisions.

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Yes. Challenges against shareholder or board resolutions under the MA may only be brought in the case of mergers, demergers or conversions of legal form. In the case of other transaction forms, shareholder resolutions may only be challenged under general Swiss corporate law. Liability claims under the MA are only available in the case of mergers, demergers, conversions of legal form or transfers of assets. In the context of other transactions, liability claims against officers and directors, founders or auditors must be brought under general Swiss corporate law. Claims for review and determination of adequate compensation by the court are only available in the case of mergers, demergers or conversions of legal form.

### Negotiated or hostile transaction

- 5 Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No. Under Swiss law, the types of claims do not differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer.

## Party suffering loss

### 6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

No, but this has an impact on who has standing to bring a liability claim: if a loss is suffered by the corporation, liability claims may be brought both by the corporation itself or by individual shareholders. Shareholders can sue either on behalf of the corporation (derivative suit) or in their own right. However, a shareholder who decides to bring an action in his or her own right will be limited to claiming damages directly suffered by that shareholder (see also question 8).

As regards challenges to shareholder resolutions under the MA or requests for review and determination of adequate compensation by the court, only shareholders have standing to bring such claims.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

#### 7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

For the time being, Swiss procedural law does not provide for class actions. Therefore, a shareholder may only pursue claims on his or her own behalf. The limited options for collective proceedings before Swiss courts are through a joinder of parties. Pursuant to the Swiss Code of Civil Procedure (CCP), parties may join their claims and appear jointly in a trial when their case is based on similar factual circumstances or legal grounds. While the concept of joinder may have some advantages for plaintiffs who wish to coordinate their actions (eg, only one evidentiary proceeding, reduced costs and avoidance of conflicting judgments), it is not particularly suited for litigation involving large groups of plaintiffs, as it lacks many of the features and advantages of (common-law types of) class actions. For example, the rules relating to the joinder of parties do not provide for mandatory joint representation. Furthermore, while the CCP does provide for the possibility to bring all the joined claims in the jurisdiction of one single court, this rule does not establish mandatory and exclusive jurisdiction for all claims that are based on the same facts.

### Derivative litigation

#### 8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes, loss suffered by the corporation in connection with an M&A transaction may be claimed by individual shareholders in a derivative action. Such action is not brought in the name of the company but in the name of the individual shareholder. However, the plaintiff shareholder may only request payment of damages on account of the corporation (not the plaintiff shareholder) to compensate for the loss suffered by the corporation.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

#### 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

In the case of urgency, Swiss courts may order injunctive or interim relief in summary proceedings upon a prima facie showing that a right of the plaintiff has been violated or is about to be violated (eg, by a

shareholder resolution that violates principles or provisions of corporate law or the corporation's articles of association, or both), and that such violation will cause the plaintiff irreparable harm. In such proceedings, the court further assesses whether the relief requested by the plaintiff is reasonable and the harm caused to the defendant if such relief was granted is proportionate (balance of the equities). On this basis, a Swiss court may prevent the closing of or enjoin an M&A transaction. In the case of utmost urgency (which is not caused by the plaintiff's delay in applying for injunctive or interim relief), the court may also grant such relief ex parte, subject to confirmation in inter partes proceedings. Note that any interim or injunctive relief granted by a court must be pursued by the plaintiff in ordinary proceedings in order to have a court confirm the right of the plaintiff and the violation thereof.

An interested party (such as, eg, a shareholder) may further file an objection with the commercial register and request that the commercial register is blocked and any applications filed by the company must not be entered into the register. If such objection is filed, the commercial register will not make such entries for ten days. Prior to the lapse of the 10-day deadline, the party which filed the objection must file an application for injunctive relief with the competent court. Unless such application is filed or if the application is dismissed by the court, the commercial register will make the registration applied for by the company. The possibility of any party to seek such a temporary blockage of the commercial register is a powerful remedy against shareholder resolutions which must be registered in the commercial register to have legal effect.

As mentioned in questions 1 and 2, under the MA, upon application by a plaintiff shareholder, a Swiss court may review if the shareholders' membership rights are adequately safeguarded in the context of a merger, demerger or conversion of legal form, and may determine adequate compensation. In that sense, a Swiss court may modify deal terms. However, such action does not enjoin the M&A transaction or prevent its closing. Moreover, adequate compensation is not determined on an injunctive or interim relief basis but in ordinary inter partes proceedings.

### Early dismissal of shareholder complaint

#### 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

No. First of all, Swiss procedural law does not provide for discovery, and it allows only limited disclosure in the context of the court's taking of evidence. There are no specific procedural remedies for parties to seek an early or summary dismissal of claims. However, the court may decide to dismiss claims without the taking of evidence (or ruling on requests for document production) if it finds that the plaintiff failed to state its case or to sufficiently substantiate a claim, or if the court is persuaded based on the available documentary evidence that it may dismiss (or grant) the claims without a need to take further evidence.

In any event, a Swiss court would not proceed with a case if the basic procedural requirements of an action (legitimate interest in the action, jurisdiction, no lis pendens of the same action, no res judicata, capacity to sue, payment of advance on court costs, etc) are not met by the plaintiff at the outset of the litigation. In that case, the court would not even enter the merits of the case, but would rather dismiss the claims on procedural grounds.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

#### 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

In principle, claims against third-party advisers that assist in M&A transactions may only be brought by the parties contracting the services of such third-party advisers: that is, typically the corporation(s) that are assisted by such advisers. However, to the extent third-party advisers are involved in the review of a merger, demerger or conversion of legal form as specifically required under the MA, they may become liable both to the involved corporation(s) and to the shareholders for damage or loss caused by the intentional or negligent breach of their duties. A corporation's auditors who are involved in auditing the annual and consolidated financial statements, the formation of the corporation, and a capital increase or reduction of capital, are subject to a similar liability.

### Claims against counterparties

#### 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

In principle, no. Shareholders may bring claims only against officers, directors, founders or auditors of the corporation in which they hold shares. However, to the extent persons involved in a merger, demerger, conversion or transfer of assets, or the review thereof, breaches duties under the MA that aim at protecting the shareholders of all corporations involved in such transaction, they may be held liable by the shareholders of each of the involved corporations. Moreover, if a counterparty's involvement in the breach of a fiduciary duty by an officer or director of a corporation was of such significance that the counterparty de facto assumed and exercised the role of such officer or director, it could be held liable by the corporation's shareholders as a de facto officer or director.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

#### 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

The articles of association determine a corporation's purpose and may specify the scope of a board member's or executive's duties. Therefore, the articles of association may have an impact on the extent board members or executives can be held liable. However, the articles of association may not validly limit the extent of liability of board members or executives.

A limitation of liability can rather result from a release or waiver of liability claims that may be granted by shareholder resolution. Moreover, under Swiss law, a corporation may agree on a contractual basis to indemnify its board members or executives against liability claims brought by third parties, provided these claims do not stem from a grossly negligent or intentional breach of duties.

### Statutory or regulatory limitations on claims

#### 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

For Swiss corporations, it is a standard agenda item of the annual general shareholders' meeting to resolve whether to release directors and officers from liability. Pursuant to general Swiss corporate law, a release

resolution adopted by the general shareholders' meeting provides directors and officers with a legal defence against a liability action brought by the corporation or by shareholders who consented to the release resolution, to the extent the liability action is based on facts that were known to the shareholders when adopting the release resolution. Such release resolution further limits the non-consenting shareholders' ability to bring liability claims, since the right to bring action of these shareholders is forfeited six months after the resolution of release has been adopted.

In the context of M&A transactions, if the general shareholders' meeting approves a merger or demerger contract or a conversion plan, respectively, such shareholder resolution is generally deemed to have the same effect with respect to such transaction as a release resolution. Therefore, shareholder resolutions approving certain M&A transactions provide the directors and officers with a legal defence against liability claims brought by the corporation or consenting shareholders in the context of such transaction, provided the facts on which such liability claims are based were properly disclosed and, thus, known (or at least easily recognisable) to the shareholders when adopting the resolution.

### Common law limitations on claims

#### 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Switzerland's legal system is based on civil law, not common law. That being said, during the past decade the Swiss Federal Supreme Court has recognised a business judgement rule concept pursuant to which Swiss courts should exercise restraint in reviewing business decisions from an ex post perspective, provided these decisions are the result of a proper decision-making process on the basis of sufficient information and free from conflicts of interest. If these requirements are met, Swiss courts may only review whether such business decision was reasonable and must not review whether the decision was correct in substance.

Moreover, pursuant to general principles of Swiss law, a corporation is estopped from raising liability claims to the extent the corporation or its shareholders consented to the behaviour that allegedly caused damage or loss to the company.

## STANDARD OF LIABILITY

### General standard

#### 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

Whether a board member or executive is in breach of his or her duties is determined pursuant to the specific duties in the context of an M&A transaction as set forth in the MA and pursuant to the general duty of care and loyalty under Swiss corporate law: that is, the duty to apply due diligence and to safeguard the interests of the company in good faith. The standard of care is objective: a Swiss court will assess whether the board member or executive applied the level of care a reasonable person in the position of such board member or executive would be expected to apply in a similar situation. Any failure to meet this standard triggers liability. Even minimal negligence is, in principle, sufficient; in practice, however, the level of negligence (along with other factors, including the application of the business judgement rule) will typically have an impact on the court's determination as to whether a board member or executive is liable.

**Type of transaction**

17 | Does the standard vary depending on the type of transaction at issue?

No. In principle, the standard does not vary depending on the type of transaction at issue. However, a Swiss court would assess the specific transaction situation at hand when determining the level of care expected from a board member or executive in such situation.

**Type of consideration**

18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No. The standard does not vary depending on the type of consideration being paid to the seller's shareholders.

**Potential conflicts of interest**

19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

While the standard does not vary, in the case of conflicts of interest, the Swiss law concept of the business judgement rule (see question 15) does not apply, and Swiss courts may, in principle, fully review whether a business decision taken under the influence of a conflict of interest was correct in substance. While a conflict of interest may be a breach of duty in and by itself, this is not necessarily the case and does not trigger liability automatically. However, according to a recent precedent by the Swiss Federal Supreme Court, where a conflict of interest is established, there is a factual presumption that such board member or executive acted in breach of his or her duties by taking a business decision under the influence of such conflict. This presumption may be rebutted by showing that the corporation's interests were safeguarded despite the conflict of interest.

**Controlling shareholders**

20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

While the standard does not vary, a Swiss court would assess the specific transaction at hand when determining the level of care expected from board members or executives in such situation. Note that in the case of public tender offers, Swiss stock exchange law generally prevents a controlling shareholder from receiving consideration that is not shared proportionally with all shareholders.

**INDEMNITIES****Legal restrictions on indemnities**

21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

It is the majority view in legal doctrine that under Swiss law, a company may advance the legal fees of its officers and directors named as defendants, at least in the case where a liability action is brought by third parties (shareholders). Provided the defendants did not act intentionally or grossly negligently, it is further accepted that the company bears the legal fees of or indemnifies the defendants, respectively. Moreover, it is undisputed and general practice for public and large non-public Swiss companies to contract and pay for

directors' and officers' (D&O) insurance for the benefit of its directors and officers.

**M&A CLAUSES AND TERMS****Challenges to particular terms**

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

In public transactions, the extent to which corporations may agree on certain clauses or terms (offer conditions, break-fees, etc) are limited, and the competent authorities under Swiss stock exchange law review whether a tender offer respects these limits. A shareholder who wishes to challenge such clause may thus apply to these authorities and argue that such clause was in violation of the stock exchange law and regulations.

Outside of the scope of the stock exchange law and regulations, shareholders may only challenge the resolutions of the general shareholders' meeting, and in certain instances also resolutions of the board of directors, which approve a merger, demerger or conversion of legal form, but not individual clauses in M&A transaction documents.

**PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION****Shareholder vote**

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

The vote of shareholders in an M&A transaction, or the approval thereof, respectively, generally strengthens the board's position in M&A litigation. As mentioned above, a shareholder resolution approving a merger, demerger or conversion of legal form is in principle deemed to have the same effect as a release of liability with respect to such transaction, and provides the board members and officers with a legal defence against liability claims (see question 14). At the same time, the challenge of shareholder resolutions in the context of M&A transactions is often the primary means for individual shareholders to challenge the M&A transaction as such and to prevent it from closing.

**Insurance**

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

At least in the case of public or larger private Swiss corporations that regularly contract and pay for D&O insurance (see question 21), such insurance plays an important role in liability actions brought by shareholders against directors or officers (including those arising from M&A transactions).

**Burden of proof**

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

In the case of liability actions against board members or officers, the plaintiff shareholder bears the burden of proof to establish that the defendant breached a legal duty under Swiss corporate law or the MA; that such breach caused loss or damage to the corporation(s) involved and/or to the plaintiff shareholder; and that there is an adequate causal nexus between the breach of duty and such loss or damage. As mentioned in question 2, it depends on the specific claim, and it is controversial whether the plaintiff shareholder must also establish fault of the defendant or whether fault is presumed (and the defendant must prove that he or she was not at fault to escape liability).



In the case of challenge actions against resolutions adopted by the shareholders or (under the MA) against resolutions adopted by the board, it is generally the plaintiff shareholder who bears the burden of proof that the challenged resolution was in breach of provisions or principles of Swiss corporate law, the MA and/or the corporation's articles of association.

### Pre-litigation tools

**26** | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Shareholders in a Swiss corporation have the statutory right to ask the board of directors at the general shareholders' meeting for information on company matters. The board is obliged to provide this information to the extent required for the proper exercise of shareholders' rights, but may refuse to provide information where doing so would jeopardise the corporation's business secrets or other interests worth protecting. Furthermore, a shareholder may only inspect the company's accounts or business correspondence upon express authorisation by a shareholder or board resolution, and if the appropriate measures are taken to protect the corporation's business secrets. If the board refuses to provide the requested information without just cause, the shareholder may apply to a court, which may order the corporation to provide the requested information.

Moreover, any shareholder may request the general shareholders' meeting to have specific company matters investigated by means of a special audit where this is necessary for the proper exercise of shareholders' rights. The main purpose of such special audit is in fact to investigate potential liability claims against board members or executives and to enable shareholders to decide on whether to bring such claims. The right to request a special audit presupposes that the shareholder has exercised his or her statutory right to information and inspection (see above). If the general shareholders' meeting approves the special audit, the corporation or any shareholder may apply to a court within 30 days to appoint an independent special auditor. In the event that the general meeting does not approve the special audit, shareholders who together represent at least 10 per cent of the share capital or hold shares with a nominal value of 2 million Swiss francs may apply to a court within three months to appoint an independent special auditor. They are entitled to such audit despite the general meeting's refusal if they can establish prima facie that directors or officers of the corporation have violated their duties and caused damage or loss to the corporation and/or the shareholders.

### Forum

**27** | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Under Swiss law, both in a domestic and an international context, challenges against shareholder resolutions must be brought at the seat of the corporation. Subject to certain limitations or additional requirements in cases where the defendant resides in a member state of the Lugano Convention, liability actions against directors or officers may either be brought at the seat of the corporation or at the individual defendant's domicile.

Whether forum selection or arbitration clauses in a corporation's articles of association are binding upon shareholders or directors and officers of the corporation is currently subject to debate. To date, forum selection or arbitration clauses are of limited practical relevance for challenges to shareholder resolutions or liability actions. However, the Swiss legislature is currently considering the introduction of a new provision in corporate law pursuant to which the articles of association

may provide that corporate law disputes are subject to the jurisdiction of an arbitral tribunal sitting in Switzerland, and that such arbitration clause is binding upon the corporation, its governing bodies, the directors and officers, and the shareholders. Such a rule, if enacted and eventually implemented by a company, would also limit where the shareholders may bring litigation in an M&A context.

### Expedited proceedings and discovery

**28** | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

As mentioned in question 10, discovery is not available under Swiss procedural law.

In M&A litigation, expedited (summary) proceedings are applicable in the case of requests for interim or injunctive relief (see question 9). If an M&A dispute is subject to arbitration, expedited arbitration proceedings may be available depending on the arbitration clause or the procedural rules agreed upon by the parties (eg, by reference to the rules of an arbitration institution such as the ICC or the Swiss Chambers' Arbitration Institution).

## DAMAGES AND SETTLEMENTS

### Damages

**29** | How are damages calculated in M&A litigation in your jurisdiction?

As for any damage calculation under Swiss law, including in M&A litigation, damage is defined as the difference between the injured party's actual assets and the injured party's hypothetical assets absent the breach of duty that caused damage or loss to the injured party. The injured party bears the burden to substantiate and prove the damage or loss with a high level of detail. If it is not reasonably possible to quantify the damage or loss, a Swiss court may estimate the quantum in its discretion in light of the normal course of events. However, in general Swiss courts are reluctant to exercise this discretion to estimate the damage or loss, and would do so only upon the plaintiff showing that he or she has exhausted all available means to substantiate and prove the damage or loss. While states courts apply very strict, sometimes exaggerated standards regarding the burden of substantiation and proof (and are more inclined to dismiss claims if these standards are not met), arbitral tribunals are often more generous (and also more flexible when it comes to the application of certain valuation methods, eg, for the calculating of future loss of profits).

### Settlements

**30** | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

In the case of a challenge against shareholder resolutions, the defendant corporation (which is represented by its board of directors unless the challenge is brought by the board) may not enter into a settlement agreement with the plaintiff shareholder since the board lacks the power to modify shareholder resolutions. Therefore, such settlement would require shareholder approval. However, settlement agreements under which the plaintiff shareholder withdraws the challenge are permissible.

## THIRD PARTIES

### Third parties preventing transactions

31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Unless such third party has specific contractual arrangements with the sellers or the target company (such as an exclusivity agreement), there is in principle no legal basis under Swiss law for litigation to break up or stop agreed M&A transactions prior to closing. However, to the extent a third party is a shareholder to a corporation involved in an M&A transaction, it may challenge shareholder resolutions that are required in this context, and may cause a transaction to fail through such litigation.

### Third parties supporting transactions

32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Unless such third party has a specific contractual arrangement with the corporation or shareholders under which they are obliged to enter into a certain M&A transaction (and specific performance of such undertaking is practically feasible), litigation is generally not available for this purpose. Shareholders who are dissatisfied with a board's reluctance to enter into M&A transactions may, however, raise pressure, for example by exercising their statutory information and inspection rights (see question 26), by challenging shareholder resolutions or by threatening to bring liability claims in the case of continued inaction. However, it would be difficult for shareholders to hold directors or officers liable for not having entered into M&A transactions except in extraordinary circumstances.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

In the case of an unsolicited or unwanted proposal to enter into an M&A transaction, the board of directors must perform its duties with due diligence and must safeguard the interests of the corporation in good faith. The board is further required to afford equal treatment to all shareholders in similar circumstances.

In the case of a public tender offer, pursuant to the stock exchange law and regulations, the board is obliged to publish a complete and accurate report in which the board comments on the tender offer. Moreover, from the moment in time the tender offer becomes public, the board may not enter into transactions that would have a significant impact on the corporation's assets or liabilities.

## COUNTERPARTIES' CLAIMS

### Common types of claim

34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

The most common types of claims asserted by parties to M&A transactions under Swiss law are claims for breaches of representations and warranties as well as claims for price adjustments or earn-out payments. All of these claims are typically brought post-closing. To a lesser extent, parties to M&A transactions under Swiss law bring:

## LENZ & STAEHELIN

### Harold Frey

harold.frey@lenzstaehelin.com

### Dominique Müller

dominique.mueller@lenzstaehelin.com

Brandschenkestrasse 24  
8027 Zurich  
Switzerland  
Tel: +41 58 450 80 00  
Fax: +41 58 450 80 01

Route de Chêne 30  
1211 Geneva 6  
Switzerland  
Tel: +41 58 450 70 00  
Fax: +41 58 450 70 01

Avenue de Rhodanie 58  
1007 Lausanne  
Switzerland  
Tel: +41 58 450 70 00  
Fax: +41 58 450 70 01

www.lenzstaehelin.com

- claims to enforce exclusivity or confidentiality agreements;
- damages or break-fee claims in relation to aborted negotiations;
- claims to compel the signing or the closing of an M&A transaction; and
- claims arising from a breach of covenants on the target company's conduct of business between the signing and closing.

### Differences from litigation brought by shareholders

35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Disputes arising between the parties to an M&A transaction are often resolved through arbitration, which has in fact become the method of choice for dispute resolution in international M&A transactions. Most parties and M&A practitioners perceive arbitration as a commercially effective means to resolve M&A disputes and prefer it over state court proceedings. The main advantages of arbitration over state court litigation are:

- the possibility to select a neutral forum and to prevent home bias;
- to appoint arbitrators who are experienced in M&A disputes;
- confidentiality of the dispute resolution process; and
- the flexibility to tailor arbitration proceedings to the specific disputes that may arise in an M&A transaction.

In contrast, a challenge of a shareholders' resolution or liability claims brought by plaintiff shareholders in the context of M&A transactions under Swiss law are almost exclusively litigated in front of state courts, and are often a matter of public interest.

**UPDATE AND TRENDS****Key developments****36 | What are the most current trends and developments in M&A litigation in your jurisdiction?**

Litigation between parties to an M&A transaction agreement over breaches of representations and warranties or price adjustments claims is fairly common in Switzerland. It is often resolved through arbitration, in particular in international M&A transactions. While the number of litigations between the parties of these transactions (in particular after closing) has slightly increased during the past decade, there is no clear trend as regards the frequency or the type of disputes arising out of M&A transactions. In contrast, in recent years Switzerland has seen an increasing number of high-profile litigations in the context of unfriendly takeovers and proxy fights. These litigations often involve multiple proceedings, such as requests for injunctive or interim relief in advance of general shareholders' meetings, challenge actions against shareholder resolutions, and liability actions against directors and officers of the corporations involved. Unlike M&A disputes between the transacting parties, these cases are almost exclusively litigated in state courts and often trigger significant public attention. Among the most prominent cases of such M&A litigation during the past few years are the attempted takeover of Sika AG by Compagnie de Saint-Gobain and the proxy fight regarding Schmolz + Bickenbach AG.

# Turkey

Yavuz Şahin Şen and Ebru Temizer

Gen & Temizer | Özer

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The principal contractual documents in relation to M&A transactions are the share purchase agreement executed between the seller and purchaser in respect of the sale of shares in a target entity, and the shareholders' agreement executed between the shareholders of the company. Therefore, the main claims shareholders may assert are contractual claims arising from these documents. The main types of claims in this regard may be categorised as follows:

- claims for breach of representations and warranties or monetary damages or cancellation of transaction in the case of misrepresentation by the sellers;
- indemnity claims arising from an indemnification clause whereby the sellers undertake to indemnify the buyers against any losses arising from situations identified in the contract (such as tax or regulatory claims);
- claims regarding post-closing price adjustments; and
- claims in relation to share option rights.

The relief sought as a result of these claims are usually monetary damages, cancellation of the relevant transaction or declaratory relief in relation to the interpretation of a post-closing price adjustment or option price.

Claims may also be brought by shareholders for breach of the articles of association of a corporation. Depending on the circumstances, such claims may be brought by a shareholder against another shareholder, the corporation itself or the directors for failure to comply with the terms of the articles of association.

While the foregoing claims are the most common claims in practice, the Turkish Commercial Code (TCC) specifically provides that the following claims may also be brought before the courts in relation to a merger process that is conducted in accordance with the provisions of the TCC (pursuant to which two companies are legally merged):

- a shareholder may request compensation in cases where its shareholding or rights could not be protected in a post-merger structure;
- shareholders, the target company or its creditors may raise a tortious-style claim against anyone involved in the merger process where there is a loss due to their negligence in the merger process; and
- shareholders may request cancellation of a merger where it is not conducted properly in accordance with the TCC.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

To bring a successful suit under Turkish law for damages for breach of contract, the shareholders making the claim will have the burden of proof to set out the basis of their claim with concrete evidence. In this respect, the claims must be systematically explained in detail through the lawsuit documents and would typically be supported by an independent expert report (for example, on a technical matter or for quantum), documents and witnesses or similar evidence to prove (i) there has been a breach or contravention of the relevant contract and (ii) the damages resulting from such breach or contravention. However, where the claim only concerns a demand for payment of an undisputed sum for payment (for example, the purchase price) and the defendant to such claim alleges that it has already paid it, the burden is on the defendant to prove through documents evidencing the payment.

Regarding cancellation requests arising from claims under the TCC in relation to a merger, the shareholders must show that the resolutions and procedures in relation to the transaction are contrary to the articles of association or provisions of the TCC.

In cases where a liability claim is raised against a third party involved in the transaction process (such as accountants or financial advisers), the claimants are required to demonstrate the negligence of the third party and prove the loss to be compensated.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes. The Turkish capital markets law (the Capital Market Law No. 6362) (the Turkish Capital Market Law) provides a specific exit right to shareholders in case of mergers or acquisitions that result in a change in control of a public company.

As per article 24 of the Turkish Capital Market Law, shareholders who vote against the merger and who record their opposition in the shareholder meeting minutes have a right to exit through selling their shares to the company in consideration for the average of the daily weighted average price per share on the stock exchange over the thirty day period prior to the date when the merger has been disclosed to the public.

As per article 26 of the Turkish Capital Market Law, where the buyer in a takeover of a public company's shares acquires control of a public company (either through acquisition of over 50 per cent of the shares or board control), the buyer must make a mandatory tender offer to other shareholders to acquire their shares for a price not less than the average of the daily weighted average price per share during the six month period prior to the date of public disclosure of the takeover

offer. Where the buyer fails to put a mandatory offer to the remaining shareholders, the shareholders may bring a lawsuit claiming monetary compensation for this amount plus default interest.

### Form of transaction

4 | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

Yes. While shareholders can bring contractual claims in relation to transactions (ie, breach of representation and warranties, indemnification claims, claims in relation to price, etc), challenges for cancellation of corporate resolutions are only available for legal merger transactions regulated under the TCC.

A sale of assets that constitutes a significant amount of the value of a target company must be approved by a shareholder general assembly resolution with the affirmative votes of shareholders holding at least 75 per cent of the shares of the target company. Therefore, in such an asset sale, shareholders may challenge the general assembly resolution approving such an asset sale transaction.

In relation to public tender offers or mergers, shareholders may enforce their exit rights pursuant to the Turkish Capital Market Law as mentioned in question 3.

### Negotiated or hostile transaction

5 | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

No. The types of claims do not differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer. See, nevertheless, question 3 on the entitlement of public shareholders to be bought out in the event of a mandatory tender offer being triggered regardless of whether such shareholders have contractually agreed or not to sell their shares.

### Party suffering loss

6 | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

The types of claims would be the same for compensation of losses whether suffered by the corporation or by the shareholder directly. Where the shareholder itself suffers loss, it will be the claimant and may request the loss to be compensated directly to itself or through indemnification of the corporation depending on the nature of the loss. If the loss is suffered directly by the company, either the company may make the claim or the shareholders may request compensation to be paid to the company. If the actual loss is suffered by the corporation, then the shareholders may issue the claim themselves (without joining the corporation to the claim) but any compensation would be paid directly to the corporation.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

7 | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

No. A shareholder may only pursue claims on his or her own behalf and there is no concept of class or collective action through which a selected claimant can effectively pursue a claim on behalf of others. As per Turkish Civil Procedure Law, where claimants have a common claim as a result of losses arising from the same transaction, facts or

legal causes, claimants may jointly file a lawsuit against defendants or seek permission from the court for the cases to be joined. However, a shareholder may not represent claims of other persons except where a person has agreed to assign the cause of action (and is permitted to do so) to another shareholder.

In Turkish litigation practice, sometimes shareholders who suffer a loss in connection with a transaction may appoint the same legal counsel to bring a joint claim against the defendant. Even in such cases, this would not constitute a collective action on behalf of other shareholders.

### Derivative litigation

8 | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes. Where a loss is suffered by the corporation, the corporation, its shareholders or its creditors may bring a lawsuit for payment of compensation to the corporation. Such a lawsuit is not brought on behalf of or in the name of the corporation but by the shareholder itself. However, the relief sought by the shareholders may only be in the form of compensation payable to the corporation. The shareholder should follow the standard civil litigation procedure and file lawsuit before the commercial courts of first instance in the defendant's headquarters or (if it is a real person) place of habitual residence. The relief section of the petition should explicitly state that compensation is sought to be paid to the corporation. There is no requirement under this procedure to join the corporation itself to the proceedings.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

As per Turkish Civil Procedure Law, a court may award injunctive or other relief to prevent closing of an M&A transaction if the claimant can satisfy the court that the following alternative conditions are met: (i) it will be significantly harder or impossible for the claimant to be entitled to its rights owing to a change in the current situation (ie, as a result of closing of the transaction) or (ii) significant irreparable damage will occur due to failure to award interim relief. The courts conduct a prima facie examination for injunctive relief requests. In cases of urgency, requests for injunctive relief may be sought ex parte provided that the main claim relating to the dispute is brought within two weeks as of the date of the award of relief. Violation of an award of injunctive relief is subject to punitive sanctions of up to 6 months imprisonment and any transaction violating the injunctive relief may be cancelled by the claimant.

Regarding the second part of the question, the courts have limited powers to enjoin or force parties to close an M&A transaction for example through an order for specific performance. Such a remedy is not recognised in Turkish law specifically in the meaning of the common law equivalent. However, where there is a contractual right to call for the transfer of shares (or a similar right such as a right of first refusal) given in favour of a party to an M&A transaction, such option may be enforceable against the counterparty provided that the shares have not already been sold to a bona fide third party. In this case, the courts may only order compensation to be paid to the holder of the right in accordance with article 49/II of the Turkish Code of Obligations.

Finally, the Turkish courts may issue declaratory relief that the transaction is invalid or void if it breaches the TCC or the articles of association. However, the court may not modify deal terms except under

application of the 'theory of imprevision' (or onerous circumstances) pursuant to article 138 of the TCC. This enables the court to adapt the provisions of a contract to current circumstances in cases where the terms of a transaction have significantly changed owing to the occurrence of events beyond the control of the parties and such change means that performance of the obligations of either party under the transaction effectively becomes impossible. However, such intervention by the court to modify deal terms is extremely exceptional and highly unlikely to be awarded especially given the emphasis in the TCC and Code of Obligations on freedom of contract and the concept of prudent commercial parties who are taken to understand the risks associated with a commercial transaction. The Turkish courts will generally respect the will of the parties to a transaction provided that it complies with general principles of corporate law, the TCC (and Capital Markets Law where applicable) and the articles of association.

### Early dismissal of shareholder complaint

#### 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

There is not an early dismissal or summary judgment procedure in Turkish civil procedure law such as through a prima facie examination of the facts. However, where a lawsuit does not meet certain formalistic conditions, the courts may dismiss a lawsuit before it examines the merits of the case. These conditions are: (i) jurisdiction, (ii) standing of the claimant, (iii) payment of court fees, (iv) that there is no ongoing lawsuit for the same claim and (v) that a final decision has not already been rendered on the same claim (*res judicata*). If these conditions are satisfied the court will proceed to examine the merits of a case. However, for instance, if the claim is related to the rights of a shareholder and the claimant is not a shareholder, then the court would dismiss the lawsuit due to lack of standing.

There is no process of disclosure or discovery of documents under the Turkish civil procedure system akin to that in common law jurisdictions. Parties to a dispute will attach to their pleadings the evidence on which they intend to rely. A party would need to make a specific application to court that the opposing party disclose a document or evidence that it holds that a party is aware of and on the grounds that it is relevant to the case during the course of a proceeding.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

#### 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Yes. In principle, shareholders may bring claims against any third party (including advisers) that is involved in an M&A transaction where the shareholder suffers losses arising either from a formal contract (such as an engagement letter) to which the shareholder (or company) is a party or based on the tortious concept of 'unjust action' by a third party. Shareholders bringing claims against third-party advisers must prove that the advisers acted negligently or fraudulent in relation to its services and that losses arose as a result of such negligence or fraud. In practice, advisers usually protect themselves from such claims through agreements with express limitations or disclaimers.

### Claims against counterparties

#### 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

In principle, the shareholder of a party (ie, corporation) to a transaction may only bring a claim against the directors of the company for

breach of fiduciary duty. However, for mergers and demergers, as per article 193 of the TCC, any person involved in a merger and demerger processes are liable against the company, its shareholders or creditor where it suffers losses.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

#### 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

The liability of directors is regulated under the TCC. The main basis of a director's liability is for negligence in the execution of his or her duties of due care and diligence to act for the benefit of the company of which he or she is a director. The term 'negligence' is construed very strictly in this context. This is because of the 'business judgement' rule that has been introduced through article 369 of the TCC. According to this rule, it is assumed that directors have acted in accordance with the fiduciary standards of loyalty, prudence and care in reaching business decisions. Unless it is apparent that the directors have blatantly violated these rules of conduct, their commercial decisions should not be second-guessed by the court.

As a general principle the statutory duties of directors may not be limited by any of the corporation's constituting documents including the articles of association. However, shareholders may release directors from their liabilities in relation to a certain period (such as a financial year) through a general assembly resolution following the end of the relevant period (and not before). However, this type of release is limited and would not apply to losses arising out of an action that is not disclosed in the financial statements or that is dishonestly concealed, and would not operate to limit liability to third parties.

Furthermore, as described in question 15, while the general supervisory duty of care of board members may not be limited by the corporation's constituting documents, it is possible for board members to assign specifically defined roles to defined third parties such as senior managers of the corporation pursuant to the power under article 370/II of the TCC.

### Statutory or regulatory limitations on claims

#### 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

No. Shareholders may bring claims against directors and officers in connection with any transaction in accordance with the principles explained under question 13. Where the directors are released from their liability as a result of a general assembly meeting, the shareholders may not bring any claim against the directors for the period that they are released unless the exceptions referred to above apply.

### Common law limitations on claims

#### 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Turkish law is not based on common law and the liabilities of directors are regulated under the TCC. There are certain rules that impair shareholders' ability to bring claims against the directors as described in question 13 in relation to the 'business judgement' rule of reasoning. Accordingly, the relevant provision in the TCC is designed on the basis that commercial risk is part of the ordinary course of business and

courts should not second-guess the appropriateness of commercial decisions by directors.

Additionally, directors are permitted to delegate certain authorities to other persons pursuant to the articles of association. There are certain non-delegable duties such as the overall obligation to supervise the company. However, where certain delegable duties are expressly delegated to defined persons (eg, the CEO to execute a specific type of transaction) the directors may not be held liable for the decisions and actions of these nominated persons provided that the directors can demonstrate their care and diligence in choosing the delegates.

## STANDARD OF LIABILITY

### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

As we explained above, the liability of directors are subject to the business judgement rule that enables directors to make commercial decisions without being subject to second-guessing by the court. Whilst there is not a general rule specifically related to M&A transactions, the courts would apply this rule to a specific case considering objectively whether the director breached his fiduciary duty, good faith, obligation to perform his or her duty with diligence and care through wilful misconduct. The court would assess whether the director can be objectively said to have applied the level of care expected of a diligent person in the position of such director.

### Type of transaction

- 17 | Does the standard vary depending on the type of transaction at issue?

No. The basis of liability claims are the general provisions of Turkish corporate law so the court would examine the facts relevant to a specific dispute when applying the standard of care.

### Type of consideration

- 18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

### Potential conflicts of interest

- 19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

Yes. As per article 396 of the TCC, directors may not engage in any transaction that may compete with the business of the company without obtaining the prior approval of the general assembly of the shareholders. In such circumstances the relevant transaction would be void or invalid if the relevant disclosure is not made or approval is not obtained.

Additionally, as per article 393 of the TCC, the directors may not participate in any negotiation in relation to a transaction that potentially creates conflict of interests between themselves or their relatives and the company. Otherwise, the relevant board of directors resolution approving the transaction would be invalid and the director and other directors who allowed the director to participate in the negotiations would be liable for potential losses incurred by the company.

## Controlling shareholders

- 20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

Potentially this may be the case. The standard of liability of directors is general and abstract, and accordingly does not vary depending on specific circumstances. However, of course, the courts would examine the specific transaction brought before it and determine whether the act of the directors would fall under the scope of the business judgement rule or a more specific statutory restriction applies (such as those listed above: restriction against personal benefit from transactions). Where the directors are found to be in breach of that standard, the court may hold them liable for an act that may otherwise appear as an ordinary commercial decision.

If the consideration in connection with a transaction is not shared rateably according to the shareholding and such variation has not already been agreed between the shareholders (for example, through a liquidation preference in the articles of association or shareholders' agreement or other form of express consent), a shareholder could potentially bring a claim against the directors or the company for inequitable treatment that is a core protection for shareholders under article 357 of the TCC. The claim would need to demonstrate that the difference in allocation of the share price could not be justified on objective grounds, for example, that the shares being sold were all of the same class to which the same rights were attached.

## INDEMNITIES

### Legal restrictions on indemnities

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

In Turkish law, there is no provision imposing a specific restriction on a company's ability to indemnify directors or officers named as defendants. However, as per article 395, the directors may not engage in any transaction with the company without the prior approval of the general assembly of shareholders. Indemnification of directors by the company would be considered a 'transaction' for the purpose of this article. Shareholders who oppose such approval may request cancellation of the relevant general assembly resolution, for example, where the indemnification is only in favour of shareholder directors who approve the transaction or such indemnification would create inequality between shareholders.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

- 22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

If a shareholder is a party to an M&A transaction document then it may seek to challenge or renegotiate clauses during the course of negotiations.

Where the shareholder is a third party that is not a party to the transaction document itself then it may challenge provisions in an M&A transaction document on the basis that it does not comply with a principles of corporate law, provision of the TCC and the articles of association of the company or (if it is a public company) the Capital Markets Law. The court may either cancel the general assembly resolution that approves the transaction or request the company to remedy the

non-compliance. Therefore, if a particular clause of an M&A document that is subject to approval of the general assembly would be challenged by a shareholder who opposes the transaction in the general assembly meeting, for example on the basis that the transaction restricts its rights unequally or violates the Turkish Commercial Code or the articles of association, the court may review the claim and order the company to remedy such violation. However, there is no general right of shareholders to challenge clauses that would preclude third-party bidders and it is a common feature of private and public M&A transactions to agree provisions that tend to give a third-party bidder exclusivity for a defined period and provide compensation in the event of breach of such exclusivity.

In addition, shareholders of public companies who oppose a merger resolution are entitled to exit by selling their shares to the company. In case of change of control in the company, the acquiring third party must make a tender offer to the remaining shareholders and such shareholders may enforce their right to sell.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

**23** | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

A shareholder vote allows shareholders to subsequently challenge an M&A transaction. However note that shareholders who approve or who do not specifically record their opposition to an M&A transaction on a shareholder vote may not bring a claim for cancellation of the transaction.

### Insurance

**24** | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors and officers liability insurance is a type of professional liability insurance that directors are permitted to obtain under the Turkish Commercial Code. Where liabilities arising from potential M&A transactions are not exempt from the scope of D&O liability insurance, shareholders may address the claim for compensation of losses to the insurance company. It is a standard provision of insurance policies in the Turkish market that claims brought before a foreign court and arbitration are not covered with such insurance unless otherwise specifically agreed with the insurer.

### Burden of proof

**25** | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The burden of proof in an M&A litigation is not different from the general civil litigation rule: the burden of proof is borne by the party that brings the claim. In this respect each party must prove what it alleges before the court. Similarly, in M&A litigation, the claimants bear the burden of proof to establish the basis of relief sought.

As there is no legal presumption that applies in favour of the shareholder making the claim, such burden generally does not shift in M&A litigations.

### Pre-litigation tools

**26** | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Yes. One of the statutory shareholder rights that may not be restricted is the right of the shareholder to be informed about the company. As per article 437 of the Turkish Commercial Code, the right to be informed covers rights of access to financial statements, the annual activity report of the board of directors, audit reports and proposals in relation to dividend distribution. These must be kept ready for review by shareholders at least 15 days prior to the proposed general assembly meeting.

Shareholders are also entitled to obtain information from the auditor or the board of directors during the course of the general assembly meeting. In case where the questions raised in the general assembly meetings are not satisfactorily responded to, the shareholder may review the corporate books and correspondences related to such question provided that the general assembly approves this request. Where the general assembly unfairly refuses this request, the shareholder may apply to the court to exercise its right to examine the corporate documents.

The information obtained is often an effective means of enabling shareholders to develop their claims.

### Forum

**27** | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

Yes. In principle, parties may freely choose the jurisdiction of a dispute that may arise from private contracts such as a share purchase agreement. However, forum selection clauses are not permitted in the constitutional documents of a Turkish company such as the articles of association, which are subject to the exclusive jurisdiction of the Turkish courts.

Further, certain types of dispute will be subject to the jurisdiction of the Turkish courts by their nature. Where the relief sought in M&A litigation is the cancellation of the decision of a shareholder or board meeting of a Turkish company, such as an annual general assembly resolution, this must be filed before the Turkish court located within the relevant district of the registered address of the company.

### Expedited proceedings and discovery

**28** | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

No. Litigation that is suitable for expedited proceedings are strictly listed pursuant to the Turkish Civil Procedure Law and M&A litigation is not listed in the law as being suitable for expedited litigation process.

Discovery is not permitted under Turkish civil litigation procedure. Parties are not permitted to engage in processes of discovery of the other side's documentary evidence.

## DAMAGES AND SETTLEMENTS

### Damages

**29** | How are damages calculated in M&A litigation in your jurisdiction?

There is not a specific method for the calculation of damages arising from an unlawful act of third parties or breach of contract. Turkish courts almost always appoint an expert committee to calculate the damages of



the claimant in case of compensation claims. Damages are generally calculated by comparing the value of the asset that the claimant has acquired prior to and after the transaction that is subject to the dispute. The court will distinguish between losses that are directly linked to the transaction or reasonably linked to the transaction if the loss is consequential. The court conducts an objective evaluation and does not take claimant's subjective plans into account in assessing damages (eg, plans to sell the shares and invest them in a fund with a high rate of return). The principles of equity and fairness are also considered during the calculation of damages to ensure damages are proportionate and linked to the breach that is the subject of the claim.

### Settlements

#### 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

Lawsuits for cancellation of general assembly resolutions are filed against the company, not the other shareholders. Therefore, in case of such lawsuit, the company is not entitled to settle with the claimant by way of agreeing not to implement a resolution on behalf of or instead of the general assembly. The only settlement in such cases may be made if the claimant agrees to withdraw the lawsuit either voluntarily or in return for an agreed sum.

There is no special form for settlement of disputes (such as that it be executed in a particular way or before a notary public). The advantage of executing a settlement before a notary public is that neither party may deny the validity of its signature on the settlement.

## THIRD PARTIES

### Third parties preventing transactions

#### 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Only the parties to a transaction, or its shareholders, may request cancellation of the transaction. Third-party creditors of a company may only have standing to bring a claim based on director negligence and that the losses arising affected the position of creditors. However, such an action would not stop the transaction process and is merely a monetary compensation. Therefore, other third-party buyers would be rather unlikely to have standing to break up or stop agreed M&A transactions.

### Third parties supporting transactions

#### 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

The Capital Markets Law and the TCC allow minority shareholders in certain circumstances to sell their shares to the company or to force an acquirer of control over a public corporation to make a tender offer to minority shareholders. However, in the absence of a specific transaction, there is no practice in Turkey of using litigation to force corporations to open themselves up to third-party buyers.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

#### 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Directors must carry out their duties transparently and with due care and diligence in the case of an unwanted or unsolicited proposal to enter into an M&A transaction and safeguard the rights of shareholders.

## GEN & TEMIZER ÖZER

### Yavuz Şahin Şen

ysen@gentemizerozzer.com

### Ebru Temizer

etemizer@gentemizerozzer.com

Levent Cad. No: 18  
34330 Levent-Besiktas  
Istanbul  
Turkey  
Tel: +90 212 260 34 00  
Fax: +90 212 260 34 04  
www.gentemizerozzer.com

In the case of deals that trigger a mandatory tender offer owing to a change of control, the directors are responsible for compliance with the Capital Markets Law and determining the fair value for the shares (on the calculation basis stipulated in the Capital Markets Law) where it would result in a mandatory tender offer.

## COUNTERPARTIES' CLAIMS

### Common types of claim

#### 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

The most common type of claims asserted by and against counterparties to an M&A transaction are indemnification or monetary claims due to breach of representation and warranties as well as claims relating to purchase price adjustments or earn-out claims.

### Differences from litigation brought by shareholders

#### 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between parties to an M&A transaction are generally based on contractually agreed provisions in the transaction documents. These documents often contain arbitration clauses and therefore in cases of dispute the parties to a transaction start proceedings in accordance with the arbitration rules of the relevant body or organisation.

However, where the shareholders are not a party to an M&A transaction, they are not bound with the jurisdiction clause and their most common form of action is usually to challenge the general assembly resolution approving the transaction. Such challenges must be brought before the local courts pursuant to Turkish law.

**UPDATE AND TRENDS****Key developments**

36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

Following the establishment of the Istanbul Arbitration Centre (ISTAC), there is an increasing trend to use ISTAC in jurisdiction clauses where one or more of the parties to an M&A transaction is Turkish. While the International Chamber of Commerce is still a preferred arbitration institution in cross-border M&A transactions, the establishment of ISTAC has increased the popularity of arbitration in Turkey by introducing the concept of resolution by way of arbitration to a wider group of Turkish businesses. We expect this trend to continue for the foreseeable future.

# United Kingdom

Neil Mirchandani, John Tillman and Katie Skeels

Hogan Lovells International LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

Directors owe duties under the Companies Act 2006 (CA 2006) and also owe fiduciary duties to the company they serve. In respect of an M&A transaction, the most important duties owed by a director are:

- to act in a way that he or she considers, in good faith, would promote the success of the company for the benefit of the shareholders as a whole;
- not to exercise his or her powers for an improper purpose, such as issuing new shares in the company for the purpose of reducing the influence of dissenting shareholders;
- to avoid conflicts between his or her own interests and those of the company, and to declare any interest he or she may have in the proposed transaction;
- to exercise independent judgement; and
- to exercise reasonable care, skill and diligence.

The most likely claim against a director or officer is that, in pursuing a transaction, he or she acted in breach of one or more of these duties.

As a general proposition, such duties are owed to the company, and the cause of action therefore vests in the company and not in any individual shareholder. Furthermore, individual shareholders are, on the whole, prevented from disputing any course of conduct by the company that has been approved by a majority of shareholders.

However, there are certain specific remedies available to individual shareholders, which are principally a derivative claim by a shareholder on behalf of a company; an unfair prejudice petition by a shareholder; and a petition for the company to be wound up on just and equitable grounds.

These remedies require court action, and there are high hurdles to overcome to get proceedings for these started in the courts (explained further in question 2). For these reasons, claims for these remedies are not particularly prevalent in the English courts.

In rare cases, a shareholder may also have a direct cause of action against the directors or officers, or against third parties, on the basis that a duty that was owed personally to him or her has been breached. For example, a shareholder who voted on a transaction on the basis of a company circular that he or she subsequently alleges to have been misleading may seek a remedy directly from the directors in his or her own name. A director may also owe a fiduciary duty to a shareholder depending on the existence of a special factual relationship, for example in relation to the disclosure of material facts or an obligation to use commercial or confidential information to benefit the shareholders. However, a court will not permit a shareholder to make such a claim where the loss he or she is seeking to remedy is merely a reflection

of a loss suffered by the company (eg, a diminution in the value of the shareholder's shares) – which in practice can be a real stumbling block for shareholders seeking to bring claims.

Finally, a shareholder in a public company may have a claim against a director responsible for listing particulars and prospectuses if the shareholder acquired or contracted to acquire securities to which they applied, and he or she has suffered loss as a result of any untrue or misleading statements in the particulars or prospectus, or through any omission of information otherwise required to be included (section 90, Financial Services and Markets Act 2000 (FSMA)).

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

First, a derivative claim against a director or third party can be pursued by a shareholder on behalf of a company, if a court gives permission, where there has been any actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director (or shadow director) of the company. For example, by causing the company to engage in corrupt or illegal conduct, or in respect of fraudulent accounting irregularities. A claimant must obtain permission from the court to continue a derivative claim, which the court may give at its discretion. The claimant shareholder must be able to demonstrate that he or she has a prima facie case. The court must refuse permission if it considers that a person acting in accordance with the statutory duty to promote the company's success would not seek to continue the claim, or if the act or omission complained of has been authorised or ratified by the company (and the court may in fact adjourn the proceedings to allow such ratification to be obtained); the court may also refuse permission based on a number of other factors including the absence of good faith by the applicant in bringing the claim or the availability of a personal remedy which the applicant could bring against the company in his own name.

Second, a petition alleging unfair prejudice can be brought by a shareholder where the company's affairs are being conducted in a manner that is unfairly prejudicial to the interests of some or all of its shareholders as shareholders; or a current or proposed act or omission would be unfairly prejudicial to the interests of some or all of its shareholders as shareholders.

The complaining shareholder must be able to show that unfair prejudice has in fact been suffered. Unfair prejudice petitions may be appropriate in many different circumstances, for example where a shareholder has an expectation to be included in the management of a company but has been excluded; in the case of excessive remuneration of the directors, inadequate payment of dividends or loss of confidence in the management of the company; or, in respect of an M&A transaction, if the directors take action to thwart a prospective transaction that is in the company's interests. A court will decide on a case-by-case basis

whether a petitioning shareholder has adduced sufficient evidence to establish the relevant unfair prejudice and its seriousness.

On a successful derivative action or unfair prejudice claim, the court has a wide discretion to impose such remedy as it sees fit. In particular, it can order a company to refrain from or carry out particular acts – although it is unlikely that a court would order an M&A transaction to be stopped or to force one to go ahead. A court could also order, in respect of an unfair prejudice petition, that the petitioner’s shares in the company be purchased at a fair price.

Third, a petition for the company to be wound up on just and equitable grounds can be brought by a shareholder. The just and equitable grounds are not exhaustively defined, but can include circumstances where there has been a justifiable loss of confidence in the management arising from serious mismanagement, or mismanagement which frustrates proper and legitimate expectations. It is important to note that an order will not be made where another remedy is available to the petitioner: this is a remedy of last resort and therefore rarely granted.

All breaches of duty (statutory or fiduciary) are capable of ratification by an ordinary resolution of the shareholders (over 50 per cent of votes cast) at a general meeting if there is full disclosure of all material circumstances, which in practice can nullify any claim centred on that breach of duty by a minority shareholder who did not support the ratification (however, see question 14).

**Publicly traded or privately held corporations**

**3** | Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Shareholders in publicly traded and private companies are equally eligible to bring the claims explained in questions 1 and 2. In addition, further claims or grounds for claims may arise:

- in respect of public companies, by virtue of their regulation by the Takeover Code and, where their shares are publicly traded, the UK Listing Rules or the AIM Company Rules and related legislation that applies to quoted companies such as the Market Abuse Regulation. For example, Class 1 and related-party transactions by publicly traded companies require shareholder approval; and
- in respect of private companies, by virtue of any additional obligations or restrictions imposed under the company’s articles of association or any shareholders’ agreement.

**Form of transaction**

**4** | Do the types of claims that shareholders can bring differ depending on the form of the transaction?

The basis of any claim is likely to be as explained in questions 1 and 2. However, the formulation of the claim may differ depending on the form of the transaction complained about. For example, in the case of a tender offer, the bidder makes an offer to the target’s shareholders and the shareholders are the selling parties who approve the transaction, whereas, in the case of an acquisition or disposal by a company of a business or the share capital of a subsidiary, it is the company that is the party to the relevant transaction and its board of directors makes the decision to buy or sell.

**Negotiated or hostile transaction**

**5** | Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

In principle, the types of claims available would not differ. However, similarly to question 4, the nature of the transaction may affect the

formulation of a claim because acceptance of a hostile offer for a public company would not, at least when made, be recommended by the directors of the target company and the offer would be successful only if a sufficient number of shareholders accepted the offer (however, see question 1 in relation to a potential claim for misleading statements). A negotiated transaction would normally require only the approval of the board of directors of the selling company (in the case of an asset or subsidiary sale or purchase, if shareholder approval is not required by the UK Listing Rules, or any shareholders’ agreement or the company’s articles of association).

**Party suffering loss**

**6** | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

This is a critical issue in English law where a shareholder tries to commence a personal claim against a director or a third party. As explained in question 1, he or she will be precluded from making such a claim if the loss he or she is looking to recover is merely reflective of loss suffered by the company that it can claim for in its own name (eg, a diminution in the value of his or her shareholding). Such circumstances, however, are not prima facie a bar to a shareholder commencing a derivative claim, unfair prejudice petition or petition for winding up.

**COLLECTIVE AND DERIVATION LITIGATION**

**Class or collective actions**

**7** | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Collective action by shareholders is possible under English law. First, a shareholder is able to bring or continue a claim as a representative for one or more other persons with the same interest in that claim. Second, a court may consolidate claims by multiple claimants together, using its case management powers, or claims can be brought jointly. Third, a court may make a group litigation order whereby multiple claims giving rise to the same issues are grouped together and managed according to specialist procedural rules.

Any new claimant must actively ‘opt-in’ to benefit from the collective action being brought.

On a successful collective action according to any of the three methods above, judgment will be binding on all claimants involved.

Notably, there have historically been very few collective shareholder actions in the UK. This may arise, in part, because English law does not make any presumption of reliance (such as a ‘fraud-on-the-market’ doctrine) by any shareholder on the company’s conduct giving rise to the alleged loss; individual reliance must be shown by each claimant shareholder. There is also a limited body of English jurisprudence regarding the correct calculation of damages in collective actions. However, this may change in light of an increasing public sentiment in the UK to hold the directing minds of a company ‘to account’.

**Derivative litigation**

**8** | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

As explained in questions 1 and 2, a shareholder can bring a derivative action on behalf of a company in limited circumstances.

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

- 9 | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

It would be open to a shareholder to seek (final) injunctive or interim relief to prevent a transaction closing, and the courts have a wide discretion to make appropriate orders if:

- in the case of an interim injunction:
  - there is a serious issue to be tried; and
  - the balance of convenience requires that an order be made, namely that damages would not be an adequate remedy if the claimant were to succeed at trial, a cross-undertaking in damages would adequately protect the respondent from any relief subsequently judged to have been wrongly granted and any other factors relevant to the balance of convenience justify the making of the order sought; and
- in the case of a final injunction at the conclusion of a trial where a claimant has established a legal or equitable right and the court considers it just to exercise its discretion to make such an order.

The same tests apply whether the injunction sought is prohibitory (requiring a person not to carry out a wrongful act) or mandatory (requiring a person not to continue a wrongful omission, or to undo the consequences of a wrongful act), although historically the courts are more reluctant to grant the latter.

As explained in questions 1 and 2, a court also has a wide discretion to grant an appropriate remedy on a successful derivative claim or unfair prejudice petition. However, a court is unlikely to make an order preventing a transaction from closing, and is further unlikely to modify or redraft the terms of a proposed transaction.

### Early dismissal of shareholder complaint

- 10 | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

If a shareholder complains by making a derivative claim, he or she must seek the permission of the court to continue that claim (explained further in question 2).

Furthermore, a defendant or respondent to a derivative claim, unfair prejudice petition or petition for winding up could apply for its early dismissal by:

- applying for summary judgment on the claim where, on the basis of either a relevant point of law or the evidence adduced, the claimant has no real prospect of succeeding in his or her claim, and there is no other compelling reason why the claim should wait to be disposed of at trial; or
- applying for a strike-out of the claimant's statement of case where:
  - it discloses no reasonable ground for being brought;
  - it is an abuse of the court's process;
  - it is otherwise likely to obstruct the just disposal of proceedings; or
  - there has been a failure to comply with a procedural rule.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

A shareholder may be able to bring a claim against a third-party deal adviser if he or she can establish that he or she was owed:

- a duty of care by that third party not to be negligent because the damage he or she has suffered was foreseeable, there was sufficient proximity between him or her and the adviser, and it is fair, just and reasonable in the circumstances for a duty of care to be imposed; or
- a duty of care by that third party not to make negligent misstatements where the adviser assumed a responsibility towards the shareholder.

In practice, it may be difficult to establish that a third-party deal adviser did owe a shareholder a relevant duty of care: the tests to be satisfied are restrictive. In addition, such an adviser usually contracts directly with the company, and in such circumstances the courts have rarely found that a collateral duty is owed in favour of a shareholder. Furthermore, if the company has a readily available remedy against the adviser for all of the loss suffered as a result of the wrongdoing, then the shareholder's personal claim will be barred under the principle of reflective loss (as explained further in questions 1 and 6).

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

In principle, a shareholder could bring a derivative claim or an unfair prejudice petition against a director and a third party (eg, a counterparty to an M&A transaction) who participated in the director's wrongdoing where the claim arises out of the director's breach or the shareholder obtains the court's permission. On either cause of action, the court could order relief against a third party.

If the shareholder was seeking recovery of loss from a third party unconnected with any wrongdoing by a director, he or she may have a personal claim against the party concerned if he or she could establish that he or she was owed an independent duty by that party, and the loss he or she is seeking to recover is not merely reflective of the company's loss.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

Directors have a duty to comply with a company's constitutional documents, which may impose more rigorous standards than those in the CA 2006.

English law does not allow a director's duties or liabilities to be diluted or limited by the company's articles of association.

**Statutory or regulatory limitations on claims**

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

A derivative claim may not be brought where the act or omission has been authorised or ratified by the company. In respect of such authorisation or ratification, the vote of the director whose actions are being challenged or of any connected person must be disregarded.

An act or omission complained of cannot be authorised or ratified if it can be regarded as a 'fraud upon the minority', for example where the complaining shareholder has no other remedy and the directors have used their power to benefit themselves at the expense of the company, or where the relevant action involves an attempt by majority shareholders to expropriate shares held by the minority.

Authorisation or ratification does not preclude an unfair prejudice petition.

A court also has the power to relieve a director of liability entirely or in part in any proceedings for negligence, default, breach of trust or duty if it appears that he or she acted honestly and reasonably and, having regard to all of the circumstances, he or she ought fairly to be excused under section 1157(1) CA 2006. If a director suspects that a claim may be made against him or her, he or she can apply for pre-emptive relief. Relief is likely to be granted only in limited circumstances, such as where a director has acted honestly and on legal advice and had no alternative course of action.

**Common law limitations on claims**

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

The CA 2006 requires that a director, in carrying out and complying with his or her duties, exercises the care, skill and diligence of a reasonably diligent person. The director must satisfy an objective test: that he or she has acted with the general knowledge, skill and experience that can reasonably be expected of a person carrying out the functions carried out by that director. He or she must also satisfy a subjective test: that he or she has acted with the general knowledge, skill and experience that he or she actually has.

The duties imposed on directors allow, prima facie, for the scrutiny of directors' conduct by the courts. For example, an allegation that a director has acted in breach of his or her duty to promote the success of the company for the benefit of its shareholders as a whole ostensibly requires the courts to examine the reasoning of the director, and the factors that he or she took into account in managing the company, and in taking decisions and acting in the way he or she did.

The intention behind the legislation is to impose a high standard on directors. However, a court is likely to be slow to second-guess a director's good faith discretionary decision.

Note also our comments in question 14 regarding the court's ability to relieve a director of liability.

**STANDARD OF LIABILITY****General standard**

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

See question 15.

**Type of transaction**

- 17 | Does the standard vary depending on the type of transaction at issue?

No.

**Type of consideration**

- 18 | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

No.

**Potential conflicts of interest**

- 19 | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

The standard of care owed by a director does not vary depending on whether he or she has a potential conflict of interest in connection with an M&A transaction.

However, a director has a duty to notify the other directors of any interest he or she may have in a proposed transaction or arrangement with the company, and (save to the extent authorised by shareholders or, where permitted, the other directors) to avoid an actual or potential conflict as regards matters other than a proposed transaction where in either case the situation can reasonably be regarded as likely to give rise to a conflict of interest. In addition, the company's articles of association will often contain provisions regulating the situation and, in most cases where a director has any material conflict in relation to a proposed transaction, he or she will either as a matter of law or best practice recuse him or herself from any board decisions regarding the matter.

**Controlling shareholders**

- 20 | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

As explained in question 19, the applicable standard of care does not vary.

Where the company is involved in the transaction, its directors will have a duty to ensure that the transaction is in the interests of the company as a whole and not just that of the controlling shareholder.

**INDEMNITIES****Legal restrictions on indemnities**

- 21 | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

The CA 2006 prohibits a company from indemnifying or exempting a director of the company, or of an associated company, from any liability in connection with any negligence, default, breach of duty or breach of trust by him or her in relation to the company.

However, there is a specific exception that, subject to certain requirements, allows a company to indemnify directors in respect of liabilities arising from proceedings brought by third parties (eg, class actions or actions brought by shareholders following M&A or share issues). In addition, companies may purchase directors' and officers' insurance to protect directors from loss resulting from claims made against them in relation to the discharge of their duties as directors, and the constitution of a UK company will often expressly permit the purchase of such insurance (on which, see question 24).

## M&A CLAUSES AND TERMS

### Challenges to particular terms

22 | Can shareholders challenge particular clauses or terms in M&A transaction documents?

A shareholder has no personal right to challenge the terms of an M&A transaction.

However, as explained in question 1, a director has a duty, *inter alia*, to act in the best interests of the company. If the particular M&A term is damaging to a company's interests, a shareholder may be able to raise an argument that in agreeing to it the director has breached this duty. However, the CA 2006 makes it clear that the decision as to what will promote the success of the company, and what constitutes such success, is one for a director's good faith judgement. As such, unless a director's good faith can be impugned, a court is unlikely to determine that a decision has not been properly made.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

23 | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

See question 14.

### Insurance

24 | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Directors' and officers' (D&O) insurance policies typically cover the directors and officers of the company for claims made directly against them that are not subject to an indemnity from the company (known as 'Side A' cover); and the company itself in respect of any reimbursement or indemnity paid to the directors and officers arising from a claim against them (known as 'Side B' cover).

Whether directors and officers are able to rely on an indemnity from their company in particular circumstances will depend on the nature of the claim. As a result, Side A claims will typically be claims made against directors by the company itself or by shareholders, whereas Side B claims will typically be claims made by third parties.

In addition, D&O insurance policies usually provide cover in respect of directors' defence costs, so that the costs of defending a Side A or Side B claim that are reasonably incurred will typically be covered, subject to approval by insurers. If there is an open question as to cover under the policy, insurers may approve defence costs incurred subject to a reservation of rights.

Therefore, D&O insurance provides an important protection in respect of shareholder and derivative claims both for individual directors and officers (in cases where their company cannot indemnify them) and for the company itself (if it is in a position to provide an indemnity to the relevant directors or officers). Whether a particular shareholder claim will attract cover under any given D&O policy will of course depend on the nature of the claim and the specific terms of the relevant D&O policy.

### Burden of proof

25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The shareholder bringing the claim has the burden of proof, and the burden does not shift in the course of proceedings.

### Pre-litigation tools

26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

A shareholder has limited rights to access company records or obtain company information. In particular, a shareholder has no general right to inspect documentation such as board minutes or general financial records.

Shareholders have a statutory right to receive copies of various reports and records that directors have statutory obligations to prepare or maintain, such as annual accounts and statutory registers. However, these documents may postdate any act or omission complained of, and may provide only limited information to assist a shareholder with his or her complaint.

A shareholder may apply for pre-action disclosure of company records before commencing a claim if:

- he or she and the respondent are likely to be parties to subsequent proceedings;
- the respondent's duty to give disclosure in any proceedings would extend to the requested documents; and
- the disclosure is desirable to dispose fairly of the proceedings, assist the resolution of the dispute and save costs. However, this is not an easy test to meet.

Furthermore, a company may argue that certain documents are privileged, although such claims will only be sustained if the document was created in connection with actual, threatened or contemplated litigation with the shareholder. Otherwise, a company has no general right of legal privilege against its shareholders.

Finally, a shareholder may be able to rely on a right to copies of documents or other information contained in a shareholders' agreement or the articles of association. Conversely, the articles of association or any shareholders' agreement may place additional restrictions on a shareholder's access to information.

### Forum

27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

A company's articles of association can contain an enforceable choice of jurisdiction clause, which may dictate where any proceedings by a shareholder against the company or a director can be brought.

Otherwise, the appropriate forum would ordinarily be the company's place of incorporation.

### Expedited proceedings and discovery

28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

A court is able to expedite proceedings using its general case management powers, but this is a matter of judicial discretion and requires grounds of genuine urgency.

Generally, parties to English proceedings are obliged to give disclosure. This has traditionally been on the basis of what is called standard disclosure, comprising a reasonable search for and production of documents that:

- are within that party's control and on which he or she relies;
- adversely affect or support his or her or another party's case; or
- he or she is otherwise required to disclose under the English civil procedure rules.

Recent disclosure reforms (which apply to most commercial cases) have now introduced a menu of approaches to disclosure for a court to select on the basis of what is appropriate and proportionate in a particular case. The extent of a party's disclosure obligations under this new scheme could vary from a wide search for relevant material (akin to standard disclosure), to more narrow issue or request-based searches, or to 'known adverse documents' only.

Parties are not obliged to disclose documents that are legally privileged: see question 26 in relation to the assertion of privilege by a company against a shareholder. Issues can also arise where a party alleges that a document is not disclosable because it is not within his or her control, or does not fall within the test for standard disclosure (or whichever other test is ordered to apply), either of which may be contentious areas in an M&A dispute if a shareholder is seeking documents that arguably belong to a counterparty. Disclosure can be ordered against a non-party if the documents sought are likely either to support the case of the applicant or adversely affect the case of one of the other parties to the proceedings, and such disclosure is necessary to dispose fairly of the claim or to save costs, which may prove useful to a shareholder in relation to a dispute over an M&A transaction.

Confidentiality obligations may be cited by a company in refusing to give disclosure of particular documents. However, in a recent decision it has been emphasised that the public interest in the fairness of proceedings accorded by the parties giving full disclosure of all relevant material overrides the public and/or private interest in maintaining a particular confidentiality. In *Omers Administration v Tesco plc* [2019], an ongoing shareholder class action against Tesco plc in the High Court brought under section 90A FSMA, it was held that Tesco must disclose documents that the Serious Fraud Office (SFO) had originally obtained from third parties (including interview transcripts and witness statements) in the context of a criminal investigation into a Tesco subsidiary. The SFO had subsequently provided these documents to Tesco's legal representatives on a confidential basis expressly for the use in negotiating a deferred prosecution agreement between the SFO and its subsidiary. Tesco argued, inter alia, that disclosure should be withheld on the basis of the public or private interests in the confidentiality of the materials given their source and the circumstances in which Tesco received them. Nevertheless, the court emphasised the primacy of full disclosure of relevant materials in ordering that the documents be disclosed.

If a party considers that inadequate disclosure has been given by another party, he or she can apply to the court for an order for specific disclosure requiring either the disclosure of particular documents that are currently absent, or that the party conduct specific searches for further documents that he or she is then obliged to disclose. If a party is still dissatisfied with the disclosure given, he or she has the following options:

- an application for contempt against the party giving disclosure, on the basis that the disclosure statement confirming the adequacy of disclosure given was falsely signed; or
- an application for disclosure of specific documents on an 'unless' basis: ie, unless the disclosure is made, that party will be sanctioned, for example, by having all or part of his or her claim struck out.

## DAMAGES AND SETTLEMENTS

### Damages

29 | How are damages calculated in M&A litigation in your jurisdiction?

The calculation of damages depends on the nature of the claim, the alleged wrongdoing and the particular remedy that was sought at the outset.

The court has a wide discretion to order an appropriate remedy in respect of a successful derivative claim. The court could order a payment to the company in compensation for any loss suffered, an account of profits or an appropriate order against a third party joined to the proceedings.

In relation to an unfair prejudice petition, the court has a similarly wide discretion, but its purpose in granting relief is specifically to remedy the unfair prejudice suffered by the shareholder. This is a very wide discretion, and could result in, for example, an order for the purchase of the minority shareholder's shares by the majority at a fair value or price to be determined by the court or otherwise, (rarely) an order for the purchase of the majority's shares by the minority, an order for an inquiry for the benefit of the company, an order to authorise the bringing of civil proceedings on behalf of the company or an order to regulate the company's affairs in the future.

### Settlements

30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

There are no special issues.

## THIRD PARTIES

### Third parties preventing transactions

31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Third parties are unlikely to have any direct causes of action in respect of an M&A transaction, but they may seek to intervene, for example, on the basis that the transaction is in breach of competition law, or that the board is acting improperly or not in the shareholders' best interests.

Such third parties might seek to buy shares in the company concerned in order to advance such arguments as a shareholder.

### Third parties supporting transactions

32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

No.

## UNSOLICITED OR UNWANTED PROPOSALS

### Directors' duties

33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

Where an M&A transaction involves the acquisition of assets from the company concerned, the directors of the company will need to determine whether entry into the transaction is in the company's interests and that there is no statutory or other legal requirement for the directors to involve shareholders in the decision (unless the company is party to an agreement that requires this or the transaction otherwise requires shareholder approval, for example, under the UK Listing Rules).

Where the proposed M&A transaction is the acquisition of the company's existing share capital (which would normally be effected by an offer to the company's shareholders in the case of most private companies), the directors of the company will normally not have any specific involvement in the transaction unless the company is subject to the UK City Code on Takeovers and Mergers (Code) or the company has a significant number of shareholders. The rules and general principles of the Code regulate the conduct of UK public takeovers, as well as



certain takeovers where there is a shared jurisdiction between the UK and other EEA countries, and is administered by the Panel on Takeovers and Mergers. Under the Code, the directors of a target company must, inter alia:

- provide shareholders with their opinion on the offer and their reasons for forming their opinion;
- obtain competent independent advice as to whether the financial terms of the offer are fair and reasonable; and
- make known the substance of that advice to the shareholders.

## COUNTERPARTIES' CLAIMS

### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

Litigation between counterparties to an M&A transaction may involve warranty claims and, in rare cases, misrepresentation claims. Where there are earn-out entitlements following an M&A transaction, litigation can ensue if the entitlements are disputed.

### Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Litigation between counterparties does not tend to involve issues concerning the correct claimants and defendants, which is a common feature of shareholder litigation. In addition, the issue of reflective loss (explained further in questions 1, 6 and 11) does not arise between counterparties.

## UPDATE AND TRENDS

### Key developments

- 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

The significant growth in the litigation funding market in the UK is having an increasing effect in the shareholder litigation space.

Litigation funding is where a third party agrees to finance the legal costs of a litigant in return for a fee to be paid out of any proceeds if the litigation is successful. Litigation funding is legal in the UK, and there is now even a Code of Conduct of the Association of Litigation Funders designed to regulate and undoubtedly raise the profile of litigation funding in the UK. As at 2018, the estimated value of global assets under management by the 16 main litigation funders in the UK was over £1.5 billion (up from £180 million in 2009). Litigation funding can be an attractive prospect to litigants without access to significant legal budgets or those who wish to share the risk of litigation, or for commercial reasons.

Litigation funding has been behind a number of shareholder class actions in recent times, and it has the potential to get M&A litigation off the ground where it otherwise wouldn't.

As already mentioned above, there have also been a number of recent actions where shareholders have taken action collectively. Such collective action can be facilitated, in part, by the presence of litigation funding, and there is also an increasing market for boutique law firms who specialise in identifying cases ripe for collective action. Enormous tactical advantage can be achieved by taking collective action, and it has resulted in some positive settlements for shareholder litigants in the past few years.

However, one should not underestimate the practical implications of one firm managing collective claims by a multitude of claimants. The



#### Neil Mirchandani

neil.mirchandani@hoganlovells.com

#### John Tillman

john.tillman@hoganlovells.com

#### Katie Skeels

katie.skeels@hoganlovells.com

Atlantic House  
Holborn Viaduct  
London EC1A 2FG  
United Kingdom  
Tel: +44 20 7296 2000  
Fax: +44 20 7296 2001  
www.hoganlovells.com

same procedural and evidential burdens of pursuing litigation in the English courts apply, and it is unlikely that a court would sympathise with incomplete pleadings, failures to comply with any court timetable, gaps in the evidence or an absence of key witnesses. The way in which collective claims are managed and pursued is therefore of vital importance to their success. It is also apparent that the management of collective claims could be ripe for abuse by unscrupulous individuals; this is another area of concern to be carefully managed for a successful collective action.

Finally, while the number of shareholder activism campaigns has remained relatively static in the UK, there is evidence that shareholders are adopting more US-style tactics to challenge issues such as remuneration and corporate governance. Such action is not necessarily litigious, but shareholder claims may be used if traction is not being gained by other methods.

# United States

William M Regan, Jon M Talotta and Ryan M Philp  
Hogan Lovells US LLP

## TYPES OF SHAREHOLDERS' CLAIMS

### Main claims

- 1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The claims typically asserted by shareholders in connection with M&A transactions arise out of the fiduciary duties owed by boards of directors to companies and their constituents. Corporate directors owe a corporation and its shareholders two principal fiduciary duties: the duty of care and the duty of loyalty. These two duties generally encompass a number of related duties, such as the duty of disclosure (or *can-dour*), the duty of oversight and the duty of good faith.

After an M&A transaction is announced, the seller's shareholders frequently assert breach of fiduciary duty claims alleging that the board of directors agreed to sell the company for an inadequate price following the conclusion of an unfair or conflicted sales process, or both. In addition, shareholders often challenge the adequacy of the seller's disclosures in connection with a transaction, including, in particular, disclosures provided in the materials used to solicit shareholder votes on the transaction.

The law governing a board of directors' fiduciary duties is the law of the state where the company is incorporated. In the United States, the majority of large public companies are incorporated in Delaware, which has a well-developed and widely followed body of case law concerning M&A transactions. Other states have broadly similar fiduciary duty rules, but may differ on particular points of law. In the interest of brevity, this chapter discusses the most common or generally applicable US legal concepts in the context of an M&A litigation and not the law of any particular state.

### Requirements for successful claims

- 2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

To successfully bring a breach of fiduciary duty claim, shareholders generally must show the existence of a fiduciary duty and a breach of that duty. For claims alleging a breach of the duty of care, shareholders must show that the defendant did not use the amount of care that an ordinarily careful and prudent person would use in similar circumstances. For claims alleging a breach of the duty of loyalty, shareholders must show that the defendant failed to act in the best interest of the corporation and its shareholders. To successfully bring a disclosure claim under state law, shareholders must show that the defendant failed to disclose fully and fairly all information that is material to a shareholder's decision.

In recent years, many courts have become increasingly sceptical of disclosure claims brought under state fiduciary duty law. As a result, many shareholders now bring disclosure claims under the US federal

securities laws. Such claims require shareholders to demonstrate that a disclosure document failed to accurately disclose material information relating to an M&A transaction. In certain cases, the false or misleading statement must be intentional and not merely negligent or inadvertent.

### Publicly traded or privately held corporations

- 3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes. In the context of public M&A transactions, shareholder claims typically are brought derivatively, on behalf of the corporation, or as a class action, and the claims are premised on the fiduciary duties owed by the company's directors to the company or the requirements of US federal securities laws governing disclosures to shareholders. By contrast, in the context of privately held corporations, claims typically are brought by the buyer or buyers, or the seller or sellers, and arise out of the parties' contract or direct dealings. Claims in private M&A transactions most frequently involve purchase price adjustment or earn-out disputes, indemnification disputes arising from contractual representations and warranties, and fraud claims based on alleged misstatements or omissions that induced one party to enter into the contract.

### Form of transaction

- 4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

In certain cases, yes, but not in others. For example, in the public M&A context, shareholder claims alleging state law breach of fiduciary duty will not necessarily differ if a transaction is structured as a merger instead of a tender offer. For disclosure claims brought under federal law, however, shareholder claims vary depending on the structure of the transaction. For example, certain US courts have held that shareholders challenging disclosures in connection with a tender offer under section 14(e) of the Securities Exchange Act of 1934 must show that the speaker acted with *scienter* or the intent to deceive investors and satisfy heightened pleading standards. In contrast, in a merger structure where shareholders challenge proxy disclosures under section 14(a) of that same statute, most courts hold that shareholders do not need to establish that a false or misleading statement was intentional.

### Negotiated or hostile transaction

- 5 Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

As a general matter, the fiduciary duties of a board of directors do not differ depending on whether the transaction is negotiated or is the result of a hostile or unsolicited offer. In both circumstances, the board

is required to act in a fully informed manner, with the requisite level of care, and in the best interests of the company and its shareholders. In the context of a hostile or unsolicited offer, it is generally accepted that a target board may, in appropriate circumstances, act consistently with its fiduciary duties by resisting or rejecting a hostile or unsolicited offer. However, where shareholders challenge affirmative conduct by a company to resist a hostile or unsolicited offer, such as the implementation of a 'poison pill' or shareholder rights plan, the board's conduct will be evaluated under more rigorous standards of review designed to ensure that the board is acting to protect shareholder interests.

### Party suffering loss

**6** | Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes. Claims for losses suffered by a corporation typically belong to the corporation. Therefore, for the shareholder to bring claims on behalf of the corporation – that is, derivatively – the law imposes several threshold requirements that a shareholder must satisfy to have standing to bring corporate claims. Shareholder derivative actions seek recovery for the benefit of the corporation as a whole. In contrast, where the loss is suffered by shareholders, as distinct from the corporation itself, one or more shareholders may seek to pursue direct recovery from the alleged wrongdoers (including recovery from the corporation). Such 'direct' actions frequently seek recovery on behalf of a group (or class) of shareholders, and thus must satisfy different procedural requirements that apply to class actions. Recovery in a class action belongs to the shareholders, not the corporation.

In M&A transactions, courts typically hold that shareholders have direct claims when asked to vote based on misleading disclosures or when forced to exchange shares for inadequate consideration.

## COLLECTIVE AND DERIVATION LITIGATION

### Class or collective actions

**7** | Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Yes. In instances where a loss is suffered directly by individual shareholders, as distinct from losses suffered by the corporation, shareholders may seek to bring a class action lawsuit on behalf of themselves and other similarly situated shareholders. To commence a class action lawsuit, the named plaintiff must meet several requirements designed to ensure that prosecution of claims on a class-wide basis is necessary and practical, and that the named plaintiff is properly situated to act on behalf of the class.

Among other things, a proposed class representative must show that:

- the class members are so numerous that it would be impracticable to join them all in a single litigation;
- there are common questions of law or fact applicable to all class members;
- the proposed representative's claims are typical of all class member claims; and
- the proposed representative will adequately represent the interests of the absent class members.

In addition, the proposed class representative must show that common questions predominate over any individualised issues applicable to the class members.

### Derivative litigation

**8** | Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes. Where a loss is suffered by the corporation, rather than shareholders individually or as a group, shareholders may bring derivative actions on behalf of the corporation. To have standing to bring a derivative claim on behalf of the corporation, a shareholder must meet strict requirements intended to determine whether it is appropriate to vest the shareholder with authority to bring claims belonging to the corporation. One threshold issue is whether the shareholder makes a demand on the corporation to take action in response to allegedly improper conduct. To proceed with a derivative action, a shareholder must either make a demand on the board that is wrongfully refused, or demonstrate in the complaint that any such demand would have been futile. Further, a derivative plaintiff must remain a shareholder from the time of the challenged transaction until the conclusion of the litigation.

Derivative claims arise more frequently in connection with failed M&A transactions (eg, where a board of directors terminates a deal or changes its recommendation and thereby causes the company to pay a substantial termination fee to the counterparty).

## INTERIM RELIEF AND EARLY DISMISSAL

### Injunctive or other interim relief

**9** | What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Due to the impracticability of unwinding a transaction after it has closed, US courts have the discretion to issue an injunction to prevent the closing of an M&A transaction in certain circumstances, including where the disclosures fail to provide shareholders with adequate information, or the deal protection provisions in the M&A agreement improperly preclude other potential bidders from coming forward or coerce shareholders into voting in favour of the transaction. Although the injunction standard differs slightly from jurisdiction to jurisdiction, most courts consider whether there is a reasonable probability that the movant will succeed on its claim, whether the movant will suffer imminent and irreparable harm, and the balance of the equities. Rather than enjoin a transaction, courts also in limited circumstances may strike objectionable deal terms.

### Early dismissal of shareholder complaint

**10** | May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Yes. Defendants may seek early dismissal of a shareholder complaint by filing a motion to dismiss. Defendants may seek dismissal of shareholder derivative and class actions on the ground that the shareholder plaintiffs fail to meet one or more of the procedural requirements for commencing such an action. Defendants also may seek dismissal of shareholder claims on the ground that the complaint fails to adequately state an actionable claim.

## ADVISERS AND COUNTERPARTIES

### Claims against third-party advisers

- 11 | Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Yes. The most common claims against third-party advisers are based on financial advisers' undisclosed conflicts of interest. Typically, such claims have been asserted on the theory that conflicted financial advisers aided and abetted breaches of fiduciary duty by the board of directors. For example, shareholders have asserted claims against financial advisers who provided fairness opinions to the target, but had undisclosed financial incentives related to the buyer. However, aiding and abetting liability only will be imposed based upon knowing misconduct.

### Claims against counterparties

- 12 | Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Yes. Generally, efforts to achieve a better deal through arm's-length negotiations will not give rise to liability, but liability for aiding and abetting may arise in very limited circumstances where, for example, a party intentionally creates or exploits a conflict of interest. In addition, shareholders may bring claims against a counterparty based upon allegedly false or misleading disclosures, such as where a joint proxy is issued or in connection with a tender offer.

## LIMITATIONS ON CLAIMS

### Limitations of liability in corporation's constitution documents

- 13 | What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

Many state corporation statutes permit corporations to include in their charter a provision eliminating director monetary liability for breaches of the duty of care. Such provisions make it difficult for shareholders to prevail in post-closing damages cases where the core contention is that the directors should have or could have obtained a better price when selling the company.

However, exculpatory provisions of this kind do not eliminate director monetary liability for breaches of the duty of loyalty or for actions undertaken in bad faith. Nor do these provisions prevent a shareholder from pursuing a claim for non-monetary relief (eg, an injunction against consummation of an M&A transaction), or from pursuing a claim for monetary damages for actions undertaken by an officer of the corporation.

### Statutory or regulatory limitations on claims

- 14 | Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

As a general matter, there are no statutory or regulatory provisions precluding such claims, but as noted above there are procedural rules applicable to shareholder class and derivative actions challenging M&A transactions. A shareholder class action asserting claims under the federal securities laws also must comply with the requirements of the Private Securities Litigation Reform Act of 1995.

## Common law limitations on claims

- 15 | Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Under traditional common law, most decisions by disinterested directors receive the protections of the business judgement rule. This doctrine provides a presumption that directors making a business decision acted on an informed basis, in good faith and in the honest belief that the action was taken in the best interests of the company. A plaintiff can rebut the business judgement rule by demonstrating a breach of the directors' obligations of good faith, loyalty or due care (eg, by proving corporate waste). When the business judgement rule applies and is not rebutted, a court will not second-guess director decisions.

## STANDARD OF LIABILITY

### General standard

- 16 | What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

There are three primary standards for assessing director conduct in M&A transactions: the business judgement rule, enhanced scrutiny and entire fairness.

### Business judgment rule

As discussed above, when the business judgement rule applies, courts generally will not second-guess the decisions of directors.

### Enhanced scrutiny

An intermediate standard of review applicable to M&A transactions involving control of a company that requires directors to satisfy certain conditions before they will enjoy the benefits of the business judgement rule. For example, forms of enhanced scrutiny apply to transactions involving a break-up of a corporation and to defensive measures adopted by directors in response to a potential change in control.

### Entire fairness

Courts will require directors to prove the entire fairness of an M&A transaction in which a majority of directors are interested or that involves a controlling shareholder. The defendants bear the burden of proving entire fairness.

In many litigations involving M&A transactions, the standard of review that the court chooses to apply will be dispositive. Where a court applies the business judgement rule, decisions made by a board of directors are upheld in the vast majority of cases. In contrast, an entire fairness review strongly favours plaintiff shareholders because it switches the burden of proof by forcing the defendant directors to affirmatively prove that all aspects of the process and price were fair.

### Type of transaction

- 17 | Does the standard vary depending on the type of transaction at issue?

Yes, in certain cases. For example, enhanced scrutiny applies and 'Revlon duties' are implicated when a company initiates an active bidding process involving a clear break-up of the company; when, in response to an offer, a target abandons its long-term strategy and seeks an alternative transaction; or when approval of a transaction results in a 'change of control'.

Interested transactions (eg, a going private transaction with a controlling shareholder) are subject to the entire fairness test. Other

M&A transactions (eg, a merger of equals between two public corporations with no controlling shareholder) generally are subject to the business judgement rule.

### Type of consideration

**18** | Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

Yes, in certain cases. In a cash-out merger where shareholders will have their investment in the ongoing enterprise terminated, *Revlon* duties will apply and courts will consider whether directors have taken reasonable steps to provide shareholders with the best transaction reasonably available. A stock-for-stock merger in which control of the combined entity will remain in a fluid market, by contrast, generally will not trigger enhanced scrutiny. Transactions involving a mixture of cash and stock are assessed on a case-by-case basis, although enhanced scrutiny will generally apply when 50 per cent or more of the consideration that shareholders receive is in cash.

### Potential conflicts of interest

**19** | Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

A transaction in which a majority of directors are interested will be subject to the entire fairness test. Under the entire fairness test, the burden of proof is on the board of directors to show that the transaction was the product of a fair process that resulted in an objectively fair price. The entire fairness test is fact-intensive by nature and often requires resolution by trial (and not pretrial motion practice).

### Controlling shareholders

**20** | Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared rateably with all shareholders?

Yes. A transaction in which a controlling shareholder is a party or has an interest different from other shareholders ordinarily will be scrutinised under the entire fairness test. However, the business judgement rule can apply to a transaction with a controlling shareholder if the transaction is conditioned upon approval by a fully empowered special committee of disinterested and independent directors; and the transaction is conditioned upon approval by an informed and non-coerced vote by a majority of the minority shareholders.

Where only one of these two conditions is met, the entire fairness test will continue to apply, but the burden will shift to the plaintiff to prove the unfairness of the transaction.

## INDEMNITIES

### Legal restrictions on indemnities

**21** | Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Indemnification may be required, permitted or prohibited depending on the facts and circumstances of a particular case. To the extent a director or officer has been successful on the merits in connection with an M&A litigation, indemnification for attorneys' fees and expenses is typically mandatory. At the other extreme, directors and officers may not be indemnified for a claim, issue or matter in which they are found to be liable to the corporation (eg, a shareholder derivative action)

absent court approval. In all other cases, directors and officers may be indemnified if it is determined that they acted in good faith in a manner reasonably believed to be in, or not opposed to, the best interests of the corporation and, in a criminal action or proceeding, where there is no reasonable cause to believe the person's conduct was unlawful.

Corporations may advance legal fees to a director or officer if the person receiving advancement furnishes an undertaking agreeing to repay the corporation if it is ultimately determined that the standard for indemnification has not been met.

## M&A CLAUSES AND TERMS

### Challenges to particular terms

**22** | Can shareholders challenge particular clauses or terms in M&A transaction documents?

Yes, shareholders challenging an M&A transaction often will focus on deal-protection devices (eg, termination fees, matching rights, 'no-shop' clauses). These devices will be evaluated under the enhanced scrutiny standards described above. Courts generally allow parties to include such devices in their M&A transaction agreements provided that they do not, separately or in the aggregate, preclude other bidders from making offers to acquire the seller or coerce shareholders into approving a transaction favoured by management.

## PRE-LITIGATION TOOLS AND PROCEDURE IN M&A LITIGATION

### Shareholder vote

**23** | What impact does a shareholder vote have on M&A litigation in your jurisdiction?

In a transaction that does not involve a controlling shareholder, a fully informed and uncoerced shareholder vote approving the transaction will result in the irrebuttable application of the business judgement rule. Courts conclude that such a vote will 'cleanse' any breach of fiduciary duty that took place in connection with the deal approval process.

In transactions involving a controlling shareholder, and absent satisfaction of the other prerequisites described above, shareholder approval will shift the burden to a plaintiff to prove the unfairness of a transaction.

### Insurance

**24** | What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Companies typically have insurance for their directors and officers that will cover the types of claims generally asserted in shareholder litigation arising from M&A transactions. The most important role of directors' and officers' insurance is minimising the risk that a director or officer will be subject to personal liability in connection with shareholder litigation. Directors' and officers' insurance also can influence the parties' willingness or ability to settle shareholder claims. Insurers generally play a small role in the preliminary phases of litigation, but may become more involved if a matter progresses or enters into formal settlement negotiations, such as mediation.

In recent years, many insurance carriers have substantially increased the deductible or retention applicable to M&A litigation such that a significant part of defence costs and early-stage settlement payments are made by the insured.

## Burden of proof

- 25 | Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The business judgement rule protects the decisions of officers and directors of a corporation if those decisions are made in good faith, informed and believed to be in the best interests of the corporation. Where the business judgement rule applies, the plaintiff has the burden to rebut the presumption. The plaintiff may do so by showing, for example, that the board of directors failed to consider relevant material information or rushed to a decision without a legitimate business justification. If a plaintiff is able to overcome the business judgement rule presumption, then the burden shifts to the defendants, who must demonstrate 'entire fairness', which requires that the transaction be entirely fair to the corporation and its shareholders.

## Pre-litigation tools

- 26 | Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Shareholders have a qualified, statutory right to inspect a corporation's books and records. To do so, a shareholder must make a demand that includes a proper purpose for the inspection. A proper purpose is one reasonably related to an individual's interest as a shareholder, such as investigating alleged mismanagement or corporate waste. If the shareholder can state a proper purpose, then he or she may seek books-and-records that are necessary to accomplish that proper purpose. The scope of documents available to a shareholder pursuant to a books and records demand is narrower than is available during discovery between litigation parties, although recent court decisions have taken a broader view and permitted email files, among other things.

Shareholders increasingly are making books-and-records demands in response to M&A transactions (rather than proceeding directly to litigation) for two reasons. First, Delaware courts have encouraged shareholders to obtain books and records to plead more detailed complaints. Second, to successfully proceed with a post-closing damages case, shareholders need to show that a vote or tender was not made on an informed basis or was the product of material conflicts.

## Forum

- 27 | Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

A shareholder must bring M&A litigation in a forum that has subject matter jurisdiction over the claims as well as personal jurisdiction over the parties. A federal court generally may exercise subject matter jurisdiction over state law claims if a shareholder also asserts valid federal claims or if the parties' citizenship is diverse. A state court generally does not have subject matter jurisdiction over federal claims. Personal jurisdiction over a corporation exists, at a minimum, in its state of incorporation and principal place of business, and may exist elsewhere depending on the corporation's business contacts with the jurisdiction. Whether a court has personal jurisdiction over a director or officer is a more detailed inquiry, and turns on the contacts between that director or officer and the forum. A corporation also may control where suits can be brought by adopting a forum selection clause in its by-laws or articles of incorporation.

## Expedited proceedings and discovery

- 28 | Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Shareholders may seek expedited proceedings for the purpose of setting expedited discovery deadlines and the date for an injunction hearing. The court generally has broad power to permit expedited proceedings, and the plaintiff's burden is relatively minimal, that is, the plaintiff need only demonstrate a colourable claim and a sufficient possibility of irreparable harm to obtain expedition. When expedited discovery is allowed, the seller typically is required to produce presentations from its financial adviser, board minutes relating to the transactions, and management projections or forecasts, among other things.

The most common discovery issues concern attorney-client privilege. Some jurisdictions recognise a fiduciary exception to the attorney-client privilege, which, under certain circumstances, allows shareholders to invade the corporation's attorney-client privilege to prove fiduciary breaches by officers and directors upon a showing of good cause. In addition, if the corporation is based outside of the US, issues may arise regarding applicable blocking or privacy statutes.

## DAMAGES AND SETTLEMENTS

### Damages

- 29 | How are damages calculated in M&A litigation in your jurisdiction?

In class actions, damages typically are designed to restore the shareholder to the position he or she would have been in if the alleged misconduct had not occurred. In M&A litigation, shareholders generally seek the difference between the deal price and what the deal price would have been absent the alleged misconduct. To litigate damages, plaintiffs and defendants usually retain experts, who typically employ one or more generally accepted valuation methodologies (eg, discounted cash-flow analysis, an analysis of comparable transactions) to support an opinion that the deal price should have been higher or lower (on the plaintiffs' side) or that the deal price was fair and reasonable (on the defendants' side).

### Settlements

- 30 | What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

Settlements of shareholder class actions and derivative cases generally require court approval. Typically, the plaintiff shareholder, through counsel, will file a motion seeking the court's preliminary approval of the proposed settlement. The motion will request that the court approve, among other things, a process for providing notice to the shareholders; the content of a notice to be mailed or published in a newspaper or trade journal, or both; and the deadline for shareholders to object in writing, at a final approval hearing, or both.

Often, the lawyers for the shareholder plaintiff also will seek the court's approval of an attorneys' fees award to be paid from the common settlement fund. At a final settlement hearing, the court will assess whether the settlement is fair and reasonable, subject to any objections it receives.

Over the past decade, M&A litigation has become increasingly common. At one point, complaints were filed in connection with approximately 95 per cent of public company deals valued at more than US\$1 billion. These filings often were followed by what became known as 'disclosure-only' settlements in which the seller's shareholders received supplemental disclosures prior to a vote or tender, the defendants

received a broad class-wide release covering all claims relating to the transaction and plaintiffs' counsel received a substantial fee award.

US courts have become increasingly sceptical of disclosure-only settlements, concluding that shareholders receive no real benefit in the majority of cases. As a result, courts now prefer in most instances that parties pursue mootness resolutions without court involvement in which the defendants agree to address the shareholders' disclosure claims, the release given to defendants is narrowed and the attorneys' fees paid to shareholders' counsel are lower.

### THIRD PARTIES

#### Third parties preventing transactions

- 31 | Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Third parties – increasingly, activist hedge funds – can employ a variety of strategies to stop or break up proposed M&A transactions, some of which involve filing litigation (in their capacity as shareholders) and some of which do not (such as publicly criticising the transaction or soliciting shareholder proxies opposing the transaction). Activist investors may seek to enjoin a proposed transaction by, among other things, attacking the motives and financial interests of the target company's board of directors and management team, challenging deal-related disclosures or asserting that deal protection measures agreed to with the buyer interfere with or preclude a superior bid. In certain circumstances, activist investors may pursue one or more of these strategies in collaboration with other financial or strategic buyers.

In addition, potential purchasers have in the past pursued M&A litigations to break up agreed transactions and acquire the target away from the preferred buyer. Purchasers in such situations typically need to be shareholders in the target company to have standing. Such cases have become less common in recent years as courts have clarified the law concerning permissible anti-takeover and deal-protection measures.

#### Third parties supporting transactions

- 32 | Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Activist investors also may pursue litigation or other tactics to force or pressure corporations to enter into unsolicited transactions. Generally, defensive measures taken by a board of directors to resist unsolicited offers are subject to enhanced judicial scrutiny, and thus are subject to challenge by shareholders who wish to see the transaction proceed. In addition, activist investors may pursue non-litigation alternatives to exert pressure, such as instituting a proxy contest to obtain board control or making an unsolicited offer in the hopes that additional, superior offers will emerge.

### UNSOLICITED OR UNWANTED PROPOSALS

#### Directors' duties

- 33 | What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

As a general matter, the fiduciary obligations of a target company's management and directors in response to an unsolicited or unwanted proposal are to act in good faith, with due care and loyalty, in what they believe to be the best interests of the corporation. A board of directors has no fiduciary duty to negotiate or sell in response to an unsolicited offer – the board may 'just say no'. In appropriate circumstances, the

board of directors may implement defensive measures to resist an offer that the board believes represents a threat. However, to be upheld by a court, such defensive measures must be in response to a legitimate threat to corporate interests, and must be reasonable and proportional in relation to the threat. Once a company elects to consider an alternative involving a break-up of the company or initiates an active bidding process, the board is required to take steps reasonably calculated to obtain the best price available.

### COUNTERPARTIES' CLAIMS

#### Common types of claim

- 34 | Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

In the context of private M&A transactions, the most common claims arise out of the terms of the purchase agreement, including claims for breaches of contractual representations, covenants and warranties. These claims often are subject to indemnity provisions, and may be made against merger consideration held in escrow. In addition, purchase agreements frequently contain a mechanism for a post-closing purchase price adjustment whereby the purchase price may be adjusted to account for variations in the target's value or a depletion of its working capital. These claims typically are resolved by arbitration. In addition, buyers may assert claims premised on fraud, including claims for fraud in the inducement.

#### Differences from litigation brought by shareholders

- 35 | How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Shareholder litigation arising out of M&A transactions generally is commenced in a representative capacity, that is, by an individual shareholder as a class action (on behalf of a larger class of shareholders) or as a derivative action (on behalf of the company), and seeks to enforce fiduciary duties owed by a company's board of directors to the company. In contrast, litigation between parties to an M&A transaction is brought directly between the parties. Private M&A litigation typically relates to the terms of the negotiated agreements and the veracity of the representations made by the parties prior to closing. Contractual counterparties do not owe each other fiduciary duties.

### UPDATE AND TRENDS

#### Key developments

- 36 | What are the most current trends and developments in M&A litigation in your jurisdiction?

M&A litigation in the US continued to evolve in significant ways in 2018. As widely reported, stockholders file lawsuits challenging the vast majority of US public company M&A transactions. Prior to 2016, many of these cases were resolved through 'disclosure-only' settlements – ie, settlements whereby the defendants agree to provide supplemental disclosures to stockholders in advance of the approval vote; the stockholder plaintiffs agree to dismiss the complaint and provide the defendants with a release; and plaintiffs' counsel, through agreement or via an application to the court, receives an attorneys' fee award for having caused the defendants to provide the supplemental disclosures to the stockholders.

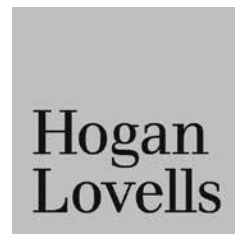
In 2016, the Delaware Court of Chancery issued its landmark decision in *In re Trulia, Inc Shareholder Litigation*. The Court of Chancery concluded that many disclosure-only settlements provided limited

value to stockholders while benefitting plaintiffs' counsel (in the form of fee awards) and deal parties (in the form of broad releases). For that reason, the Chancery Court held that, going forward, it would approve disclosure-only settlements only where the supplemental disclosures provided to stockholders were 'plainly material'. As a result of the *Trulia* decision, many disclosure-related cases instead are resolved through mootness fees – ie, after supplemental disclosures are made by the company that moot the plaintiff's disclosure-related claims, the plaintiff agrees to voluntarily dismiss the case in exchange for an agreed attorneys' fee amount paid to plaintiff's counsel. Depending on the jurisdiction, mootness fees may not require court approval. In addition, to avoid the impact of *Trulia*, many stockholder plaintiffs began filing M&A lawsuits in federal court asserting disclosure-related claims under the Securities Act of 1934 (the Exchange Act), rather than in state court.

In 2018, the United States Court of Appeals for the Ninth Circuit issued its decision in *Varbajedian v Emulex Corp* in which it held that claims under section 14(e) of the Exchange Act, which prohibits the making of false or misleading statements in tender offer communications, require only that the defendants negligently misled investors and not, as other courts had long held, that defendants acted with scienter, or the intent to deceive investors. The United States Supreme Court agreed to hear an appeal of the Ninth Circuit's decision, but recently dismissed the appeal as improvidently granted. As a result, the United States Supreme Court did not resolve the conflict between United States federal courts on this issue. Thus, until the United States Supreme Court takes this issue up again, there will continue to be a lack of uniformity among United States federal courts regarding the standard for claims under Section 14(e) of the Exchange Act.

A second notable development concerns the material adverse effect (MAE) clauses common in M&A agreements (also known as material adverse change (MAC) clauses). Although MAE clauses vary significantly from agreement to agreement, these provisions typically give the buyer the option not to close an M&A transaction if, during the period between signing and closing, the seller experiences events or changes that adversely and materially impact its financial condition. Prior to 2018, merger parties often raised the possibility of invoking MAE clauses, and there were a handful of litigated cases, but no Delaware court ever had held that a buyer justifiably declined to close or terminated a transaction on the basis of an MAE clause. That changed with the Court of Chancery's 246-page decision in *Akorn, Inc v Fresenius Kabi AG*, which was later affirmed by the Delaware Supreme Court. Among other things, the *Akorn* court found that, during the post-signing period, the seller lost hundreds of millions of dollars in value due to pervasive regulatory issues while experiencing year-over-year earnings declines of more than 55 per cent. Although the facts leading to the *Akorn* court's MAE conclusion are extreme, the case provides important guidance for MAE standards generally, as well as with respect to the manner in which buyers should proceed with closing efforts while evaluating whether or not to invoke an MAE clause.

A third significant development relates to the power of a corporation to choose where it will be sued by its stockholders. In recent years, many US corporations adopted 'forum selection' by-laws providing that breach of duty claims filed by company stockholders against board members must be brought in a stated jurisdiction (often Delaware). Delaware courts have approved these forum selection by-laws to the extent they address fiduciary duty and other claims involving the 'internal affairs' of the company. Several companies attempted to expand these by-laws to cover claims filed by stockholders against the corporation under the federal securities laws. In *Sciabacuccho v Salzberg*, the Delaware Court of Chancery invalidated these expanded by-laws on the ground that rights under the federal securities laws were not part of the internal affairs of a corporation, nor were they within the 'corporate contract' between investors and other corporate constituents.




---

**William M Regan**

william.regan@hoganlovells.com

**Jon M Talotta**

jon.talotta@hoganlovells.com

**Ryan M Philp**

ryan.philp@hoganlovells.com

---

390 Madison Avenue  
New York, NY 10017  
United States  
Tel: +1 212 918 3000  
Fax: +1 212 918 3100  
www.hoganlovells.com

Another trend concerns appraisal actions. Following the Delaware Supreme Court's 2017 decisions in *Dell, Inc v Magnetar Global Event Driven Master Fund Ltd*, and *DFC Global Corp v Muirfield Value Partners LP*. Delaware courts determined in several 2018 cases that 'fair value' for the stockholder in an appraisal action was significantly less than the amount the stockholder would have received in the transaction. In the recent cases, the Delaware Court of Chancery emphasised that in an appraisal action, stockholders are not entitled to any value arising from synergies created by the transaction at issue, and that the best indicator of fair value in public company cases often may be the unaffiliated (pre-deal announcement) stock market price. The recent case law substantially increases the risks for investors pursuing an appraisal arbitration strategy.

Finally, courts in 2018 continued to develop and apply the Delaware Supreme Court's ruling in *Corwin v KKR Financial Holdings*. Several decisions confirmed that *Corwin* ratification can be a powerful defence to breach of fiduciary duty claims that helps resolve stockholder litigation at the pleading stage. Other recent cases, however, illustrate that *Corwin* is not without limits and that a stockholder complaint will survive a motion to dismiss where the plaintiff can plead facts indicating that stockholder approval was not obtained on the basis of a fully informed vote.





Hogan  
Lovells

We work as part of your team, helping solve your toughest and most complex legal issues.

**Wherever you are.**

Hogan Lovells is an international legal practice that includes Hogan Lovells International LLP, Hogan Lovells US LLP and their affiliated businesses. Images of people may feature current or former lawyers and employees at Hogan Lovells or models not connected with the firm.

[www.hoganlovells.com](http://www.hoganlovells.com)

© Hogan Lovells 2019. All rights reserved.

## Other titles available in this series

Acquisition Finance	Distribution & Agency	Islamic Finance & Markets	Real Estate M&A
Advertising & Marketing	Domains & Domain Names	Joint Ventures	Renewable Energy
Agribusiness	Dominance	Labour & Employment	Restructuring & Insolvency
Air Transport	e-Commerce	Legal Privilege & Professional Secrecy	Right of Publicity
Anti-Corruption Regulation	Electricity Regulation	Licensing	Risk & Compliance Management
Anti-Money Laundering	Energy Disputes	Life Sciences	Securities Finance
Appeals	Enforcement of Foreign Judgments	Litigation Funding	Securities Litigation
Arbitration	Environment & Climate Regulation	Loans & Secured Financing	Shareholder Activism & Engagement
Art Law	Equity Derivatives	M&A Litigation	Ship Finance
Asset Recovery	Executive Compensation & Employee Benefits	Mediation	Shipbuilding
Automotive	Financial Services Compliance	Merger Control	Shipping
Aviation Finance & Leasing	Financial Services Litigation	Mining	Sovereign Immunity
Aviation Liability	Fintech	Oil Regulation	Sports Law
Banking Regulation	Foreign Investment Review	Patents	State Aid
Cartel Regulation	Franchise	Pensions & Retirement Plans	Structured Finance & Securitisation
Class Actions	Fund Management	Pharmaceutical Antitrust	Tax Controversy
Cloud Computing	Gaming	Ports & Terminals	Tax on Inbound Investment
Commercial Contracts	Gas Regulation	Private Antitrust Litigation	Technology M&A
Competition Compliance	Government Investigations	Private Banking & Wealth Management	Telecoms & Media
Complex Commercial Litigation	Government Relations	Private Client	Trade & Customs
Construction	Healthcare Enforcement & Litigation	Private Equity	Trademarks
Copyright	High-Yield Debt	Private M&A	Transfer Pricing
Corporate Governance	Initial Public Offerings	Product Liability	Vertical Agreements
Corporate Immigration	Insurance & Reinsurance	Product Recall	
Corporate Reorganisations	Insurance Litigation	Project Finance	
Cybersecurity	Intellectual Property & Antitrust	Public M&A	
Data Protection & Privacy	Investment Treaty Arbitration	Public Procurement	
Debt Capital Markets		Public-Private Partnerships	
Defence & Security		Rail Transport	
Procurement		Real Estate	
Dispute Resolution			

Also available digitally

[lexology.com/gtdt](https://www.lexology.com/gtdt)