

The German Foreign Trade Law and Its Effects on International M&A Transactions

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The German government recently passed new versions of the German Federal Act on Foreign Trade (*Außenwirtschaftsgesetz*) and the German Foreign Trade Ordinance that became effective on 1 September 2013 (the "**German Foreign Trade Law**"). Their aim was to simplify the existing law and to conform it to the European regulations.

Also under the new German Foreign Trade Law, an M&A transaction may become subject to review and prohibition by the German Federal Ministry of Economics and Technology (*Bundesministerium für Wirtschaft und Technologie*) (the "**Ministry**"), if a person or entity not located in the European Union¹ ("**Foreign Buyer**") directly or indirectly acquires a company located in Germany or a direct or indirect participation in such company.

Until expiry of the review periods, the direct or indirect acquisition of a company located in Germany (or a 25% interest therein) is subject to the Ministry prohibiting or allowing the transaction. If the Ministry prohibits the transaction, the parties must reverse such transaction. In order to enforce a prohibition, the Ministry is entitled to prohibit the exercise of voting rights from shares of the Foreign Buyer or its subsidiary in the acquired company or to appoint a trustee who shall reverse the transaction.

Even though only specific transactions which the Ministry considers an endangerment of the public order or security are affected by the German Foreign Trade Law, it should be kept in mind for each and every transaction involving a German entity.

I. Requirements for Potential Prohibition

Regardless of both the acquisition structure and sector in which the acquired company operates, review and prohibition might become relevant for a transaction if the following requirements are met:

A. Acquisition of a Company or Participation in a Company Located in Germany

A Foreign Buyer acquires a company or direct participation of at least 25% of the voting rights in a company located in Germany, i.e., the company's registered seat or place of management is located within the economic territory of Germany. Additionally, the acquisition of an indirect participation of at least 25% of the voting rights in a company located in Germany needs closer review with respect to the potential applicability of the Foreign Trade Legislation. Therefore, if the acquired company has a direct or indirect subsidiary in Germany, the acquisition of a non-German company can also be subject to the German Foreign Trade Law.

If a Foreign Buyer acquires 25% of a third party that has voting rights in the relevant company, these voting rights will be attributed to the Foreign Buyer. The same applies if the Foreign Buyer enters into a voting rights pooling contract with another shareholder.

German Foreign Trade Law is also applicable if a Foreign Buyer who already holds a direct or indirect participation of at least 25% in a company located in Germany directly or indirectly acquires an additional participation in this company.

B. Endangerment of the Public Order or Security

In order for review and prohibition to become relevant, the transaction must endanger the public order or security of the Federal Republic of Germany. The term “endangerment of the public order or security” is largely influenced by European Law and should be understood as actual and material endangerment of fundamental interests of the German community. This means that the transaction must either affect material legal interests such as the existence, function and supply of the German population, or substantive issues regarding national and international security, in particular the operation of the German economy, German institutions, important public services and the survival of the German population.

Important economic areas are the telecommunication sector, electricity sector, energy and water supply sector and other services of strategic importance. However, in addition to these sectors, which are obviously of great importance for the functionality of the German community, one must always keep in mind that public security in particular can also be endangered if products produced or developed by a company located in Germany can also be used for purposes other than their original use, especially if this constitutes military purposes.

II. Review Process

The potential review process in which the Ministry has to decide upon a potential prohibition is divided into two parts: (i) a period of a maximum of three months starting with the signing of the agreement to initiate the review process and (ii) a period of a maximum of two months starting upon receipt of all information requested by the Ministry from the Foreign Buyer.

With respect to the initiation of the review process, the parties are not obliged to inform the Ministry about the transaction. However, if the Ministry finds out about the transaction (e.g., through publications from the cartel authorities or public media) and decides to initiate a review of the transaction, it must inform the buyer of its decision and the buyer must provide the Ministry with the transaction documentation.

If the Ministry is of the opinion that the transaction endangers public order or security of the Federal Republic of Germany, it is entitled - with consent of the German government and within the two-month period - to prohibit the transaction or to give orders in connection with the transaction.

III. Obtaining Legal Certainty Via a Foreign Investment Clearance Certificate

If the parties would like to obtain sufficient assurance as to whether the transaction presents a threat to public order or security, the purchaser may obtain a clearance certificate (“**Foreign Investment Clearance Certificate**”). If the Ministry issues such certificate or does not initiate a review process within one month after receipt of the written application for a Foreign Investment Clearance Certificate, it is not entitled to review the transaction again with respect to a potential conflict with the regulations of the German Foreign Trade Law.

IV. Closing Conditions

The parties of a transaction might not want to risk the German Ministry prohibiting the transaction once the transaction has been completed.

One way to avoid such risk is to request a Foreign Investment Clearance Certificate prior to signing the binding transaction documents. However, in this case, the envisaged transaction will become public. Another way to avoid such risk is to cover the implications of the German Foreign Trade Law within a closing condition of the purchase agreement, according to which the transaction will only be completed upon confirmation that the transaction will not be prohibited by the Ministry (e.g., a Foreign Investment Clearance Certificate has been obtained).

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¹ Exceptionally, buyers located in the member states of the European Free Trade Association (EFTA) and buyers located in Iceland, Liechtenstein, Norway or Switzerland shall not be considered as Foreign Buyers pursuant to the Foreign Trade Legislation.