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# THE MERGERS & ACQUISITIONS REVIEW

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## Chapter 33

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# LUXEMBOURG

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### I OVERVIEW OF 2007/2008 M&A ACTIVITY

2007 was a milestone in Luxembourg M&A activity as it saw the finalisation of the *Mittal/ Arcelor* merger, one of the most spectacular merger transactions ever to take place in Luxembourg with a worldwide dimension.

In addition to the *Mittal/ Arcelor* merger, M&A transactions were quite frequent in the first half of 2007, mainly through leveraged private equity transactions using top-structure Luxembourg SPVs or SICARs. The real estate market also grew, in terms of numbers of transactions and of geographical spread (there were notable developments in the Central and Eastern European countries). The second half of 2007 and early 2008 were, however, increasingly affected by the devastating effects of the subprime crisis and ‘credit crunch’, which had severe effects on leveraged acquisitions. Although 2008 will probably be one of the quieter years of the decade in M&A transactions, Luxembourg, thanks to its continuing efforts to encourage investments (e.g., its attractive IP income regime and its reduction of capital duty in 2008, from 1 to 0.5 per cent, with abolition scheduled for 2009) keeps on increasing its attractiveness in M&A structuring.

### II GENERAL INTRODUCTION ON THE LUXEMBOURG LEGISLATIVE M&A FRAMEWORK

No overall coordinated legal framework applies to Luxembourg M&A transactions. The applicable legal provisions mainly depend on the characteristics of the transactions at stake (private or listed target, share or asset deal). As an EU Member State, Luxembourg is bound by the applicable European regulations and has transposed the whole range of

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directives which constitute, together with its national body of laws, a complete, up-to-date and business-oriented legal system.

As with other jurisdictions rooted in the Roman law tradition, reference should be made to the Civil Code, which provides the principles applicable to contracts in general (validity of contracts, contractual liability, property rights), specific contracts (sale agreements, encumbrances, rights in rem, etc), as well as the fundamental corporate law principles.

With respect to secured deals, the Law of 5 August 2005 on financial collateral governs standard securities, such as pledges, with the notable effect of immunising the pledgees against the potential detrimental effects of bankruptcy situations affecting pledgors.

The Law of 10 August 1915 on Commercial Companies, as amended (‘the Companies Law’) is the principle corporate legislation. It contains, *inter alia*, the rules governing mergers and demergers.

Implemented in urgency in the turmoil of the *Mittal/Arcelor* takeover bid (until then Luxembourg had no takeover legislation), the Law of 19 May 2006 concerning Takeover Bids (‘the Takeover Law’) is a close transposition of Directive 2004/25/EC. The Takeover Law sets forth the main rules and the procedure applicable to takeover bids in Luxembourg. It provides, *inter alia*, the rules relating to general principles to be complied with, determination of the competent control authorities, the applicable law, the protection of the minority shareholders, the mandatory bid and the pricing of the offer. It also sets forth the regime for squeeze-outs and buyouts.

The Law of 11 January 2008 on Transparency Requirements for Issuers of Securities (‘the Transparency Law’), which is a close transposition of Directive 2004/109/EC of 15 December 2004, contains the provisions applicable to the acquisition or disposal of Luxembourg-listed companies. The Transparency Law contains the rules governing the notification requirements when specific thresholds of voting rights are reached as a consequence of a disposal or an acquisition of listed shares. It also provides for the disclosure of information about issuers.

The Law of 9 May 2006 on Market Abuse aims to prevent insider trading and market abuse.

The Law of 10 July 2005 on the Prospectus concerning Securities (‘the Prospectus Law’) contains the prospectus requirements, which could *inter alia* apply where new shares are issued in consideration of a takeover.

The Commission de Surveillance du Secteur Financier (‘CSSF’) is the authority in charge of supervising the financial sector and is also vested with the power to ensure the compliance of the Takeover, Transparency and Prospectus Laws. The CSSF periodically issues circulars that complement and clarify the regulatory framework. The CSSF’s circulars are not legally binding but provide helpful interpretations and guidelines to investors and professionals.

### III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

Two laws of 23 March 2007 (‘the Merger Laws’) have substantially modified the provisions relating to mergers, demergers and cross-border transactions. The Merger Laws introduced five main changes:

- a* the merger and demerger regime has been extended to all types of companies vested with legal personality;
- b* the merger and demerger regime has been made applicable to the companies or economic interest groups that are acquired or will cease to exist as a consequence of a merger or a subdivision, and which are the subject of bankruptcy proceedings, proceedings relating to composition with creditors or similar procedure such as the suspension of payments, controlled management or proceedings instituting special management or supervision of one or more companies. Prior to the enactment of the Merger Laws, a company subject to bankruptcy or other insolvency proceedings could not merge with another company;
- c* the specific object and purpose of one of the Merger Laws was to permit cross-border mergers and subdivisions: the new regime provides for the effectiveness of the universal transfer of all the assets and liabilities of the companies involved in the merger or subdivision process and in respect of third parties. However, given that these principles were implemented in urgency under the pressure of the *Mittal/Arcelor* merger, the law only set out the basic principles of cross-border mergers and divisions. The pending Draft Bill No. 5829 shall implement in detail the EC Directive 2005/56 on cross-border mergers;
- d* the Merger Laws have implemented the legal regime for transfer of assets, branches of activity and all assets and liabilities. Formerly, with the exception of a demerger, a company could not transfer a portion of its business with the effect of immediately transferring assets and liabilities. The new regime avoids the drawbacks of the demerger (winding-up of the company concerned) or contribution in kind (which does not allow to contribute liabilities) and provides automatic transfer of the assets and liabilities without compelling the transfer of each item individually pursuant to burdensome assignment or acceptance formalities; and
- e* the Merger Laws have introduced a regime of transfer of professional assets and enable the transferor to submit such transfer to the provisions applicable to the demerger (the automatic winding-up of the transferor being excepted) and therefore to benefit of the automatic transfer of the related assets and liabilities.

### IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

Luxembourg has always been focused on attracting foreign investors by implementing an efficient, flexible and business-friendly legal environment. With the exception of the European standards relating to anti-money laundering, which are strictly complied with in Luxembourg – and which constitute a guarantee for the seriousness of the financial centre – foreign involvement in M&A transactions is not subject to any other specific restrictions.

Indeed, Luxembourg has a broad range of regulation adapted to foreign requirements. For instance, it is possible to express the share capital of Luxembourg companies in foreign currencies or to have the corporate and contractual documentation directly drawn up in English.

With respect to ongoing and future local M&A transactions, March 2008 saw the start of a significant cross-border transaction in the mobile telephony sector. Belgacom, the leading Belgian telecoms operator, announced the acquisition of Tele2Tango Luxembourg, the second mobile operator in Luxembourg, holding 39 per cent share of the local mobile market. The transaction value is estimated at an amount of €207 million.

## V FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

For a number of reasons (low minimum share capital, closed character which reduces the anti-dilution risks, flexibility due to the non-application of EC company directives' restrictions, among others), the *société à responsabilité limitée* (private limited liability company) is the common corporate vehicle used for Luxembourg-structured acquisitions. For more complex structures, the *société en commandite par actions* is also a useful corporate form, which combines limited and unlimited liability depending on the nature of the shareholders.

A mix of debt and equity is used at the Luxembourg level so as to finance, directly or indirectly, the acquisitions. Most notably, the debt/capitalisation ratio is interpreted quite flexibly in Luxembourg, which allows the maximising of the debt deductibility. In this respect, advanced rulings by the Luxembourg tax authorities give an appreciable comfort to investors.

The financing of acquisitions by hybrid instruments, although commonly applied in practice by means of *sociétés à responsabilité limitée* raised legal issues as the provisions governing such companies did not quite fit with such practice. One of the features of Draft Bill No. 5730 on the modernisation of company law is to allow all types of commercial companies vested with legal personality to proceed to the issuance of public or private bonds, in bearer or in registered form.

## VI SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND HOT INDUSTRIES

The most significant transaction in Luxembourg in 2007 was obviously the completion of the *Mittal/Arcelor* merger.

The merger started in January 2006, when the world's largest steel company, Mittal Steel, launched a takeover bid for Arcelor, the biggest Luxembourg-based company, which was listed on most European stock exchanges. This announcement came as a great surprise, given that Arcelor was then proudly regarded as a European industrial flagship which had been built up on the remnants of the Luxembourg, French and Spanish national steel industries. However, after brief hesitation, it soon appeared that the reluctant management of Arcelor had failed to organise a coordinated anti-Mittal takeover strategy. Most notably, the Luxembourg political and economic decision-makers

felt that such a strategy would be in clear contradiction with the traditional Luxembourg free-market approach.

In June 2006, Mittal Steel and Arcelor reached an agreement to enter into a merger. The terms of the transaction were approved by the boards of Arcelor and Mittal Steel, which recommended the merger to their respective shareholders. It was intended that the combined group, like Arcelor, would have its registered office and headquarters in Luxembourg. It would bear the name of ArcelorMittal.

The merger process completed in a two-stage offer. In the first step, Mittal Steel offered 11 Mittal shares for 7 Arcelor shares which ended with Mittal Steel holding 93.7 per cent of Arcelor by August 2006, and in the second step, Mittal Steel offered 8 Mittal (ArcelorMittal) shares for 7 Arcelor shares. On 5 November 2007 the extraordinary general meeting of the shareholders of Arcelor approved the proposed merger conditions of the second-step merger of ArcelorMittal into Arcelor.

## **VII PENSION & EMPLOYMENT LAW – RECENT DEVELOPMENTS AND LEGISLATION RELEVANT TO M&A**

The aforementioned Draft Bill No. 5829 on cross-border mergers will amend the Luxembourg Labour Code with a new section devoted to the participation of the employees within the framework of the merger process. The current Luxembourg legal provisions concerning the representation of the employees in public limited companies will apply in the case of a cross-border merger.

In addition, the company which will have been created pursuant to the merger will be bound to take adequate measures to ensure the rights of participation of the employees during the three years following the completion of the cross-border merger.

## **VIII TAX LAW**

Luxembourg has always been at the forefront in terms of innovation, flexibility and pragmatic approach in the field of taxation matters. In line with this well-established tradition, 2007 proved to be remarkably fruitful in this respect with the implementation of (i) the *société de gestion du patrimoine familial*, (ii) the reduction and projected abolition of the capital duty, (iii) the IP taxation regime and (iv) tax measures in relation to mergers.

### *i*      *SPF*

The Law of 11 May 2007 introduced a new private equity vehicle, the *société de gestion du patrimoine familial* (company for family wealth management, ‘SPF’). The predecessor of which was the Holding 29 tax regime, which had been banned by the European Commission as prohibited state aid.

The SPF is designed to fall outside the scope of state aid scrutiny as it is not allowed to perform any economic activity. Therefore, the SPF is not an ‘undertaking’ in the meaning of Article 87 of the EC Treaty.

The exclusive object of the SPF is the acquisition, holding, management and disposal of financial assets (e.g., shares, bonds, warrants, futures). However, the SPF is not allowed to invest directly in real estate, to grant interest bearing loans, to provide

services, to receive royalties or to be involved in the management of other companies. As mentioned, the SPF is not allowed to perform any commercial activity. It may be set up under the form of any type of share capital company (*société anonyme, société à responsabilité limitée, société en commandite par actions*). Conversely, the SPF may not be established under the form of a partnership.

Only specific types of investors can hold a participation in the SPF:

- a* one or several individuals managing their personal assets;
- b* an entity acting exclusively in the interest of one or more individuals in private assets management (such as a trust); and
- c* intermediaries acting on behalf of the investors referred to above.

The *raison d'être* of the SPF is that it is treated as a transparent entity and is therefore exempt from corporate income tax, municipal business tax and net wealth tax. However, the SPF could lose its tax exemption status if it receives, for one fiscal year, more than 5 per cent of its total dividend income from interests located in non-resident companies that are not subject to corporate income tax of a minimum rate of 11 per cent.

As the SPF may not undertake any commercial activity, it is not subject to VAT.

The SPF is only subject to a capital duty of 0.5 per cent upon incorporation or upon any subsequent capital increases or contributions and to an annual subscription tax of 0.25 per cent (with a minimum of €100 and a maximum of €125,000 a year), calculated on the aggregate amount of (i) the paid-up capital; (ii) the share premium; and increased by (iii) the debts exceeding eight times the paid-up capital plus the share premium.

## *ii Capital duty*

Pursuant to the Law of 21 December 2007, which came into effect on 1 January 2008, the capital duty (due upon incorporation of commercial companies or upon subsequent contributions) has been reduced from 1 per cent to 0.5 per cent. On 22 May 2008, the Luxembourg government announced that capital duty will be abolished as from 1 January 2009. However, no further bill has been filed so far.

## *iii IP revenue exemption*

The Law of 21 December 2007 introduced an exemption of 80 per cent of income and gains derived from intellectual property rights.

This exemption applies to software, copyrights, patents, trademarks, designs and models. Copyrights of literary or artistic works, plans, secret formulae or processes are not covered by the exemption regime.

The application of the IP partial exemption regime is subject to the following conditions:

- a* the IP has been created or acquired after 31 December 2007;
- b* during the first fiscal year in which the IP partial exemption regime is requested, taxpayers must capitalise in their tax balance sheet all the previous expenses, amortisations and deductions connected with the IP and include in their taxable basis for that year the corresponding credit; and

- c* the IP must not have been acquired from related companies, which are defined as:
- parent companies that directly own at least 10 per cent of the share capital of the taxpayer;
  - subsidiaries in which the taxpayer holds directly at least 10 per cent of the share capital; and
  - sister companies as long as at least 10 per cent of their share capital is directly owned by the same parent company.

*iv* *Implementation of the Merger Directive*

Draft Bill No. 5708 implementing Council Directive 2005/19/EC amending Council Directive 90/434/EEC concerning the common tax regime applicable to restructuring operations in the European Union (‘the Merger Directive’) was submitted to the Luxembourg Parliament on 16 March 2007.

The provisions regarding the restructuring operations such as partial division and transfer of seat of a European Company and a European Cooperative Company have already been implemented in Luxembourg, so that those transactions can be conducted under tax neutrality in accordance with the principles set forth in the Merger Directive.

The regime applicable to a European Company and a Cooperative European Company is extended to companies that are taxpayers in their home state but are considered as tax transparent by the other Member States.

In the case of a merger by absorption, the minimum holding percentage to qualify for a tax exemption on capital gains accruing in the absorbing company upon cancellation of its participation in the transferring company has been reduced from 25 per cent to 10 per cent.

Draft Bill No. 5708 also aims to extend the Luxembourg provisions transposing both the merger and the parent-subsidiary directives so as to cover any share capital company or cooperative company resident in a Member State of the European Economic Area (EEA) that is subject to income tax at a rate comparable to the Luxembourg income tax rate.

## **IX COMPETITION LAW**

Two distinct authorities deal with competition law in Luxembourg: (i) the Competition Council, which is an independent administrative authority (‘the Council’) and (ii) the competition inspectorate, which is a body of the Luxembourg Ministry of the Economy and Trade (‘the Inspectorate’) (together, ‘the Authorities’). The Authorities are members of the European Competition Network (‘ECN’). The Inspectorate is in charge of investigating cases, whereas the power to order decisions, recommendations or penalties vests in the Council, acting as a public establishment independent from the political authorities.

Compliance with competition law principles within the framework of a merger is not specifically regulated in Luxembourg and Luxembourg law does not expressly grant power to the Authorities to investigate merger cases or to conduct a pre-merger control.

Even though the Authorities are empowered to ensure that there are no agreements, decisions, practices that would prevent or restrict fair competition and, accordingly, the Authorities would be entitled to investigate on mergers that could potentially breach the competition rules, in practice the Authorities have never used this power in the context of a merger. So far, the Authorities consider that merger operations do not fall within the scope of their powers. As a result, there are no pre-merger filing or notification requirements under Luxembourg law, except for mergers that would have a European dimension. In this case, the control is made at the level of the European Commission in particular on the grounds of the EC Regulation 139/2004 of 20 January 2004. In such a scenario (as for instance, the *Mittal/Arcelor* merger), the European Commission will request assistance from the Authorities in respect of the Luxembourg competition law issues.

## X FUTURE DEVELOPMENTS AND OUTLOOK

Several important draft bills are currently tabled on the Luxembourg legislative agenda:

- a* Draft Bill No. 5730 regarding the modernisation of the Law of 10 August 1915 concerning commercial companies;
- b* the aforementioned Draft Bill No. 5829 aiming to transpose into Luxembourg law the EC Cross-Border Mergers Directive is awaited by practitioners as it will give Luxembourg the wide range of legal instruments favouring restructuring operations on a pan-European level; and
- c* in November 2007, the Luxembourg government adopted a draft bill concerning the acquisition in the financial sector implementing the European directive 2007/44/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector. The purpose of this draft bill is to secure the acquisitions in the financial sector and to detail the procedure of approval of the acquisition by the CSSF, as well as the description of the prudential measures that the CSSF must adopt.