SHEARMAN & STERLING LLP

M&A AND CORPORATE LAW

NEWSLETTER 04 MARCH 2012

In this issue:

Dear Sir or Madam,

I am delighted to once again bring to your attention current issues in the areas of M&A and corporate law with this first edition of our Newsletter in 2012. Particularly noteworthy is the decision of the Federal Court of Justice concerning the good faith acquisition of shares of a limited liability company in case of intermediate dispositions (*Zwischenverfügungen*).

The German Supervisory Authority for Financial Services (Bundesanstalt für Finanzdienstleistungsaufsicht – *BaFin*) has published answers to frequently asked questions regarding Sec. 25a Securities Trading Act (*Wertpapierhandelsgesetz – WpHG*). According to BaFin's FAQs a real shift of paradigms has taken place with regard to information obligations on voting rights in the context of M&A transactions.

I would also like to draw your attention to the review of the permissibility of and limitations to remuneration granted to members of the management and supervisory boards by third parties - an issue highly topical in times of crisis.

I hope this Newsletter will again be of interest to you.

Yours, Martin Neuhaus

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Obligation to inform in the Context of Compliance Suspicions prior to M&A Transactions

Problem Statement

Compliance issues have recently become increasingly important in the M&A context. In connection with a deliberate breach of a precontractual duty to inform, compliance deficiencies in a transaction concerning the purchase of a company can give rise to legal remedies, including the right to unwind the transaction.

Obligation to provide Information regarding Suspicious Events prior to M&A Transactions

Although negotiating parties typically have conflicting interests, according to a well established judicature there is a duty to inform the other party of circumstances that are of such significance to the other party that they could frustrate the purpose of the intended contract. By providing information, the seller shall enable the purchaser to independently evaluate the risks. In principle, this also applies when there are parties – as is typically the case in the context of the purchase of a company – who are knowledgeable in the matter and the industry and who, in addition, are each advised by investment banks, corporate consultants and attorneys. Generally, the potential purchaser cannot furnish himself with the information which is meaningful to him and is dependent on the seller's willingness to provide clarification. As well as answering the purchaser's questions completely and correctly, the seller also has an obligation to disclose all facts that are objectively material to the purchaser, regardless of whether the purchaser asked for these. This obligation on the part of the seller to provide clarification also includes the obligation to disclose suspicions as a suspicion of a defect, when it is based on concrete and grave facts, constitutes a defect in itself in case it may not be clarified by measures which are reasonable for the purchaser. The Higher Regional Court of Hamm ruled that the compliance-relevant questions as to whether turnover and salaries have been booked correctly or whether payments have been effected through slush funds outside of the company's financial statements are subject to an obligation to disclose as such matters are material to the purchaser's decision. In the event of a culpable breach of an obligation to disclose by the seller, contributory negligence on the part of the purchaser may not be assumed, even if a due diligence has been conducted. A potential purchaser may be expected to ask for balance sheets, profit and loss statements, business management analyses or other comparably meaningful documentation, if these are material to the purchaser. Often, however, compliance issues are only within the knowledge of those persons that have responsibility for internal operational matters. In the event that a seller deliberately breaches its duty to inform, it may not exercise an agreed disclaimer of warranty or claim that such matters were not covered by the representations and warranties contained in the transaction agreement.

Consequences in Practice

It has become increasingly the case that M&A transactions depend on the question as to whether the seller has sufficiently informed the purchaser about potential compliance infringements and suspicions. In case of doubt only an explicit indication is sufficient. For the purchaser, on the other hand, it is important whether the information disclosed provides a basis for specific questions to be asked and whether prior to the transaction the purchaser makes it sufficiently clear to the seller which circumstances are material to his purchase decision.

Third-Party Payments to Members of the Corporate Bodies of a German Stock Corporation

Third-party payments are payments to members of a management board or supervisory board relating to their board activities that are not paid by the company itself but by a third party.

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Third-party payments are becoming more and more important due to the increasing demands and the associated risks in connection with the activities of the corporate bodies. A candidate will increasingly only be prepared to take on a particular position in exchange for a commensurately high payment. In many cases, third-party payments are necessary to be able to pay such high amounts. In particular in the case of groups of companies, the question regularly arises with respect to payments of a parent company to members of a subsidiary's corporate body.

The legal requirements for members of the supervisory board are largely unexplored. The same applies to the recommendations of the German Corporate Governance Code. Here, the issue is whether an "adequacy test" (*Angemessenheitsprüfung*) of the overall compensation including the third-party payment must take place (Sec. 113 para. 1 sentence 3 German Stock Corporation Act (*Aktiengesetz – AktG*)). The risk of a conflict of interests including any disclosure obligations should also be taken into account. The formal requirements are also insufficiently clear: Is the consent of the general meeting (*Hauptversammlung*) mandatory? Is disclosure of the third-party payments required in the notes to the annual financial statements?

Although they have been generally discussed, there is still some uncertainty with regard to the legal requirements for members of the management. While it is established that the overall remuneration for members of the management board including third-party payments has to be "adequate" (*angemessen*) and Sec. 285 No. 9a sentence 5-8, 314 para. 1 No. 6a sentence 5-8 German Commercial Code (*Handelsgesetzbuch – HGB*) explicitly call for individual disclosure of the remuneration, some questions still remain unresolved: To what extent must the supervisory board be involved in the decision concerning the third-party payments? In the context of the "adequacy test", to what extent must third-party payments also be considered? What targets may be set by the third party, if any?

An overview of the problems associated with third-party payments and related legal requirements can be found in the publications of:
Neuhaus/Gelliβen, Drittvergütungen für Aufsichtsratsmitglieder, NZG 2011, 1361 et seq.

Diekmann, Die Drittvergütung von Mitgliedern des Vorstands einer Aktiengesellschaft, in: Festschrift für Georg Maier-Reimer zum 70. Geburtstag, 2010, 75 et seq.

German Federal Court of Justice (FCJ) limits the Possibility for an Acquisition in Good Faith of Shares in a German Limited Liability Company (*GmbH*)

For the first time, in its decision of September 20, 2011 (BGH II ZB 17/10), the FCJ addressed Sec. 16 para. 3 German Act on Limited Liability Companies (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung – GmbHG*) as amended by the German Act to Modernize the Law on Private Limited Companies and Combat Abuses (*Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen – MoMiG*).

Background

A notary involved in an assignment of a share in a GmbH subject to a condition precedent wanted to submit a shareholders' list to the commercial register, which contained a note indicating that the assignment was subject to conditions precedent. In the notary's opinion such an addendum was necessary to prevent a potential good faith acquisition of the share by a third party.

Limited Reliability of the Shareholders' List

The FCJ has now confirmed the Registry Court's refusal to adopt such a list, since such a protection for the first acquirer was redundant.

The acquisition of rights subject to a condition precedent is, pursuant to Sec. 161 para. 1 German Civil Code (*Bürgerliches Gesetzbuch – BGB*), in principle protected against all further encumbering interim transfers. According to

the recent FCJ's decision, this also applies to an acquisition of shares in a GmbH. In particular, the newly created possibility for a good faith acquisition of GmbH shares as implemented in Sec. 16 para. 3 GmbHG does not allow a good faith acquisition of shares free from third party rights, since the shareholders' list only indicates the seller's actual ownership and not his unlimited rights of disposal as well.

Thus, the FCJ has relieved the practice of acquiring shares in a GmbH subject to conditions precedent (*e.g.*, full payment of purchase price or merger clearance) from complex measures for preventing an interim acquisition in good faith. The inclusion of a reference in the shareholders' list to this effect, which the FCJ has now rejected, had been proposed in this respect.

At the same time, the FCJ has limited the scope of an acquisition in good faith of GmbH shares and rejected the concept of a good faith acquisition of GmbH shares free from encumbrances.

Relevance in M&A Practice

Regarding the current practice of transfers of GmbH shares subject to conditions precedent such as the full payment of the purchase price or a merger clearance, the recent decision must be welcomed. As in the past, no additional protection measures need to be implemented.

Due to the limited scope of an acquisition in good faith when transferring GmbH shares, a comprehensive due diligence examination of the seller's unlimited right of disposal will, however, still be necessary.

German Federal Court of Justice (FCJ) specifies Diligence Requirements for Management and Supervisory Boards relying on External Legal Advice

In its judgement rendered on September 20, 2011 (II ZR 234/09), the FCJ addressed the question of in what circumstances members of the management and supervisory board may rely on external legal advice in cases of complicated capital measures.

Facts of the Case

The facts underlying the court's decision are as follows: A corporation planning to acquire several investments wanted to pay the purchase price partly by using its own shares. Pursuant to Sec. 71 AktG, the acquisition of a company's own shares for this purpose is prohibited. A legally trained member of the supervisory board therefore suggested to obtain the shares by a loan on securities from the company's majority shareholder. The company intended to return the loaned shares to the majority shareholder by issuing new shares by a capital increase. The majority shareholder settled the contribution claim resulting from the capital increase by way of contribution in kind by waiving its claim for return of the loaned shares. The corporation's liquidator sued the members of the management and supervisory boards of the corporation.

Decision of the Court

In this case, the court held that:

- Own shares are not a suitable subject for a contribution in kind; the same applies for the waiver of the claim for return of the loaned shares.
- The defendants were not entitled to presume that the transaction was lawful: in situations in which the members of the management and supervisory boards lack the relevant expertise, they have an obligation to consult an independent and qualified professional, whom they have to inform on the circumstances of the corporation and provide with all necessary documents. In addition, they have to diligently review the plausibility of the granted legal advice. The oral legal advice in this case was not sufficient in light of the complexity of the case as it did not allow for the necessary plausibility review.
- Special knowledge must be attributed to every professionally qualified member of the supervisory board since this knowledge frequently is the reason for its membership in the corporate body. Special knowledge acquired through professional experience therefore justifies more strict diligence requirements.

If you wish to review additional information regarding the decision as well as its practical relevance, you may refer to our client publication entitled "German Federal Supreme Court specifies diligence requirements for management and supervisory boards relying on external legal advice", available under: http://www.shearman.com/The_German_Federal_Supreme_Court_specifies_diligence_require-ments_for_management_and_supervisory_boards_relying_on_external_legal_advice/

BaFin's FAQs with regard to the New Reporting Obligations under Sec. 25, 25a German Securities Trading Act

Since the beginning of the year, market participants and BaFin have been trying to acquaint themselves with the new reporting obligations under Sec. 25, 25a WpHG that came into force on February 1, 2012. Prior to the effectiveness of these new reporting obligations, only directly or indirectly held voting rights (Sec. 21, 22 WpHG) or financial instruments entitling holders to acquire shares with voting rights had to be reported when reaching certain reporting thresholds. However, from now on the same also applies to financial or other kinds of instruments that *merely facilitate* (*ermöglichen*) an acquisition of shares (Sec. 25a WpHG). The primary objective of Sec. 25a WpHG is to prevent a "sneaking-up" on listed companies by way of cash-settled total return equity swaps. In the end, the stricter reporting provisions are a response to the great public attention given to the takeovers in the cases *Schaeffler/Continental* and *Porsche/VW*.

The scope of Sec. 25a WpHG was deliberately defined in broad terms in order to prevent strategies to circumvent the disclosure obligations. As such, the relevant question for market participants is: Which financial or other instruments *facilitate* (*ermöglichen*) an acquisition of shares?

Further specifications for handling instruments regarding own shares and share baskets and indices are contained in Sec. 17a of the Ordinance on Disclosure of Securities Trading and Insider Dealing (*WpAIV*). Much more interesting for market participants are, however, the answers of BaFin in the FAQ-document regarding the new reporting obligations, which is published on the internet (*available on: http://www.bafin.de*). In these FAQs, BaFin comments on several questions of demarcation regarding the new reporting obligations that – at least in part – were and still are subject to a controversial debate. The most important key words are: letter of intent or memoranda of understanding, irrevocable undertakings, handling of pre-emptive purchase rights and the obligation to tender shares for purchase in shareholder agreements, the parallel acquisition of financial or other instruments and

reporting obligations in the course of M&A transactions. While the time when listed companies had to provide information on voting rights – *e.g.* following an M&A transaction – used to be the closing of the transaction (as opposed to the signing of a contract), BaFin now interprets the contract itself as an instrument that enables the respective party to acquire shares. Thus, a real shift of paradigms has taken place.

Since this is only a part of the various topics that are being controversially discussed at the moment, it is reasonable to assume that BaFin's FAQ-document currently comprising 17 questions and answers will expand in the months to come.

For further information on this topic please refer to the publication of Merkner/Sustmann, Erste "Guidance" der BaFin zu den neuen Meldepflichten nach §§ 25, 25a WpHG, in NZG 2012, 241 et seq.

New German Short Disclosure Regime

As of March 26, 2012, new statutory notification and publication requirements will come into force for net short-selling positions in all financial instruments admitted to trading on a German regulated market (Sec. 30i WpHG). Previously, only net short-selling positions in shares of ten explicitly named companies in the financial sector were required to be notified to BaFin.

Net Short-Selling Position

A net short-selling position is deemed to exist when, after netting all financial instruments of a holder, the holder's economic exposure in the company's issued shares (*i.e.*, ordinary shares and preference shares without voting rights, if any) is equivalent to a short-selling position in shares. The calculation of the net short-selling position and the disclosure must be done on a holder by holder basis, *i.e.*, there is no netting and aggregation of positions within a group.

Two-Tier Disclosure System

Sec. 30i WpHG provides for a two-tier disclosure system. Holders whose net short-selling positions reach, exceed or fall below 0.2 percent of the company's issued shares will be required to notify BaFin. In addition, market participants with net short-selling positions that reach, exceed or fall below 0.5 percent of the company's issued shares must publish such positions in the German Electronic Federal Gazette (*elektronischer Bundesanzeiger*). If the net short-selling position reaches, exceeds or falls below the threshold of 0.2 percent (or, as the case may be, 0.5 percent) by a further 0.1 percent, additional notifications and/or publications are required.

BaFin's Draft Regulation

The technical details regarding the calculation as well as the notification and publication of net short-selling positions are provided in the Regulation on the Transparency of Net Short-Selling Positions (*Netto-Leerverkaufstransparenzverordnung – N-LPTVO*) published on March 13, 2012. The newly set-up electronic notification and publication procedure for net short-selling positions is described in the IT information sheet published by BaFin on March 13, 2012. In addition, on March 5, 2012 BaFin published FAQs on the respective specific notification and publication requirements (available on: *http://www.bafin.de*).

Net short-selling positions must be notified and, where applicable, also published by the end of the next trading day after they arise. This shall also apply to net short-selling positions existing as of March 26, 2012. However, no publication obligation in the German Electronic Federal Gazette shall exist as far as comparable notifications have been made prior to March 26, 2012 (Sec. 42b WpHG). Violations of the notification and publication requirement for net short-selling positions are punishable by fines of up to EUR 200,000.

A first overview on the new German short disclosure regime can be found in our Client Publication as of February 2012, New German Long and Short Disclosure Regimes.

Reform of Stock Corporation Act 2012 – Government decides on Draft

On December 20, 2011, the German government passed a governmental draft (*Regierungsentwurf*) Reform of the Stock Corporation Act (*Gesetz zur Reform des Aktienrechts*), the so-called *Aktienrechtsnovelle 2012*.

Increasing Transparency regarding Shareholder Structure

The governmental draft introduces new means to increase transparency with respect to the shareholder structure of

non-listed companies with bearer shares. While the initial ministerial draft (*Referentenentwurf*) stipulated that non-listed companies were no longer allowed to issue bearer shares, the governmental draft completely discards this regulatory model. The existing freedom of choice between bearer shares and registered shares thus in principle remains unaffected for non-listed companies.

However, according to the new governmental proposal, stock corporations are only allowed to issue bearer shares if they are listed or if the shareholder's claim of having a *share certificate issued for his share (Verbriefungsanspruch*) is excluded in the articles of association (*Satzung*). In the latter case, the company shall effect certification in the form of one global share certificate (*Sammelurkunde / Globalurkunde*) and deposit it with a securities deposit bank (in Germany the only such bank is Clearstream Banking AG) or with a foreign depository that meets the prerequisites stipulated in Sec. 5 para. 4 sent. 1 Securities Deposit Act (*Depotgesetz*); such depository is referred to as collective custody (*Girosammelverwahrung*). Contrary to the ministerial draft, the proposed temporary regulation (*Übergangsregelung*) provides for a comprehensive protection of existing non-listed companies whose shares are in bearer form. Under this new regulation, the aforementioned provisions shall not apply to non-listed companies that have issued bearer shares and that were founded prior to December 20, 2011.

Greater Flexibility for Stock Corporations' Funding

With respect to providing greater flexibility for stock corporations' funding, the governmental draft contains the provisions from the ministerial draft concerning preferred shares (*Vorzugsaktien*) without the right to receive arrears (*Nachzahlungsanspruch*) and reverse convertible bonds (*umgekehrte Wandelschuldverschreibungen*). In comparison to the initial terms in the ministerial draft, these new provisions are now more detailed and more specific.

Period for Actions for the Declaration of Nullity

The proposed provision establishing a time limit (*Befristung*) for filing an action to have a shareholders' resolution declared null and void was adopted almost unchanged from the ministerial draft. According to the new provision, a second action for annulment shall only be permitted within a period of one month after the first action to set aside this resolution or to have it declared null and avoid (*Anfechtungs- / Nichtigkeitsklage*) has been published in the company's designated journals (*Gesellschaftsblätter*).

Minor Changes

Finally, the draft contains numerous editorial clarifications and minor changes that were raised in the comments to the ministerial draft. These changes concern in particular the convening and implementation of the general meeting.

A comprehensive summary of the latest reform of the Stock Corporation Act can be found in Merkner/ Schmidt-Bendun, Die Aktienrechtsnovelle 2012 – Überblick über den Regierungsentwurf, DER BETRIEB 2012, 98 et seq.

Government Commission announces Proposed Changes to the DCGK

On February, 1, 2012, the Government Commission on the German Corporate Governance Code (*Deutscher Corporate Governance Kodex – DCGK*) presented its latest proposal for changes to the Code. For the first time since the implementation of the Code, the Commission published explanations of the proposed changes and invited interested stakeholders to participate in the amendment process by submitting comments.

Further Professionalization of the Supervisory Board

The main focus of the proposed changes is on the further professionalization of the supervisory board work. The current recommendations regarding the independence of board members are to become more specific. A catalogue

of negative criteria, under which a board member in general cannot be assumed to be independent, shall be implemented (Point 5.4.2 DCGK). The catalogue, *inter alia*, states that, as a general rule, a supervisory board member is not independent if he or she holds at least 10 percent of the company's shares or is a legal representative of a company that does so. However, according to the explanations, a board member can under special circumstances still be assumed to be independent, regardless of this rule example. Furthermore, in terms of its composition, the supervisory board should in future state specific targets for the number of independent supervisory board members. These targets and the state of implementation should be disclosed in the corporate governance statement (*Erklärung zur Unternehmensführung*).

In addition, several suggestions (*Anregungen*) contained in the Code are reclassified as recommendations (*Empfehlungen*). Furthermore, the former suggestion that the chairman of the supervisory board should not also chair the audit committee will be converted into a recommendation. The former suggestions that the chairman of the audit committee should be independent and not a former member of the company's management board, whose term of office expired less than two years ago, will also be upgraded to a recommendation.

Corporate Governance Statement instead of Management Report

After the implementation of the German Act to modernize Accounting Law (*Bilanzrechtsmodernisierungsgesetz*), listed corporations are required to publish a corporate governance statement as part of the company's management report (*Lagebericht*). In fact, in the future, management and supervisory boards should report on the company's corporate governance in the company's corporate governance statement. In addition, the targets set, the status of the composition of the supervisory board (Point 5.4.1 para. 3 sent. 2 DCGK) and the directors' dealings that go beyond legal reporting obligations (Point 6.6 Abs. 2 DCGK) are to be published in this statement.

Absentee Voting no longer recommended for General Meetings

The recommendation contained in Point 2.3.3 sent. 2 DCGK endorsing absentee voting (*Briefwahl*) will be deleted. This makes clear that it is not obligatory to endorse absentee voting.

The proposed changes to the Code and the respective explanations are available on the website of the Government Commission on the German Corporate Governance Code: http://www.corporate-governance-code.de/eng/news/index.html

Significant Reform of In-Court Restructurings in Germany

With effect as of March 1, 2012, German insolvency law has been significantly reformed with a view to strengthening creditors' influence and facilitating in-court restructurings of distressed companies.

Strengthening Creditors' Influence

Under the new law, creditors will be able to participate in core questions of the restructuring process. For the first time, creditors now have a formal say in selecting the (preliminary) insolvency administrator. Depending on the size of the company, a new preliminary creditors' committee will be established. Through the committee, creditors will be able to influence the selection process of the (preliminary) insolvency administrator, the decision of the insolvency court to order self-administration, as well as the appointment of a preliminary trustee (*Sachwalter*) supervising the debtor during self-administration.

Improved Restructuring Options for Distressed Companies

The reform is intended to strengthen self-administration, which was rarely applied for in the past, by limiting the discretion of the court to deny self-administration. Even during initial insolvency proceedings, the insolvency court

will not be allowed to curtail the control over the debtor unless the application for self-administration is obviously without any prospect of success. Under the previous legal regime, the court appointed a preliminary insolvency administrator during initial proceedings in any event which assumed a great degree of (if not entire) control over the company until self-administration could ultimately take effect.

The reform has further introduced a new so-called rescue umbrella, which is intended to enable an early restructuring of companies. Within a court determined protection period not exceeding three months, the company may work out an insolvency plan. During this period, the court is entitled to issue protection orders in favour of the insolvent company, thereby preventing creditors from individual enforcement actions. In addition, it will now be more difficult for individual creditors to challenge the implementation of an insolvency plan after it has been adopted by majority vote.

Finally, in insolvency plan proceedings it is now possible to complete a debt-to-equity swap and to cram-down dissenting shareholders under certain circumstances. Creditors, however, still face the risk that due to a debt-to-equity swap, the debtor may need to recognise a taxable restructuring profit and/or loose loss carry forwards. This may make a debt-to-equity swap less attractive unless a structure can be designed that eliminates or at least mitigates such tax disadvantages.

If you wish to review additional information regarding the insolvency law reform, you may refer to our client publication entitled "Reform of In-Court Restructurings in Germany – New Options and Implications for Creditors, Debtors and Shareholders", available online at http://www.shearman.com/reform-of-in-court-restructurings-in-germany-03-01-2012/.

Reform of the German Capital Markets Model Case Act (KapMuG)

On December 30, 2011, the German government passed a governmental draft concerning the reform of the German Capital Markets Model Case Act (*Kapitalanleger-Musterverfahrensgesetz – KapMuG*) (BR-Drucks. 851/11) and plans to permanently incorporate the said act into the German legal system. The initial ministerial draft already contained a proposal to extend the scope of the act to cases concerning allegedly incorrect investment advisory and brokering. It also suggested implementing provisions allowing a settlement approved by the court from which the co-summoned (*Beigeladener*) should be permitted to opt out. In addition to these proposals, the governmental draft provides for a temporary regulation. Under this transitory regime, the newly implemented provisions shall not apply to cases that were the subject matter of a hearing prior to the entry into force of the reform. This means that the proposed provisions relating to a settlement will in general not be applicable to pending cases.

An initial overview of the governmental draft can be found in Schmidt-Bendun, "Reform des Kapitalanleger-Musterverfahrensgesetzes", published in the Rechtsboard of Handelsblatt newspaper: http://blog.handelsblatt.com/rechtsboard/category/gastbeitrage/rudiger-schmidt-bendun/.
For a comprehensive review of the ministerial draft please refer to Sustmann/Schmidt-Bendun, Der Referentenentwurf zur Reform des Kapitalanleger-Musterverfahrensgesetzes (KapMuG) in NZG, 2011, 1207 et seq.

Does the Proposed Financial Transaction Tax pass the Practice Test?

There is a common understanding within Europe that the financial sector should contribute more fairly given the costs of dealing with the global economic and financial crisis. The European Commission therefore proposed a common system of a Financial Transaction Tax ("FTT") in September 2011. Pursuant to the proposal, the FTT will be introduced throughout the EU in 2014. The tax rate may not be lower than 0.1% in respect of financial transactions related to shares or bonds or 0.01% in respect of financial transactions related to derivatives. In Germany, a stamp duty and stamp duty reserve tax, as currently in effect in the UK, is being discussed as an alternative taxation of the financial sector. Such stamp duty would cover specific transactions relating to shares and other securities through the stock market or a stock broker and certain other transfers irrespective of where the transaction takes place or which platform is used.

Basic Concept of the FTT

Under the proposal, FTT is triggered in the member state where the financial institution being a party to the transaction resides. The term "financial institution" is fairly broadly defined and encompasses, *inter alia*, investment firms, insurance and reinsurance undertakings and special purpose entities. The FTT generally covers transactions relating to all types of financial instruments. The scope of the tax is not limited to trading in organized markets, but also covers other types of trading, including over-the-counter transactions.

Consequences of the FTT in Practice

The practical consequences of the proposed FTT are difficult to assess. It can be expected, though, that the FTT will lead to fairly detrimental consequences for the affected companies within its scope. In addition, the FTT is triggered by intragroup transactions. Under the wording of the proposal, transactions solely with companies outside the EU are not covered. Therefore, there is a risk that financial transactions will increasingly take place in non-EU states.

Conclusion

Experts take the view that the proposed FTT will not effectively deter harmful transactions due to the fact that financial transactions do not depend on the location where the transaction takes place. In light of the intended aim, regulation may be more effective than taxation. Further, existing tax regimes, such as the German banking levy, could be adapted.

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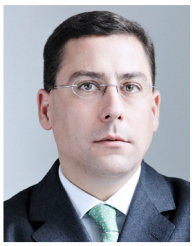

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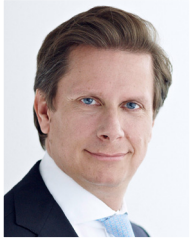

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