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Contents

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1. Trends

1.1 M&A Transactions and Deals

Generally, Austria has seen a fairly robust M&A market in the first quarter of 2019 in line with the global trend, with buyers from the USA and Europe pursuing acquisitions. While there is increasing caution with respect to the global outlook of the economy and uncertain political landscape, it seems that it has not yet adversely affected deal-making in Austria. Based on this observation, it can be expected that 2019 will continue to be a good year for M&A transactions, with additional companies coming to the market in order to benefit from the positive transaction environment, and significant transactions in the pipeline will become active.

Private equity companies are intensively looking for attractive targets and, in line with the general M&A environment, 2019 will again be a good year for private equity transactions. Private equity companies seem eager to exploit the end-of-the-growth-cycle mood of corporations by building market share and value for a future attractive exit. Another trend is the growth desire of private equity buyers looking at distressed opportunities, although such opportunities still appear to be fairly rare at this point in time. Based on a significant increase in start-ups, start-up funding and overall R&D investments in Austria, we also see a strong trend of private equity companies targeting promising growth companies.

1.2 Market Activity

Private equity deals at the top end were spread across sectors without focusing on a specific sector. However, in the mid-market, technology, industrial products, infrastructure, manufacturing and consumer goods are the sectors that are expected to see the strongest interest in 2019. Based on our experience, we expect an increase of investments by private equity in Austria's technology sector as there is a growing interest in Austrian start-ups as well as high-growth companies by private equity companies.

2. Legal Developments

2.1 Impact on Private Equity

In recent years, the most significant legal development impacting domestic private equity funds and transactions was the implementation of the Austrian Alternative Investment Fund Manager Act (AIFMG), based on Directive 2011/61/EU on Alternative Investment Fund Managers, by the Austrian legislator. Typically, Austrian funds not compliant with Directive 2009/65/EC (ie, the UCITS Directive) qualify as alternative investment funds (AIFs) since the introduction of the AIFMG. An AIF is defined as a collective investment undertaking that raises capital from a number of investors in order to invest it in accordance with a defined investment policy which does not use the capital for direct operational purposes.

Generally, managers of Austrian private equity funds are subject to the ongoing supervision of the Austrian Financial Market Authority (FMA). Managers of such AIFs are required to obtain a licence to be issued by the FMA pursuant to the AIFMG. Exceptions to this rule apply with respect to most of the Austrian funds where no such licence is required for managers of the mentioned funds provided that the cumulative AIFs under management: (i) fall below a threshold of EUR100 million in cases where leverage is used; and (ii) where the cumulative AIFs under management fall below a threshold of EUR500 million in cases where no leverage is used. When it comes to investments of private equity funds in Austria, the restrictions on asset stripping and additional disclosure requirements as outlined in the AIFMG based on the AIFMD may be relevant.

3. Regulatory Framework

3.1 Primary Regulators and Regulatory Issues

The primary regulators that are or may be relevant to private equity funds and transactions are the FMA, the Federal Competition Authority (FCA), the Austrian Takeover Commission (ATC) and the Ministry of Digital and Economic Affairs (MDEA).

Generally, there are no specific regulations that specifically address or discriminate against private equity transactions. However, certain areas of public interest (eg, in case of investments into sectors such as banking) impose restrictions depending on the identity of the buyer.

Austrian Foreign Trade Act

Pursuant to the Austrian Foreign Trade Act (*Außenwirtschaftsgesetz*, AFTA), foreign direct investments (FDI) are restricted to a certain extent. Pursuant to this regulation, the acquisition of 25% or more of the voting rights in an Austrian entity by a foreign investor (ie, non-EU/EEA/Swiss investors) requires an approval of the MDEA if such Austrian entity is operating in the sector of internal and external security, public order and safety, procurement services and crises prevention such as defence and security services, telecommunication services, water supply, healthcare, infrastructure, energy supply, traffic and education. A foreign investor is advised to assess the compliance of the envisaged transaction with the AFTA in the early stage in order to avoid unexpected consequences.

The approval of the MDEA must be obtained prior to the signing of an applicable transaction. The MDEA has a one-month review period – or, in certain cases requiring an in-depth assessment, a two-month review period – from the date of the delivery of the relevant notification. A case is deemed cleared if the MDEA does not issue a decision within these periods.

The MDEA has recently published a consultation draft for amendments to the AFTA. The draft aims to create more transparency and certainty with respect to FDI approvals in Austria and a sharper approval regime for certain transactions; it is expected to enter into force during the third quarter of 2019. Pursuant to the draft, an entity is subject to the FDI regime if the acquisition is likely to affect "security and public order" in the following non-exclusive list of sectors:

- critical infrastructure (physical or virtual) and technologies, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, biotechnologies, etc;
- supply of critical resources, including energy or raw materials and food security;
- access to sensitive information, including personal data, or the ability to control such information;
- the freedom and pluralism of the media.

Under the current regime, the acquisition of 25% or more of the voting rights in an Austrian entity is subject to an AFTA review (see above). Generally, this threshold will continue to apply under the draft. However, with respect to companies in certain business sectors – including those that operate critical infrastructure in the field of information technology, develop software for critical infrastructure, provide cloud computing services, belong to the media industry or produce certain defence-related products – the minimum threshold will be reduced to 10%.

Antitrust Regulations

The Austrian merger control rules apply to concentrations as defined in Section 7 of the Austrian Cartel Act (ACA). Each of the following events constitutes a concentration:

- the acquisition by one undertaking of all, or a substantial part of, the assets of another undertaking, in particular by means of transformation or merger;
- the acquisition of rights by one undertaking in the business of another undertaking by means of a management or lease agreement;
- the direct or indirect acquisition of shares in one undertaking by another undertaking if, as a result, a participation of 25% or 50% (in terms of capital or voting rights) is reached or exceeded;
- the establishment of interlocking directorates at the management or supervisory board level if at least half of the management or supervisory board members of two or more undertakings are identical;
- any other connection of undertakings conferring on one undertaking a direct or indirect controlling influence over another undertaking; and
- the establishment of a full-function joint venture.

A concentration must be notified prior to its completion if, in the last business year:

- the combined worldwide turnover of the undertakings concerned exceeded EUR300 million;
- the combined Austrian turnover of the undertakings concerned exceeded EUR30 million; and
- the individual worldwide turnover of each of at least two undertakings concerned exceeded EUR5 million.

Pursuant to the de minimis exception, concentrations which meet these thresholds are, however, exempted from the notification requirement if the Austrian turnover of only one of the undertakings concerned exceeded EUR5 million and the worldwide combined turnover of the other undertakings concerned did not exceed EUR30 million.

A concentration which does not meet the turnover thresholds mentioned above still has to be notified if, in the last business year:

- the combined worldwide turnover of the undertakings concerned exceeded EUR300 million;
- the combined Austrian turnover of the undertakings concerned exceeded EUR15 million;
- the value of consideration for the transaction exceeds EUR200 million; and
- the undertaking to be acquired is active in Austria to a significant extent.

Special rules apply to the calculation of the turnover of banks and insurance companies and in relation to 'media concentrations'.

A concentration which meets the turnover thresholds of the EU Merger Regulation and requires a merger control filing with the European Commission is not subject to Austrian merger control (unless the transaction qualifies as a 'media concentration', in which case parallel notifications to the European Commission and the FCA may be required).

4. Due Diligence

4.1 General Information

The scope and depth of legal due diligence of private equity buyers is usually significant, covering all relevant legal aspects of the target, such as title, contracts, compliance with law, change of control, reorganisations, real estate, employment, regulatory, IP, financings, disputes, and, increasingly, GDPR compliance (based on recent fines levied as a result of breaches under the GDPR).

The typical reporting format is a red-flag reporting standard, but based on a full-scope legal due diligence. Commonly, the legal due diligence is done within a four to six-week timeframe depending on the size of the target and how well prepared and committed the seller is. In urgent cases, the due diligence can be conducted within a two-week or even a shorter period. We have seen private equity deals where the due diligence is divided in two phases: in the first phase the buyers focus more on the areas relevant to categorise the value of the target, followed by an in-depth due diligence in the second phase. Some auction sale processes are geared towards allowing bidders to do a limited due diligence in order to contain legal fees in the early phase of a transaction and, prior to a more limited number of bidders, committing to a full-scale process.

4.2 Vendor Due Diligence

In the past few years, vendor due diligence or a fact book has been a common feature of private equity sellers. The seller usually prepares an information memorandum, conducts a vendor's due diligence and, often, prepares a legal fact book (instead of a vendor due diligence report) which will be shared with the bidders in the data room. Commonly, the advisers of the sellers request the signing of a non-reliance letter before the disclosure of the vendor due diligence report and/or the legal fact book. In the recent past we see a slight trend towards sellers offering reliance, predominately with private equity sellers. Private equity buyers regularly offer reliance on buy-side due diligence to the banks financing the buyer.

5. Structure of Transactions

5.1 Structure of the Acquisition

Commonly, disposals by private equity funds are carried out by auction sale as such process is more stringent, seller-friendly and allows the seller to maximise the sale proceeds. Typically, the auction process is handled by investment banks and/or other M&A advisors. No specific provisions apply with respect to an auction process – ie, the seller determines the rules and procedure of the auction by issuing detailed process letters. To a varying extent, the terms of an acquisition may differ between a privately negotiated transaction and an auction sale depending on the overall circumstances of the transaction – eg, the size of the transaction, the percentage of the shareholding in the target, whether one of the parties is a listed company or not, etc. While set up as a broad auction process, in many cases bidders (in particular private equity) seek to shorten the transaction process by quickly proposing an agreement on key terms and by offering transaction certainly ahead of other bidders.

5.2 Structure of the Buyer

Generally, the acquisition structure is tax-driven with financing requirements, liability and exit considerations, and specific transaction-related considerations all playing a role. Most typically, a non-Austrian TopCo (incorporated in a tax favourable jurisdiction such as Luxembourg, the Cayman Islands or the Netherlands) holds an Austrian AcquiCo in the form of a limited liability company, which acquires the Austrian target; this also helps to ring-fence the investment. Private equity funds are closely involved in structuring the key deal terms and the liability regime but otherwise rely on their lawyers to reach market-standard deal terms. Also, when acting for private equity owned portfolio companies on add-on acquisitions, the private equity owners will be involved in the transaction (though to a more limited degree).

5.3 Funding Structure of Private Equity Transactions

It is more typical for the private equity funds to hold a majority stake. Although we have seen larger private equity funds holding minority stakes in target companies with regulated revenue streams, minority stake private equity deals are rather an exception.

The type and structure of financing of private equity deals depends, inter alia, on the contemplated acquisition structure, the relevant tax environment, the industry of the target group, the aggregate deal volume (including re-financing/working capital requirements of the target group) and the standing of the relevant private equity fund on the market. Typically, acquisitions by private equity funds are highly leveraged – ie, to a large extent financed by various debt instruments that are available in the market from a variety of potential funders (eg, commercial banks, debt funds, insurance companies, pension funds, mezzanine lenders, etc) – whereas the residual financing portion is provided by the private equity funds in the form of equity, equity-like means and/or junior funds.

Senior Debt

Senior debt is provided by means of senior secured (and usually syndicated) loans (and may also take the form of senior secured bond instruments) and encompasses typically (i) a facility applied towards partial financing of the purchase price, (ii) a facility enabling the target companies to re-finance existing debt, and (iii) a facility to finance working capital requirements of the target companies. To the extent permitted by applicable laws and reasonable in light of the relevant tax environment, private equity funds may want senior debt to be pushed down to the target companies (in terms of debt service and security instruments).

Mezzanine Debt

Mezzanine debt is a hybrid of senior and junior debt and ranks junior to senior debt and senior to junior debt. Typically, Mezzanine instruments have lighter covenants of the obligors and may be secured second ranking behind the senior security package. Consequently, mezzanine carries higher interest reflecting the risk position of the mezzanine debt providers.

Junior Funds
Junior funds are usually provided in the form of shareholder loans being deeply subordinated and ranking senior only to equity. Junior funds are, therefore, typically unsecured and will only be serviced if certain financial covenants are met and after senior and mezzanine debt service.

5.4 Multiple Investors
Deals involving a consortium of private equity sponsors and co-investments by other investors alongside the private equity fund are not very common in Austria, mostly because the target companies in Austria are not large; rather, such transactions are seen where Austrian players team up with international private equity funds and other investors, typically for big ticket transactions. The so-called 'club deals' in private equity industry are seen on a global level which allow each private equity participant to reduce its concentration, maintain the diversification of its portfolio of investments and allocate risks and costs. However, such club deals have certain downsides, including conflicts among the investment strategies of the various participants. An increase of club deals in Austria is not expected.

6. Terms of Acquisition Documentation

6.1 Types of Consideration Mechanisms
Generally, the parties agree either on a locked-box consideration structure or a closing accounts consideration structure which may be combined with an earn-out element in private M&A transactions. In 2019, there was an increase in the application of locked box structures as compared to 2018 and the years before. Transaction speed and transaction certainty are increasingly a key feature for M&A transactions, with private equity often outpacing corporate bidders by way of offering a 'fast-track' transaction including a strong pricing proposal. Private equity funds prefer locked box consideration structures particularly when acting as sellers.

In connection with locked box consideration structures, private equity sellers provide the following protection(s):

- no leakage and anti-leakage protection on a euro-by-euro basis;
- ordinary course of business covenants;
- dispute resolution mechanism with respect to the leakage amount (see **6.3 Dispute Resolution for Consideration Structures**, below).

Warranty insurance is widely used by private equity sellers in order to limit recourse against the seller.

6.2 Locked Box Consideration Structures
Some buyers consider whether interest should accrue on the amount of leakage and/or whether leakage (exceeding a certain threshold) should lead to any walk-away right. However, there have not been many private equity deals where interest was in fact charged on a locked box leakage or where a walk-away right was agreed in the case of leakage.

6.3 Dispute Resolution for Consideration Structures
It is common to have a dispute resolution mechanism in place for (i) locked box consideration structures and (ii) completion accounts consideration structures in private equity transactions. In the case of completion accounts the parties agree on expert determination proceedings and arbitration proceedings in the case of disagreement with respect to the adjustment of the purchase price. In many cases the agreements provide for an expert determination in relation to the purchase price adjustment and additionally for a broad arbitration clause (as opposed to ordinary courts having jurisdiction). A similar dispute resolution mechanism is common with respect to locked box consideration structures – ie, the parties agree on an expert determination in addition to arbitration proceedings in relation to the leakage (adjustment) amount.

6.4 Conditionality in Acquisition Documentation
The acquisition agreements of a private equity deal are usually subject to a very limited number of (regulatory) conditions. The typical level of conditionality in private equity transactions is limited to mandatory regulatory clearances such as merger clearance. In particular, a private equity seller is unlikely to accept other conditions, such as a 'no material adverse change' condition, a financing condition or any similar condition. Process letters of sellers in an auction scenario typically require binding bids to not be subject to conditions other than regulatory clearances. Depending on the target, private equity buyers take a more prudent approach by seeking strong sell-side protection in return for an attractive price offer. This includes material adverse effect or change of control protection.

6.5 'Hell or High Water' Undertakings
Usually, a 'hell or high water' provision describes an independent and absolute commitment of the buyer to undertake any obligation that is required to obtain antitrust or other regulatory approval. Whereas it is common for buyers to agree on prompt filing and consulting with the seller, it is not common for a private equity buyer to accept a 'hell or high water' undertaking in deals where there is a regulatory condition.

Parties to a purchase agreement may agree on a 'light hell or high water' undertaking with respect to merger control clearance by introducing thresholds or other criteria (eg, divestment of an entity with an EBITDA below a certain threshold) in order to quantify and allocate antitrust risks connected with the transaction between the parties.

6.6 Break Fees

In private acquisitions (see **7.5 Conditions in Takeovers**, below, with respect to break fees in public M&A transactions), the parties frequently agree on (reverse) break fees in order to avoid damages, keep the cost risk low, and increase deal security. If the obliged party is a stock corporation, the permissibility of the amount of the break fee is based on the appropriateness of the break fee considering all of the individual circumstances on a case-by-case basis. In this context in particular, the type, scope and strategic importance of the particular transaction plays an essential role and must be assessed on the basis of the obligations of the management resulting from the business judgement rule. No such limitations apply to the extent the obliged party is a limited liability company and the relevant corporate approvals are in place (eg, the approval of the supervisory board or shareholder, if necessary).

In conditional deals with a private equity backed buyer, break fees are not very common as private equity deals are typically subject to a very limited number of conditions and as there is limited space for deal security elements. The same applies to reverse break fees which typically result in payment obligations of the buyer and which are usually only agreed to with respect to the fulfilment of financing condition.

6.7 Termination Rights in Acquisition Documentation

Commonly, acquisition agreements exclude all rights of the parties provided by law to terminate the contract to the fullest extent possible. Important exceptions are the right of both parties to terminate the agreement in case closing cannot be brought about by a certain date ('long-stop date') or if regulatory approvals are subject to obligations which the purchaser is not prepared to accept (ie, in the absence of a hell and high water clause). Occasionally, purchase agreements also provide for a material adverse change clause, including instances where the business deteriorates dramatically prior to closing, and which entitle the buyer to not proceed to closing and to terminate the agreement; such arrangements do not tend to occur in situations with private equity sellers. However, termination rights of a party upon a break fee payment event (ie, non-compliance with the obligation of the buyer or the seller in connection with the conditions precedent agreed in the acquisition agreements) are in evidence.

6.8 Allocation of Risk

As in private equity transactions the parties usually agree on locked box consideration structures, the typical allocation of risk between the locked box date and the closing date is the agreement on protection by way of ordinary course of business provisions and no leakage provisions and covenants. Private equity sellers typically seek to limit any legal recourse by the buyer to the maximum degree possible so as to fully protect the availability of the transaction proceeds for their investors.

Private equity sellers typically provide a high level of disclosure by way of a well-prepared due diligence process and the possibility of bidders to conduct an extensive due diligence.

Matters so disclosed typically eliminate warranty protection of a buyer which is deemed to have priced its offer based on information available to it on the basis of the due diligence. In addition, private equity sellers offer very limited contractual protection to buyers. This means that the quality of the due diligence process is very important for the buyer.

In addition, warranty insurance protection is widely used to protect the private equity seller against possible warranty claims by a buyer. The costs of warranty insurance have come down significantly over the last two years.

To the extent a buyer identifies a risk in the course of the due diligence, the parties either price such risk into the calculation of the purchase price or provide for an indemnity protection. Generally, indemnities are not subject to limitations other than with respect to amount and time limitations. Private equity sellers will not easily accept indemnification obligations for the reasons already stated.

Typically, the parties agree on further liability limitations of the seller depending on the transaction such as:

- time limitation for bringing claims;
- financial limits (eg, caps, baskets, de minimis claim exclusions);
- limitation to direct loss (as opposed to indirect and consequential loss); and
- mitigation obligations.

Usually, the parties agree on short periods upon expiry of which the warranty or indemnity claims become time-barred with claims on the basis of title warranties or no leakage obligations allowing for longer claim periods. The liability of the seller is usually capped at a certain percentage of the purchase price. The liability of the seller with respect to fundamental warranties such as claims for a breach of the title are usually capped at an amount corresponding to the purchase price amount.

6.9 Warranty Protection

Please see **6.8 Allocation of Risk**, above, with respect to warranty and indemnities in private equity deals. Generally, the private equity sellers desire to offer almost no warranties and indemnities in order to be able to allow for a clear financial exit to their investors. However, there are now more and more structures where either warranty insurance bridges the gap between the offered warranty/indemnity package and the requested protection needs of buyers, or private equity sellers accept a warranty/indemnity package to a certain extent (eg, a small portion of the purchase price is kept as an escrow hold-back).

Typically, the private equity seller provides to a buyer exit warranties on legal organisation, taxes, financial statements, employment, properties and assets, intellectual property, financing, commercial agreements, litigation and compliance. However, there is an increasing trend to limit operational warranties.

In some cases, the management team provides to a buyer statements which do not qualify as warranties but are aimed at providing comfort to the buyer on a non-recourse basis, mostly in relation to operational aspects (for example, that there is no pending or threatened litigation).

6.10 Other Protections in Acquisition Documentation

In recent years, warranty and indemnity insurance covering damages resulting from breaches of warranties and indemnities has become a key part of transactions, including transactions in the Austrian private equity market. Excluded from the insurance package are usually known risks or statements where the due diligence exercise has been weak. Such warranty and indemnity insurance is increasingly used to cover the gap between the seller's interest in limiting its exposure and achieving a clean exit and the protection and recourse requirements of the buyer. (Please also see **6.9 Warranty Protection**, above).

6.11 Commonly Litigated Provisions

Litigation in connection with private equity transactions is common. The frequency of litigation is volatile and generally depends to an essential extent on the performance of the private equity market and related transactions.

It is standard market practice in international private equity transactions to agree on arbitration clauses. The main advantages of arbitration are that the tribunal has experience in international transactions and knowledge of the underlying economic aspects of such deals compared with court litigation. In particular the failure to complete the transaction, price adjustment, leakage amounts, leakage adjustments, earn-outs, and breach of warranties are the subject of SPA-related arbitration. Disputes over financial aspects of a private equity transaction (such as leakage adjustment disputes) may alternatively or additionally be subjected to arbitral expert (*Schiedsgutachter*) procedures if accounting principles, calculation aspects or auditing processes are concerned.

7. Takeovers

7.1 Public to Privates

Public to private transactions, in particular with respect to private equity transactions, are uncommon in the Austrian market as there are only a few Austrian public companies with a large number of free-float shareholders. In public-to-private deals, the private equity fund would have to launch a voluntary takeover offer aiming for control typically combined with the condition of reaching the acceptance threshold of at least 90% of the shares of the target company. Upon reaching such threshold, the private equity fund can squeeze out the remaining minority shareholders. While public takeovers by private equity are on the rise globally, we do not expect an increase of such transactions in Austria.

7.2 Material Shareholding Thresholds

A shareholder of a public company is required to publicly disclose its shareholdings to the FMA, the Stock Exchange and the issuer, if it – directly, indirectly or through financial instruments or derivatives – reaches, exceeds or falls below 4%, 5%, 10%, 15%, 20%, 25%, 30%, 35%, 40%, 45%, 50%, 75% or 90% of the voting rights. The articles of association may contain an additional disclosure threshold at 3% which will need to be published on the website of the issuer; additionally, the FMA will need to be informed. A shareholder is required to disclose immediately, and in any event within two trading days, each time a relevant threshold falls below or exceeds any of the threshold amounts.

If a shareholder does not comply with the above-mentioned disclosure obligations, voting rights attached to the shares not disclosed will be automatically suspended. The articles of association of the company may also extend the suspension of voting rights to all voting rights of the shareholder breaching the required disclosure obligation.

7.3 Mandatory Offer Thresholds

A bidder who acquires a direct or indirect controlling interest in a public company must launch a mandatory offer in relation to all shares pursuant to Section 22 et seq of the Takeover Act (TA). The initial acquisition of a controlling interest and any change of control are encompassed by the above-mentioned provision and each trigger the obligation of launching an offer. However, the acquisition of up to 30% of the voting rights does not trigger any obligation to launch a mandatory offer (safe harbour). However, a shareholding between 26% and 30% must be notified to the ATC. Consequently, the acquisition of voting rights of more than 30% triggers the obligation to launch a mandatory bid for all shares.

7.4 Consideration

Commonly, cash considerations are used in public M&A transactions. The bidder is entitled to offer cash, shares or a combination of cash and shares. There are generally no minimum pricing rules or cash requirements. However, in a mandatory offer and a voluntary offer aimed at control, the bidder must offer a cash consideration and can only offer shares as an alternative to such cash offer. In such a case the cash consideration offered must comply with the minimum price requirements – ie, the cash offer must be (i) at least, the higher of the average share price of the target shares during the six-month prior to the publication of the offer, or (ii) the highest price paid or offered for the target shares by the bidder in the 12 months prior to filing the offer.

7.5 Conditions in Takeovers

Pursuant to Section 8 of the TA, in the case of voluntary offers and voluntary offers to acquire control, the offer can be conditional on the fulfilment of conditions. Generally, conditions are permissible pursuant to the TA to the extent the conditions are objectively justified. In practice that means each relevant condition with respect to a takeover offer must be analysed and assessed on a case-by-case basis. Generally, conditions are not permitted to the extent their fulfilment is at the discretion of the bidder. Pursuant to Section 25b of the TA mandatory offers can only be subject to conditions which are required by law such as the approval from antitrust authorities.

In public M&A transactions, the agreement of break fees is generally not prohibited but break fees are fairly uncommon in practice. Depending on the amount of break fees, such agreement may hinder competing offers and thereby violate the provisions of the TA. An agreement with respect to break fees must be explicitly contained in the offer document.

7.6 Acquiring Less Than 100%

If a private equity bidder does not seek or obtain 100% ownership of a listed target, the governance rights with respect to the target outside of its shareholdings very much depend on the rights connected with the shareholding of such bidder by law and under the existing by-laws of the target. Therefore, the investor should first analyse details of the rights available to it by law, based on the level of its shareholding, and in the existing governance documents prior to developing a strategy on optimising corporate governance.

Shareholders holding more than 25% of a company's share capital present at a shareholders' meeting may object to the amendments of the articles of the company (including capital measures) and measures excluding shareholder subscription rights. Shareholders holding at least 30% of a company's share capital have the right to elect an additional supervisory board member if three or more members of the supervisory board are elected in one shareholders' meeting and one candidate got at least one-third of the votes in all prior elections without being successfully elected. In that case the unsuccessful candidate having received the one-third vote in prior elections will be declared as elected without any further votes.

It is to be expected that private equity funds seek the right to nominate board members and to request veto rights (though there is no Austrian practice in relation to private equity targeting listed companies).

Pursuant to the Squeeze-Out Act, a majority shareholder which directly or indirectly owns 90% of the share capital of a target is entitled to squeeze out the remaining minority shareholders. The minority shareholders cannot stop the squeeze out but can generally request the compensation granted to them to be reviewed by a court. The mentioned squeeze-out process applies to public and private companies. Therefore, a voluntary offer aimed at control often contains a minimum acceptance threshold of 90% in order to ensure the possibility of a squeeze out and the acquisition of all the shares in the target following a successful tender offer.

7.7 Irrevocable Commitments

Irrevocable commitments are usually only concluded with the principal shareholder of the target and are promises of security holders of the target to tender their shares to the bidder in the course of a takeover offer. This way the bidder tries to secure securities in the target company prior to the announcement of its decision to make an offer. In particular, the agreement of irrevocable commitments makes it easier for the bidder to determine an offer price for the envisaged transaction (the value arrived at during the negotiations for the acquisition of a controlling stake – please see **7.4 Consideration**, above).

Irrevocables are not prohibited under the TA and there are good arguments as to why irrevocables are permitted. Generally, principle shareholders are entitled to freely dispose of their shares and, in particular, to agree on the sale of their shares to the bidder. However, the literature points out that irrevocables may discourage competing offers and not comply with the duty of confidentiality. Therefore, irrevocables should be cleared with the ATC in advance.

7.8 Hostile Takeover Offers

Hostile takeover offers (ie, offers that are not supported by the management board and supervisory board of the target) are permitted but uncommon in Austria. The TA does not differentiate between hostile and friendly takeovers – the same rules apply to both types of takeover offers. Private equity backed buyers did not engage in hostile takeover offers in Austria so far. In the case of a hostile takeover, the management and supervisory board of a public company are not entitled to implement defensive measures but are required to remain neutral pursuant to Section 12 of the TA in consideration of the interest of the shareholders.

8. Management Incentives

8.1 Equity Incentivisation and Ownership
Equity incentivisation of the management team is a common feature of private equity transactions in Austria in order to ensure their commitment following the change of the ownership in the target. Therefore, the management usually has the opportunity to acquire an interest in the target company. The level of equity ownership for the management team depends on the specific circumstances of a transaction, but often a shareholding corresponding to 10% is granted to the management team; in smaller deals, an even higher shareholding, corresponding to up to 20%, may be granted.

8.2 Management Participation
Commonly, the management team of the target has the opportunity to acquire shares in the target company and sometimes such participation and commitment is required by the buyer. The structure of the management participation is also tax-driven. There are also deals where the management team is offered the opportunity to invest in the same instruments ('institutional strip') acquired by the private equity buyer to ensure that the interests of the management and such buyer are fully aligned. To the extent the management is invested on a target level, we have seen different structures such as share options, profit participation rights without any voting rights and phantom stock options.

Typically, shares held by the management are pooled (ie, the investor has de facto one co-investor). Commonly, restrictions encompass a drag-along right of the private equity fund and other obligations to transfer the shares to the extent the management and employment agreements are terminated. The pricing formula, which is to apply to the transfer of shares following termination, depends on the reason for such termination.

8.3 Vesting/Leaver Provisions
Commonly, leaver provisions for management shareholders are the so-called 'good leaver' and 'bad leaver' provisions impacting, in particular, the price for their shares to be transferred following the termination of their management agreement, vesting provisions and the option for the investor to purchase the shareholding of the management team in the case of termination. Typically, good leaver provisions are more favourable to management and apply in the case of the termination of a management agreement without cause, illness of the manager or the expiry of the term, whereas other termination causes usually qualify as bad leaver events which provide for less favourable sale terms for the management.

8.4 Restrictions on Manager Shareholders
The customary restrictive covenants agreed to by the management shareholders are usually non-compete and non-solicitation undertakings. To the extent the management shareholders are employees of the target (assuming the target is either a limited liability or a stock corporation), such managing directors are required by law to fulfil non-compete and non-solicitation obligations throughout the period of their management position.

Generally, non-compete and non-solicitation provisions are enforceable for a period of two years following the termination of the relationship with the company in combination with the sale of shares. To the extent the shareholder is an employee of the company, the enforceability of the above-mentioned non-compete and non-solicitation provisions is generally limited to one year from the termination of the employment agreement, provided the above-mentioned undertakings do not limit the shareholders future professional opportunities.

8.5 Minority Protection for Manager Shareholders
Please see **10.3 Tag Rights**, below.

Management shareholders sometimes enjoy tag-along rights, in particular in start-up companies and companies with considerable upside potential. Also in evidence are anti-dilution protection mechanisms in favour of the management owning target shares.

Typically, the management team does not have a right to control or influence the exit. However, a strong management team will have de facto influence on the process by bidders seeking to incentivise such a team to stay on.

9. Portfolio Company Oversight

9.1 Shareholder Control
The level of control for a private equity fund shareholder over its portfolio companies depends in particular on the legal form of the portfolio companies. Most typically, a non-Austrian entity holds an Austrian entity in the form of a limited liability company, which acquires the Austrian target (please see **5.2 Structure of the Buyer**, above). The private equity fund is usually the sole or majority shareholder of each portfolio company which is organised as a limited liability company in Austria. The majority shareholder of a limited liability has far-reaching control rights and instruction rights vis-a-vis the management. In particular, the shareholders can:

- instruct the managing directors to implement certain measures, whereby the managing directors are bound to such instructions; and
- remove the managing directors without cause at any time

Typically, the management board is required to comply with pre-defined rules of procedure setting out the requirement of shareholder consent or consent of an advisory board with respect to important measures of the company. The abovementioned rules of procedure, the instalment of an advisory board which has information and consent rights – together with the shareholder right to dismiss and appoint the management board – are essential shareholder rights enabling the private equity shareholder to exercise tight control over its portfolio companies.

9.2 Shareholder Liability

Generally, a private equity fund majority shareholder cannot be held liable for the actions of its portfolio companies. However, certain exceptions to this general rule apply which encompass in particular the following cases:

- the private equity fund majority shareholder causes the insolvency of a portfolio company;
- the private equity fund majority shareholder de facto manages the portfolio company (*faktische Geschäftsführung*), whereby in such cases the actual managing director has de facto no managing function and such action bringing about adverse consequences for the company and its creditors; and
- the assets of the private equity fund majority shareholder and the portfolio company cannot be separated (*Sphärenvermischung*).

9.3 Shareholder Compliance Policy

Private equity fund shareholders typically impose their stringent compliance policies on the portfolio companies to the extent such compliance policies do not violate Austrian law. This is in most cases required by the investors in the private equity fund in order to meet investment criteria. It also is an important element in preparing the company for a future sale.

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10. Exits

10.1 Types of Exit

The typical holding period for private equity transactions before the investment is sold or disposed of is about four to five years and private equity sellers typically reinvest upon exit. As a result of the 2008 financial crisis, we have seen longer holding periods – in particular in relation to financial institutions owned by private equity. The most common form of private equity exit we have seen so far are trade sales (ie, sale to a strategic investor) and secondary transactions (ie, sale to a financial investor). Some of the recent exits in Austria were run as dual-track processes and finally did take the IPO route (in both cases financial institutions).

10.2 Drag Rights

Typically, shareholder agreements include a transfer obligation of the shares of a limited liability company such as drag-along rights; we have seen private equity sellers utilising the drag mechanism. To the extent an agreement contains drag-along rights, tag-along rights or other option rights (such as put or call options), for a limited liability company it must be executed in the form of an Austrian notarial deed (*Notariatsakt*) in order to be enforceable.

10.3 Tag Rights

Please see **10.2 Drag Rights**, above.

Management shareholders sometimes enjoy tag-along rights depending on the deal and are rather prevalent in start-up companies and firms with considerable growth potential.

10.4 IPO

Generally, an IPO may provide for certain advantages compared to other disinvestment types; on average, higher prices for the participation are achieved when going public. In addition, in the case of a sale the private equity investor remains flexible and does not have to bind itself to one contractual partner. Moreover, the investor can usually profit from the increase in value of its unsold shares.

Typically, the underwriting banks request the lock-up of the private equity seller to a certain extent – ie, with respect to a limited portion of the shares and subject to time limitations (usually between three and six months following the IPO).