Wilmer, Cutler & Pickering

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Securities Law Developments

The Application of U.S. Securities Laws To European Merger Negotiations

This newsletter is to let you know about an important proceeding instituted by the U.S. Securities and Exchange Commission ("Commission") against the German company E.ON AG, formerly known as Veba AG, for deliberately issuing materially false and misleading statements denying it was engaged in merger negotiations with Viag AG. On September 28, 2000, the Commission accepted an offer of settlement from E.ON AG and ordered E.ON AG to cease and desist from committing or causing any violation and any future violation of section 10(b) of the Securities Exchange Act.[1]

Background

From July 29, 1999, until August 31, 1999, Veba denied repeatedly that it had been engaged in merger negotiations with Viag. In reality, in April, June, and July, Veba and Viag had been involved in high-level merger discussions. By July 29, Veba and Viag had retained investment bankers and legal counsel to advise on the merger negotiations, exchanged financial forecasts, executed a confidentiality agreement, and advised the German Cartel Office of the potential merger. Nevertheless, in response to press inquiries following a leak that Veba and Viag had sought preliminary approval of the merger from the German Cartel Office, Veba denied it was in merger talks or negotiations with Viag or any other market player. Veba published its denials in German and English with the intention of reaching investors in both Germany and the United States. Veba's CEO and Chairman of its Board of Management implemented its "absolute denial" policy, because Veba believed that disclosure would decrease its ability to obtain support from labor, government officials, and German state governments.

From August 31 until September 1, Veba responded to further press inquiries by stating that it had "no comment." Veba's Chairman made this change, because he believed that the likelihood Veba would merge with Viag was much greater and the press started asking questions about specific aspects of the merger. Veba never corrected its prior denials of any merger discussions.

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[1] A copy of the offer of settlement and the Commission's findings may be found on the Internet at http://www.sec.gov/enforce/adminact/34-43372.htm.

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On September 1, Veba and Viag acknowledged for the first time that they had agreed on the basic outline of a merger, and on September 27, 1999, they held a joint press conference to announce the merger.

Legal Findings

The Commission found that E.ON AG had violated section 10(b) of the Securities Exchange Act and Rule 10b-5 by deliberately issuing materially false and misleading statements during August 1999, in which its management denied the existence of merger negotiations with Viag. Under the antifraud provisions of U.S. securities laws, where a corporation denies that merger discussions are taking place, or makes a partial disclosure of information regarding a merger, it is under a duty to disclose material facts necessary to make the statements not misleading. Moreover, a corporation has a duty to correct statements made by its representatives when it learns that such statements were inaccurate or misleading when made. By July 29, when Veba's negotiations with Viag advanced to the point where they were material, Veba violated these duties by disseminating false denials concerning its merger negotiations with Viag. Its "no comment" response to press inquiries during the twenty-four hour period before its public announcement of a basic outline of a merger failed to correct Veba's prior false denials.

The Commission had jurisdiction over E.ON AG, because in 1997 Veba registered with the Commission under section 12(b) of the Securities Exchange Act and began to list its American Depositary Receipts on the New York Stock Exchange. In addition, Veba had a significant presence in the United States and derived approximately $4 billion, or eight percent of its 1999 revenues, from its U.S. operations. Although disclosure practices and laws regarding the existence of merger negotiations may differ in Europe, the Commission stated that it would not apply a different legal standard to foreign issuers that voluntarily availed themselves of opportunities in the U.S. capital markets.

Corporations in Europe that have registered with the Commission and list their securities on a U.S. stock exchange or otherwise fall within the jurisdiction of U.S. securities laws should be aware of the Commission's disclosure rules and regulations. In particular, during merger negotiations, such corporations, no matter where they are located, should not disseminate materially false and misleading information about the existence and/or status of a potential merger. Corporations do not have a duty to speak and comment about merger discussions. However, under U.S. securities laws, should a corporate representative speak about a potential merger - whether to deny or confirm its existence, the corporation undertakes a duty to disclose all material information completely and accurately.

If you have any questions regarding the application of U.S. securities laws to European matters, please contact Harry Weiss (202-663-6993), Jeffrey McFadden (202-663-6385), or Reed Brodsky (202-663-6401).

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