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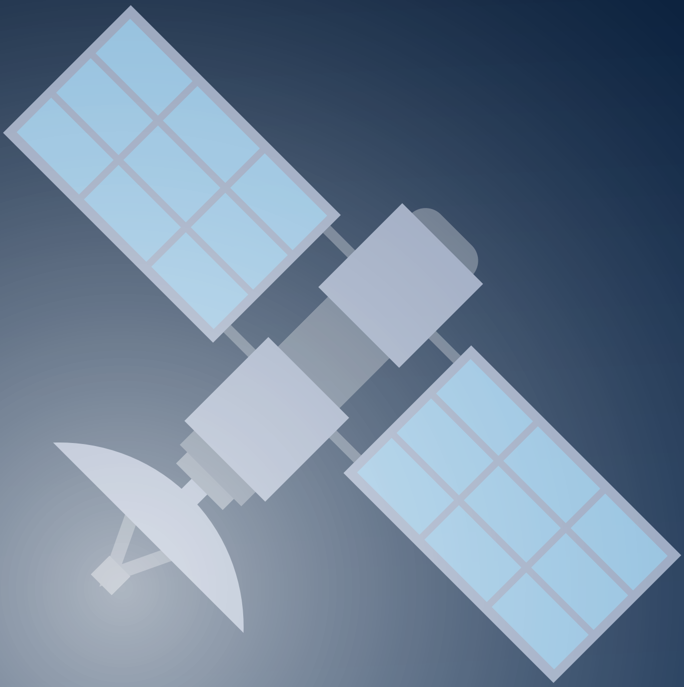

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In the game of regulations:

Outlook on relevant legislative changes for the M&A practice in 2025

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1. Introduction

The following article shall provide an overview of certain recent developments and legislative changes that may going forward affect the M&A market and the transaction business. The requirements for M&A transactions established by the AI Act will have to be observed already in the due diligence as well as in drafting the transaction documents (see section A). The EU Listing Act, which is already partially applicable today, will also have an impact on the transaction practice in short notice (see section B). Finally, the legislator has not remained inactive with respect to investment control law - at the European level, the Screening Regulation is set to be replaced and specified by a new regulation (see section C).

A. Artificial intelligence in M&A: new challenges for due diligence and contract drafting

I. The AI Act and its objectives

The regulation providing for harmonized rules on artificial intelligence (AI Act) came into effect on August 1, 2024. The European Union is pursuing two key objectives with the AI Act: First, ensure the safety of AI systems to strengthen public confidence in this technology; second, promote innovation in the field of AI. Certain provisions of the AI Act will be applicable for the first time in 2025: From February 2, the ban on AI posing an unreasonable risk pursuant to Article 5 of the AI Act and the general provisions in Articles 1 to 4, including the obligation for all providers and deployers of AI systems to teach „AI literacy" of their staff apply; on August 2, the rules on general purpose AI models, sanctions and the organization of the AI office as well as the rules for AI systems classified as high-risk in accordance with Annex I of the Regulation come into force.

II. AI Act and M&A

Overall, the integration of AI systems and the associated legal peculiarities and requirements for M&A transactions require a comprehensive legal review and careful contract drafting.

1. AI Act and due diligence

The AI Act has an impact on various areas of due diligence: Compliance with the AI Act is becoming increasingly important for companies - in many cases the AI Act requires companies to self-evaluate their AI systems. Buyers must therefore understand which AI systems the target company uses or develops and how these are classified according to the risk classification of the AI Act. Investments that are necessary to ensure compliance must be assessed, as well as the risks of a delayed adaptation process.

Further, the AI Act also affects the due diligence review of customer and supplier contracts. A key risk of such contracts are the requirements for contractual clauses under Art. 25 of the AI Act: If the target company does not use unambiguous provisions that prevent the applicability of Art. 25 (e.g. a contractual prohibition on converting the developed AI system into a high-risk AI system), this can, in the worst case, lead to a disclosure requirement for sensitive information such as technical documentation or even parts of the source code. Inadequate contract drafting can not only lead to considerable liability risks, but also jeopardize the overall compliance of an AI system. It is therefore advisable to already verify during due diligence stage whether the target company's contracts contain clauses to adequately address information obligations, liability allocations and monitoring requirements under the AI Act.

2. AI Act and M&A contract drafting

Artificial intelligence and the AI Act are also factors to be considered when drafting the transaction documentation. It must be ensured that the intellectual property (IP) in the software, relevant to the AI application and the underlying data, is covered by the subject matter of the transaction. If third party rights exist in this respect, corresponding contractual obligations are required under which the target company or the buyer is either granted rights of use by these third parties or the necessary IP rights are transferred before the closing of the transaction. This applies also to training data used for the development and improvement of the AI systems. It should be noted that training data is generally not protected as intellectual property, meaning that additional agreements are necessary to ensure the protection of this data as trade secrets.

With respect to the contractual warranties and indemnifications, it needs to be ensured that indemnities are included for known risks, e.g., for liabilities resulting from breaches of the AI Act, and that potential unknown risks in connection with AI are adequately covered by the seller's reps & warranties. Specific warranties should, e.g. cover the acquisition of training data in compliance with copyright and data protection law, as well as the AI Act. Compliance warranties should cover both, the compliance of the AI system itself and compliance of the acquired business with the AI Act.

3. Regulatory requirements and obstacles

Finally, regulatory requirements may apply to relevant M&A transactions involving AI aspects: Regulations on the control of foreign direct investment (FDI) must be taken into account if investors based outside the EU or European Free Trade Association (EFTA) wish to acquire a stake of more than 10% of the voting rights in a German AI company, as AI as one of the sectors listed in Section 55a of the Foreign Trade and Payments Ordinance (Außenwirtschaftsverordnung, AWV) is classified as particularly critical. A relevant acquisition of shares is therefore subject to approval. Such approval requirements apply in addition to those of antitrust laws. Compliance with these regulations will impact the structure and timing of the transaction and hence the drafting of the contractual documentation.

B. EU Listing Act entered into force - simplifications in the area of the Prospectus Regulation and the Market Abuse Regulation already partially applicable today

On December 4, 2024, after two years of preparation, the EU Listing Act came into force as a legislative package. The package, consisting of a regulation and two directives, aims to streamline and simplify the rules for stock exchange listings and post-admission obligations to increase the attractiveness and competitiveness of the European capital market. In addition, small and medium-sized enterprises (SMEs) shall have easier access to the capital markets and a framework for multi-voting shares shall be implemented in order to make it more attractive for fast-growing European companies to go public on a European stock exchange.

The legislative package leads to significant changes to the Prospectus Regulation, including an extension of the prospectus exemptions for primary and secondary issues, but also to the Market Abuse Regulation, particularly with regard to the ad hoc obligation. In addition, the Markets in Financial Instruments Regulation and the Markets in Financial Instruments Directive (MiFIR and MiFID II) will be amended and the previously fragmented national regulations on the issue of multi-voting shares will be harmonized for the first time.

Large parts of the legislative package will not be applicable until 2026. However, some provisions amending the Prospectus Regulation, in particular the new prospectus exemptions for certain secondary issuances, already apply today and are therefore briefly described below, as are the amendments to the Market Abuse Regulation, including the changes to the ad hoc obligation that will only apply from June 5, 2026 but are particularly relevant for the legal practice.

I. Significant simplifications in prospectus law

Regulation (EU) 2024/2809 significantly amends the Prospectus Regulation and leads to significant simplifications. In addition to a standardization of the structure and content of prospectuses and the introduction of new prospectus formats, the exemptions from the prospectus requirement for primary and secondary issuances will be substantially expanded.

The new exemptions from the prospectus requirement for certain secondary issuances that already apply today are of significant practical importance. Companies already listed on the stock exchange can now carry out secondary issues of less than 30% of the authorized share capital, calculated over 12 months, without a prospectus if (i) the new shares are (x) fungible with shares already admitted to a regulated market or SME market and (y) also to be admitted to trading on a regulated or SME market and (ii) the issuer is not undergoing restructuring or insolvency proceedings. In these cases, only the publication of a maximum eleven-page document (Annex IX document) and its filing with the competent authority is required; a review or approval of the document is not necessary. Accordingly, the threshold for the approval of securities without a prospectus has been increased from 20% to 30%. Without volume restrictions, secondary issuances are possible without a prospectus with an Annex IX document if the new securities are fungible with securities that have been admitted to trading on a regulated or SME market for at least 18 months without interruption, the issuer is not undergoing restructuring or insolvency proceedings and the securities are not issued in connection with a takeover by way of an exchange offer, merger or demerger. The new exemptions significantly reduce the costs and time required for secondary issuances. However, the preparation of a voluntary prospectus remains possible.

II. Amendment of the Market Abuse Regulation

Regulation (EU) 2024/2809 also amends the Market Abuse Regulation (MAR), even though some of the changes already apply on a national level. For example, the threshold for managers' transactions (Art. 19 MAR) has been raised to EUR 20,000. However, nothing will change for German issuers or their managers, as this threshold has already applied to them since 2020 due to a general ruling by the German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht). The national authorities also have the option of lowering the threshold to EUR 10,000 or increasing it to up to EUR 50,000 (previously EUR 20,000). In addition, the list of exceptions to the trading ban in the closed period was slightly extended. Furthermore, minimum thresholds for sanctions for legal persons for breaches of the provisions in Articles 14 through 20 MAR were introduced, whereby the Member States have until June 5, 2026, to take the necessary transposition measures.

The most relevant change for corporate practice is probably the fact that the ad hoc obligation for intermediate steps in extended circumstances will not apply for around 18 months. In case of extended processes such as M&A transactions, not only the respective final events themselves can constitute insider information, but also intermediate steps (e.g. the conclusion of a letter of intent) if these in themselves fulfill the criteria for insider information. Accordingly, even insider-relevant intermediate steps may not only trigger prohibitions on insider trading and disclosure as well as the obligation to maintain an insider list but may also themselves be subject to the ad hoc disclosure obligation. According to the new version of Art. 17 (1) MAR, insider-relevant intermediate steps should no longer trigger a separate disclosure obligation, but only the respective final event. However, the definition of insider information does not change, meaning that insider-relevant intermediate steps will continue to trigger the corresponding listing obligations and trading and disclosure bans. In addition, confidentiality must also be ensured in the case of intermediate steps that do not require disclosure, and the insider-relevant intermediate step must also be published in exceptional cases before the publication of the final event if confidentiality is no longer guaranteed. A further change, intended merely as a clarification, is provided for in the deferral provision (Art. 17 (4) MAR). The previously abstractly stated requirement that the deferral must not be likely to mislead the public will - in accordance with ESMA's MAR guidelines - be specified to the effect that the inside information must not contradict the last public announcement or any other type of communication by the issuer on the same matter to which the inside information relates.

It is doubtful whether the changes to the ad hoc publicity obligation will actually lead to the intended simplifications for listed companies. Much will depend on the Commission's further clarifications. The EU Listing Act is a step in the right direction towards increasing the competitiveness of Europe and its companies - but nothing more. For real facilitation for listed companies and the raising of capital through the markets, much more far-reaching and comprehensive interventions are needed in the sprawling regulatory jungle to which listed companies in Europe are subject.

C. Harmonization of EU investment control - will the revision of the EU FDI Screening Regulation deliver a breakthrough?

I. Introduction

Investment control has become increasingly important in recent years. The review and approval of company acquisitions - in Germany by the German Federal Ministry of Economics and Climate Protection (Bundesministerium für Wirtschaft und Klimaschutz, BMWK) - are now a regular prerequisite for the execution of transactions. Both German and European investment control laws have been the subject of reforms and reassessments for years. In Germany, based on a key issues paper presented by the BMWK in late summer 2023[1], in particular the consolidation of the investment control regulations, currently primarily governed by the German Foreign Trade and Payments Act (Außenwirtschaftsgesetz) and the associated German Foreign Trade and Payments Ordinance (Außenwirtschaftsverordnung), is being discussed.

The so-called EU Screening Regulation[2] has been in effect at European level since March 19, 2019. On January 24, 2024, the European Commission presented a proposal to reform EU investment control law[3] in response to the results of various evaluations of the EU Screening Regulation, that indicated that a revision of the regulation is necessary in order to better protect the security and public order of the EU and its Member States on the one hand and to ensure that the EU remains an attractive location for foreign investors on

[1] See also M&A Review 1-2/2024, p. 49 ff.

[2] Regulation (EU) 2019/452 of the European Parliament and of the Council of March 19, 2019 establishing a framework for the screening of foreign direct investments into the Union.

[3] Proposal for a Regulation of the European Parliament and of the Council on the screening of foreign investments in the Union and repealing Regulation (EU) 2019/452 of the European Parliament and of the Council, COM (2024) 23 final.

the other. In addition to a modified and expanded scope of investment control, the draft regulation provides in particular for a harmonization of national investment control procedures and a further development of the cooperation mechanism introduced with the EU Screening Regulation, without establishing a uniform EU-wide investment control law.

II. Key aspects of the draft regulation on the revision of the European investment control law

1. Redefinition of the term foreign (direct) investment

Pursuant to the Commission the evaluation of the current EU Screening Regulation has shown that the current scope of the regulation is clearly too narrow. The revision proposal therefore now provides for a broader definition of the term (direct) investment. In future, intra-EU investments, i.e. investments via EU subsidiaries of a non-EU investor, will be explicitly covered by investment control laws if the respective investor financially enables the economic activity of the subsidiary or exercises control over the direct acquirer in any other way. This new regulation is to be understood as a direct reaction to the European Court of Justice's Xella ruling[4], according to which the current version of the EU Screening Regulation does not apply to intra-EU transactions even if the indirect acquirer is a non-EU investor. It is disputed whether the draft regulation also intends to cover so-called greenfield investments. The wording of Art. 2 of the draft suggests that it does, but recital 17 only refers to a recommendation to Member States to include greenfield investments in particularly sensitive sectors in the scope of national investment control laws.

Finally, the draft revision aims to make the sectoral scope of the regulation more precise by defining particularly sensitive areas in greater detail. In any case, the projects and programs of EU interest listed in Annex I of the draft regulation are to be covered, as well as investments in companies operating in the areas listed in Annex II.

2. Expansion of the cooperation mechanism and harmonization of national investment control procedures

Two further, basically interrelated changes are (i) the expansion of the cooperation mechanism and (ii) the harmonization of national investment control procedures:

A central feature of the cooperation mechanism under the EU Screening Regulation is the mutual exchange that exists between the Commission and Member States and/or amongst the Member States. The starting point is usually the notification of a transaction by a Member State – which is (or at least can be) also the problem: Depending on how accurately the Member States assess the relevance of the respective transaction, either a large number of non-critical transactions are reported and/or critical transactions are not reported. The revision proposal addresses this finding by introducing (i) a differentiated notification system that distinguishes between mandatory notifications on the one hand and voluntary notifications on the other, and (ii) a so-called own-initiative procedure that enables the Commission and other Member States to obtain an investment review from the Member State primarily responsible which is accompanied by a so-called „accountability obligation“: The Member State responsible for the investment control procedure shall notify the Commission and the other Member States of its final review decision and elaborate how it has considered the submissions as far as possible in reaching its decision. This extended cooperation mechanism is supplemented by further harmonization of national investment control regimes. For example, and unlike the EU Screening Regulation, the current reform proposal provides for an obligation to adopt an investment control law. In addition, there is to be a mandatory minimum screening area that is in principle subject to national investment controls and - ex ante - subject to approval. With respect to transactions not subject to approval and in order to efficiently enforce the above-mentioned right of initiative, the investment control authorities must be authorized to conduct ex officio investment control proceedings for a period of at least 15 months after the conclusion of the transaction.

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[4] 4 ECJ, EuZW 2023, 810.