

## **Communication No. 2 of the TOB**

### **On the concept of liquidity**

**3 September 2007<sup>1</sup>**

After consultation with the Swiss Federal Banking Commission (now: Swiss Financial Market Supervisory Authority [FINMA]), the Takeover Board has adopted the following communiqué on the concept of the liquidity of an equity security pursuant to Art. 40 para. 4 SESTO-FINMA.

#### **I. CONCEPT OF LIQUIDITY UNDER NEW LEGISLATION**

Under Art. 32 para. 4 SESTA, the offer price must be at least equal to the stock market price of the target company. Art. 40 para. 2 SESTO-FINMA defines the stock market price pursuant to Art. 32 para. 4 SESTA as the volume-weighted average share price of exchange-based trades over the last 60 trading days prior to the publication of the offer or prior announcement. According to paragraph 4 of Art. 37 SESTO-FINMA, an auditor (Art. 25 SESTA) values the listed equity securities if they are not liquid prior to the publication of the offer or prior announcement. Art. 40 para. 4 SESTO-FINMA has thus codified the consistent practice of the Takeover Board which has so far already required such valuation of illiquid listed securities in the context of setting a minimum price. The definition of the concept of liquidity, on the other hand, still remains open. The question of the criteria used to determine whether a security should be described as liquid or illiquid must therefore be answered by the Takeover Board as in the past.

In order to establish legal certainty and transparency in this matter, the Takeover Board has decided to publish the present communiqué to clarify the liquidity concept.

#### **II. CRITERIA FOR DETERMINING THE CONCEPT OF LIQUIDITY**

To date, a security has been liquid if it has been traded on a least 15 days of a period of 30 trading days prior to the publication of the offer or prior announcement. As a result of the "linear" adjustment of this practice to the revised SESTO-FINMA, in future the stock can only be regarded as liquid if it has been traded on at least 30 days out of a period of 60 stock market trading days prior to publication of the offer or prior announcement.

However, the Takeover Board reserves the right to consider not only this criterion, should circumstances so justify. In particular, the Takeover Board is considering also taking account of volumes traded during the reference period.

#### **III. SPORADIC LIQUIDITY**

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<sup>1</sup> The Communication has been adapted to the new legal bases which entered into force as from 1 January 2009. With regards to contents, no alterations have been made



According to Art. 40 para. 4 SESTO-FINMA, the time of publication of the offer or prior announcement is the decisive factor in assessing whether a security is liquid or not. This means that the liquidity of a security should be assessed in the context of a specific offer. On the basis of the concept of liquidity used by the Takeover Board (II. above), it is possible for a security to be at times liquid and at times illiquid. In the case of a voluntary offer - and to a lesser extent also in the case of a mandatory offer during the two-month period pursuant to Art. 37 SESTO-FINMA - the offeror has some room for manoeuvre in that the publication of the offer or prior announcement can be timed according to the liquidity or illiquidity of the security in question.

If the market for a security is irregular and of limited volume and the security therefore is not very liquid or is even illiquid, it is relatively simple to trade a minimum volume of the security in question during the reference period in order to meet the Takeover Board's liquidity criteria. However, in some cases, the Takeover Board could construe such influencing of the market as an attempt to circumvent the rules, which would in particular infringe the principle of fairness applicable to public takeover offers (Art. 28 lit. c SESTA and Art. 1 TOO).

While bringing about a state of liquidity is quite a simple matter, bringing about a state of illiquidity is not. It requires not only the offeror and those acting in concert with that party to refrain from action, but also requires all other market participants to do likewise. The latter would practically have to refrain from placing any buy or sell orders during the reference period, or would at least have to restrict their trading activity in the securities in question sufficiently to enable the number of transactions to fall below the minimum threshold. However, there would appear to be little prospect of bringing about such a state of affairs in a free, regulated and supervised market. Logic therefore dictates that publishing a prior announcement or an offer at a time when the security is illiquid does not in principle conflict with the provisions of takeover legislation.