Antimonopoly Law Considerations and Risk Management in Connection with M&A Transactions - Assessing Competition Risks in Acquisitions

Philippe Rincazaux

Partner, Paris

ORRICK
RAMBAUD MARTEL

Introduction

- Allocation of antitrust risk is an issue that frequently arises between parties in mergers or acquisitions that raise potential antitrust concerns.
- Motivations of the **buyer** and the **seller** are the same:
  - the **buyer** wants to minimize seller interference with:
    (i) a timetable; and
    (ii) decision to offer remedies.
  - the **seller** wants to ensure that:
    (i) deal can be done as soon as possible; and
    (ii) remedies are provided in accordance.
- Antitrust lawyers play an essential role in the transaction process. They should:
  - advise the client on substantive antitrust issues raised by a proposed concentration;
  - prepare required antitrust notifications; and
  - obtain the requisite antitrust approval.

ORRICK
RAMBAUD MARTEL

Outline

I. Preliminary phase: Risk assessment of the transaction

II. Transitional phase

III. Post-closing phase

I. PRELIMINARY PHASE:
RISK ASSESSMENT OF THE TRANSACTION

I. (i) (Preliminary) Merger filing analysis

- **Question:** Is the transaction a « **concentration** » under relevant merger law?
  - **Concentration:** acquisitions of direct or indirect control of the whole or part of one or more undertakings.
  - « **Sole** » or « **joint** » control.
  - Preliminary identification of the countries where the transaction should be notified on the basis of data available at this stage.

I. (i) (Preliminary) Merger filing analysis - Antitrust due diligence analysis

ORRICK
RAMBAUD MARTEL

1. Lawyers must:
   - advise on the jurisdictions where antitrust filing may be required (European Union) or appropriate (United Kingdom);
   - gather the necessary information (parties' market shares or turnover, market studies) to complete Form CO; and
   - identify the potential antitrust issues.
2. Legal and business review of the businesses to be acquired.

I. (i) (Preliminary) Merger filing analysis - Multifiling

- In multi-jurisdictional deals, the parties might identify the specific approvals that need to be obtained as a condition to closing.
- In that regard, special care must be given by the parties to:
  - the internal (lawyers) and external (local counsel) costs;
  - the impact of the operations on the timetable;
  - the exposure of the undertaking involved with competition authorities (past infringements, ongoing investigation, etc.); and
  - the sanctions applicable in respect to filing violations.

I. (i) (Preliminary) Merger filing analysis - Sanctions for not filing

ORRICK
RAMBAUD MARTEL

- Today, most of competition authorities provide for financial penalties as a sanction for not filing:

1. The **Merger Regulation** provides the Commission with powers to impose fines of up to **10%** of aggregate worldwide turnover on the parties if they intentionally or negligently fail to notify a merger with Union dimension.

   In 2009, the Commission imposed a fine of €20 million on Electrabel for acquiring control of Compagnie National du Rhône without having notified and received prior approval for the acquisition.

2. In **Russia**, a failure to submit a required pre-completion or post-completion filing can be penalized by fines on legal entities and on managers.

I. (i) (Preliminary) Merger filing analysis
- Overview of the European Merger Regime

ORRICK
RAMBAUD MARTEL

- **Legal Base:** Council Regulation (CE) n°139/2004 (« **Merger Regulation** »).

1. Notification: mandatory for all concentrations with a Community dimension
   + concentrations shall not be implemented before clearance.
2. Phase I (**Initial examination**): detailed appraisal via request for information, interviews, etc.
3. Decision: i) does not fall within the scope of the Merger Regulation;
   ii) approval; or iii) serious doubts.
4. Phase II (**Initiation of proceedings**)
5. Final decision:
   - Final Phase I decision: within **25** working days of formal notification.
   - Final Phase II decision: within **90** working days following initiation of Phase II proceedings (extra time given in event of commitments / “stop the clock”).
   - Possibility of review by the **European General Court** within **2 months** from the date of the decision.

I. (i) (Preliminary) Merger filing analysis
- Overview of the European Merger Regime

A transaction that is not notifiable under the Merger Regulation may nonetheless be subject to notification under Member State laws.

- A transaction may be referred to the Commission by Member States or the parties' request (**Articles 22** and **4.5** of the Merger Regulation).
- Conversely, a concentration with a Community dimension may be referred in whole or in part by the Commission to one or more Member States at the request of the parties or the Member States (**Articles 9** and **4.4** of the Merger Regulation).

The risk of delay and legal uncertainty involved in such referrals may outweigh any perceived advantages in deliberately structuring a transaction to fall inside or outside the scope of the Merger Regulation.

I. (i) (Preliminary) Merger filing analysis (cont'd)

ORRICK
RAMBAUD MARTEL

When to notify?

- **EU + US systems:** notification may be made where the undertaking concerned demonstrates a **good faith intention** to conclude an agreement.
  - such a good faith intention can be demonstrated by a **Letter of Intent** signed for all undertakings concerned.

→ The sooner, the better?

- Even if the parties choose not to notify on the basis of the Letter of Intent, information should be collected to determine where filings are required or appropriate.

I. (ii) Antitrust issues
- Evaluation of the situation

ORRICK
RAMBAUD MARTEL

Preliminary questions

1. Asking questions about the affected market, such as:
   - are the products involved homogeneous?
   - is the market concentrated?
   - how high are barriers to entry/expansion?

➡ Anticompetitive arrangements are most likely on highly concentrated markets.

2. Asking questions about the likelihood of an antitrust investigation, such as:
   - are the parties in the transaction strong and uniquely close competitors with one another?
   - are the prices likely to increase?
   - has the industry, where the target is active, already been subject to investigations?

3. Asking question about the target, such as:
   - has the buyer already been subject to a cartel proceedings?

I. (ii) Antitrust issues
- Dealing with confidential information

ORRICK
RAMBAUD MARTEL

<u>“Confidentiality” or “Non-Disclosure” agreement</u>

- In order to identify the key issues to be addressed as well as ensure the success of the concentration, the seller in a potential transaction should disclose non-public information to the potential buyer.
- Why?
  - assessment of the desirability of the transaction.
  - identification of the key issues in the definitive agreement.
  - assessment of the antitrust risks.
  - ensure the successful implementation of the transaction.
- **The more sensitive the information, the more valuable it may be to the receiving party.**

I. (ii) Antitrust issues
- Dealing with confidential information (cont'd)

Risk of the disclosure: Exchange of information

If the buyer and seller are competitors, information exchange has the potential of raising competition law concerns.

- Information concerning current **customers** or **price** is highly sensitive.
- If the parties disclose confidential information without entering into a Confidentiality Agreement or do not respect such agreement, competition law (**Article 101** Treaty on the Functioning of the European Union (TFEU)) issues may arise.

Solutions: disclosing information only in aggregated form and/or disclosing such information only to counsel, accountants or business consultants who agree not to disclose such information to the receiving party (« **clean team** »).

Best practices for risk assessment of the transaction

ORRICK RAMBAUD MARTEL

<u>Conclusion on the preliminary phase – risk assessment</u>

- **Buyers** should:
  - ask the right questions;
  - assess the risks;
  - negotiate contractual safeguards; and
  - agree to strategies.
- **Sellers** should:
  - consider whether to conduct an antitrust audit before a sales process to understand the potential risks and mitigate any potential liability before the sale; and
  - put in place contractual protections to ensure that any indemnities agreed that relate to past conduct are appropriately capped, given the potentially heavy financial exposure ahead.

II. THE TRANSITIONAL PHASE

II. (i) Notification preparation

- A **Purchase Agreement** is typically the first document entered into the deal process triggering a notification obligation.
- **Best practice:** parties should contact the relevant competition authorities to discuss the filing process and submit a draft notification.
- Parties should implement their communication plan for the transaction, in particular with respect to customers and suppliers who may be contacted by the competition authorities during an investigation.

In many jurisdictions, merger control rules prohibit the implementation of notifiable transactions before regulatory approval has been granted.

II. (i) Notification preparation

Antitrust approvals clause in the Purchase Agreement

- Once the notification is made, the Purchase Agreement typically imposes an obligation for the buyer to attempt to obtain antitrust approvals.
- **May be very sensitive: transaction may be prohibited or remedies will be required.**
- The Purchase Agreement should retain a reasonable delay to notify.
- The Purchase Agreement may prohibit other acquisitions that could make it more difficult to obtain antitrust approvals.

ORRICK
RAMBAUD MARTEL

II. (ii) Antitrust approval risks

- Under the Merger Regulation, a notifiable transaction may not be put into effect until it has been approved.

  1. Drop-dead date:
     it must be established taking account of the time to obtain required antitrust approvals, including possible delays.

  2. Break-up fee provision:
     it may allocate antitrust approval risk to the buyer by providing a payment requirement to the seller in the event that the deal is not closed because required antitrust approvals are not obtained.

  3. Indemnification provision:
     it may be used to allocate antitrust risks.

ORRICK
RAMBAUD MARTEL

II. (iii) Antitrust related warranties

- The seller’s warranties may contain express promises regarding the absence or extent of antitrust liabilities.
- The seller may be obligated to declare whether or not it is party to any type of agreement with potential antitrust implications.
  - ➢ seller may attempt to negotiate provisions in a Purchase Agreement to the effect that no fact or circumstance disclosed to the buyer in due diligence will be deemed to violate the seller’s warranties.

Difficult issues may arise where the buyer’s due diligence has uncovered evidence of potential antitrust violations that have not yet resulted in litigation.
→ Inclusion of specific references to such potential violations may increase the risk that litigation will result.

III. THE POST-CLOSING PHASE

III. (i) Ancillary agreements

- The parties may enter into agreements affecting their commercial behavior. If they qualify as « **ancillary restraints** », they will be covered by the decision, clearing the transaction.

1. Non-competition clauses: limited non-competition clauses, binding on the seller, are recognized as essential to permit the buyer to obtain the full value of the transferred business.

   They must be limited:

   - to the geographical scope of the seller's activities prior to the transfer;
   - to the products or rights of the transferred business; and
   - in their duration (generally three years max).

2. Commercial agreements: a purchase or supply agreement may qualify as « ancillary restraint » provided that they do not exceed the purpose of allowing the break-up of the seller's economic activities.

- Non-ancillary agreements are potentially subject to review under **Articles 101** (cartel) and **102** TFEU (abuse of a dominant position).

III. (ii) Cartel detection - Successor liability

1. If the undertaking that was responsible for the business still exists, it remains liable for the infringement rather than the acquirer. As long as this legal person exists, responsibility for the infringement remains with this legal person even if the assets and personnel that contributed to the infringement have been transferred to third parties.

2. The liability may pass to a successor:

   - where the corporate entity which committed the infringement has ceased to exist in law after the infringement was committed. In such cases, the buyer that has acquired the physical and human assets responsible for the infringement will be held liable due to the economic continuity existing between the former target and the acquiring company; or
   - where the initial participant in the cartel still has a legal existence but no longer carries out economic activity on the relevant market and where there are structural links between the initial entity and the new operator of the undertaking.

III. (ii) Cartel detection
- Successor liability (cont'd)

Any transfer of liability envisaged under the terms of the contract of sale and purchase has **no bearing on the determination of the undertaking's liability** by the Commission.

It can only affect the internal relationship and provide a company with the right to seek redress against the other entity.

ORRICK
RAMBAUD MARTEL

III. (iv) Fines

- Fines of up to 10% of their worldwide turnover may be imposed on the parties.
- In its assessment of gravity, the Commission takes account of the effective economic capacity of the offenders to cause significant damage to other operators.

  In the Carbonless Paper decision, Bolloré's starting fine was increased by 100% for deterrence to take its size and resources into account.
- Largest fines imposed by the Commission:
  - **Saint Gobain:** €896 million (2008)
  - **E.ON jointly and severally with E.ON Ruhrgas:** €553 million (2009)
  - **GDF Suez:** €553 million (2009)

III. (v) Cartel detection - Leniency

- In any transaction, both the acquirer and the seller bear the risk of being fined for past anticompetitive behavior of the target.
- In this case, parties have two choices:
  - end the illegal conduct; or
  - blow the whistle (only the first applicant to the Commission will benefit from full immunity of fines).
- If the seller still exists, the only way not to be held responsible is to stop the illegal **behavior of the target promptly after the acquisition**. If the seller ceases to exist, the buyer is potentially exposed to the risk of liability (continuing + past infringements).

⇨ **Importance of leniency of application.**

- The seller might also be held responsible for his past conduct.

⇨ Difficulties to provide the Commission with information that adds value (no longer access to employees and documents).

ORRICK
RAMBAUD MARTEL

Thank you

Philippe Rincazaux
Partner, M&A and Private Equity; Competition Law
ORRICK RAMBAUD MARTEL SOCIETE D'AVOCATS
princazaux@orrick.com
+331 5353 7557