Private M&A

Contributing editors
Will Pearce and John Bick

2018

© Law Business Research 2017

Private M&A 2018

Contributing editors

Will Pearce and John Bick

Davis Polk & Wardwell LLP

Publisher
Gideon Roberton
gideon.roberton@lbresearch.com

Subscriptions
Sophie Pallier
subscriptions@gettingthedealthrough.com

Senior business development managers
Alan Lee
alan.lee@gettingthedealthrough.com

Adam Sargent
adam.sargent@gettingthedealthrough.com

Dan White
dan.white@gettingthedealthrough.com

Published by
Law Business Research Ltd
87 Lancaster Road
London, W11 1QQ, UK
Tel: +44 20 3708 4199
Fax: +44 20 7229 6910

© Law Business Research Ltd 2017
No photocopying without a CLA licence.
First published 2017
First edition
ISSN 2515-3781

The information provided in this publication is general and may not apply in a specific situation. Legal advice should always be sought before taking any legal action based on the information provided. This information is not intended to create, nor does receipt of it constitute, a lawyer–client relationship. The publishers and authors accept no responsibility for any acts or omissions contained herein. The information provided was verified between August and October 2017. Be advised that this is a developing area.

Printed and distributed by
Encompass Print Solutions
Tel: 0844 2480 112

© Law Business Research 2017

CONTENTS

Comparing UK and US acquisition agreements 7
Will Pearce and William Tong
Davis Polk & Wardwell London LLP

Price mechanisms: seller versus buyer considerations 11
Amit Abhyankar and Hinesh Desai
PricewaterhouseCoopers LLP

The use of W&I insurance in private M&A transactions 14
Lorraine Lloyd-Thomas
Marsh Ltd

Australia 17
Michael Wallin, Jessica Perry and Roberta Foster
MinterEllison

Austria 23
Florian Kusznier
Schoenherr Rechtsanwaelte GmbH

Belgium 29
Dries Hommez and Laurens D'Hoore
Stibbe

Canada 36
John Mercury, James McClary, Bryan Haynes, Ian Michael, Kristopher Hanc and Drew Broughton
Bennett Jones LLP

China 42
Jie Lan and Jiangshan (Jackson) Tang
Haiwen & Partners
Howard Zhang
Davis Polk & Wardwell LLP

Denmark 48
Anders Ørjan Jensen and Charlotte Thorsen
Gorrissen Federspiel

Finland 53
Sten Olsson and Johannes Husa
Hannes Snellman Attorneys Ltd

France 59
Christophe Perchet, Juliette Loget and Jean-Christophe Devouge
Davis Polk & Wardwell LLP

Germany 65
Alexander Schwarz and Ralf Morshäuser
Gleiss Lutz

Hong Kong 71
Paul Chow and Yang Chu
Davis Polk & Wardwell

India 79
Iqbal Khan and Abhinav Bhalaik
Shardul Amarchand Mangaldas & Co

Ireland 89
Paul Robinson and Conor McCarthy
Arthur Cox

Italy 96
Filippo Troisi and Francesco Florio
Legance – Avvocati Associati

Japan 103
Kayo Takigawa and Yushi Hegawa
Nagashima Ohno & Tsunematsu

Korea 109
Gene-Oh (Gene) Kim and Joon B Kim
Kim & Chang

Luxembourg 116
Gérald Origer, Claire-Marie Darnand and Michaël Meylan
Stibbe

Mexico 122
Ricardo Garcia Giorgana
Galicia Abogados, SC

Netherlands 128
Hans Witteveen and Julie-Anne Siegers
Stibbe

Norway 135
Ole Kristian Aabø-Evensen
Aabø-Evensen & Co Advokatfirma

Poland 145
Joanna Wajdzik, Anna Nowodworska and Damian Majda
Wolf Theiss

Portugal 152
Francisco Santos Costa
Cuatrecasas

Serbia 159
Nenad Stankovic, Sara Pendjer, Tijana Kovacevic and Dusan Djordjevic
Stankovic & Partners

South Africa 165
Charles Douglas and Sibonelo Mdluli
Bowmans

Spain 171
Federico Roig García-Bernalt and Francisco J Martínez Maroto
Cuatrecasas

Sweden 178
Peter Sundgren and Matthias Pannier
Advokatfirman Vinge KB

© Law Business Research 2017

Switzerland 184
Claude Lambert and Reto Heuberger
Homburger AG

Turkey 190
Noyan Turunç, Kerem Turunç, Esin Çamlıbel, Grace Maral Burnett, Didem Bengisu and Nilay Enkür
TURUNÇ

United Kingdom 196
Will Pearce, Simon J Little and William Tong
Davis Polk & Wardwell London LLP

United States 203
Harold Birnbaum, Lee Hochbaum and Brian Wolfe
Davis Polk & Wardwell LLP

© Law Business Research 2017

United Kingdom

Will Pearce, Simon J Little and William Tong
Davis Polk & Wardwell London LLP

Structure and process, legal regulation and consents

1 How are acquisitions and disposals of privately owned companies, businesses or assets structured in your jurisdiction? What might a typical transaction process involve and how long does it usually take?

Typically, a contract, referred to as a sale and purchase agreement, is executed between the relevant parties to acquire or dispose of privately owned companies, businesses or assets. Privately owned companies can also be acquired by 'contractual offer' followed by a minority squeeze-out, provided that the offer is made in accordance with Part 28 of the UK Companies Act 2006 (CA 2006), or by a 'scheme of arrangement' proposed by the company to be acquired in accordance with Part 26 of the CA 2006.

The process of acquiring a company, business or assets will often turn on the complexity of issues and the number of parties involved, as well as whether the transaction involves a bilateral negotiation or a controlled auction process with multiple potential buyers.

An auction process in which interest from several buyers is solicited will typically involve:
- drafting an information memorandum as the basis of marketing the company, business or assets, completion of vendor due diligence and drafting of a sale and purchase agreement and other sale documents (approximately six to eight weeks);
- 'round one' expressions of interest from potential buyers who will then be permitted to undertake due diligence (approximately four weeks);
- 'round two' offers by potential buyers with mark-ups of the transaction documentation (approximately four weeks); and
- negotiation of transaction documentation with one or more buyers until definitive terms are agreed with one party (up to two weeks).

The larger and more international the target company, business or assets, the longer each phase of a process can take. Up to three months will often elapse between the distribution of an information memorandum and the execution of definitive transaction documents. A bilateral transaction can take longer to complete owing to the lack of competitive tension in the process.

2 Which laws regulate private acquisitions and disposals in your jurisdiction? Must the acquisition of shares in a company, a business or assets be governed by local law?

The CA 2006 sets out the regulatory framework for English limited liability companies. There are a range of statutes and regulations dealing with the transfer of employees, title to property, data protection, pensions and competition that are relevant to private acquisitions and disposals.

Although most sales of English companies will be governed by English law, it is possible for acquisitions to be governed by the law of an overseas jurisdiction. However, legal formalities applicable to the transfer of shares and assets and liabilities that are subject to local law will have to be complied with.

3 What legal title to shares in a company, a business or assets does a buyer acquire? Is this legal title prescribed by law or can the level of assurance be negotiated by a buyer? Does legal title to shares in a company, a business or assets transfer automatically by operation of law? Is there a difference between legal and beneficial title?

Under the Law of Property (Miscellaneous Provisions) Act 1994, shares of an English company or assets located in England and Wales can be acquired with 'full title guarantee' or 'limited title guarantee' (referred to as title covenants). Subject to certain additional covenants that apply in respect of real property, a sale with full title guarantee means:
- the seller has the right to sell the property;
- the seller will (at its own cost) make reasonable efforts to give the buyer the property that is promised; and
- the property is free from charges, encumbrances and third-party rights expect those that the seller does not and could not reasonably be expected to know.

Limited title guarantee is the same except that the property is considered to be free from encumbrances from the time of the last sale for value.

Title covenants will not be implied if transaction documentation makes no reference to them. However, a buyer may be unwilling to accept the reasonableness and knowledge qualifications included in implied title covenants and prefer to negotiate unqualified title to shares or assets.

Title to shares in a company incorporated under the CA 2006 transfers upon the company's register of members being updated to reflect the buyer as the registered holder of the shares following receipt by the company of an instrument of transfer duly executed by the seller (and the buyer, if the nominal value of each share has not been paid in full). The transfer of title to assets subject to English law may require notifications to be given, consents from third parties to be obtained and registrations to be made.

Legal and beneficial title are distinct interests in property. A person registered as holding the legal title to a share in a company incorporated under the CA 2006 may be a nominee with a different party having the right to receive the economic benefits of the share. Accordingly, the beneficial interest can be transferred without having to update the register of members of the company. Interests in other assets, such as real estate, can be held in the same way.

4 Specifically in relation to the acquisition or disposal of shares in a company, where there are multiple sellers, must everyone agree to sell for the buyer to acquire all shares? If not, how can minority sellers that refuse to sell be squeezed out or dragged along by a buyer?

Typically a buyer will prefer all sellers to sign the transaction documentation and agree to be bound by the same.

Minority shareholders may, however, be required to sell their shares pursuant to 'drag-along' provisions contained in a company's articles of association or in a shareholders' agreement requiring the transfer of title to their shares if specified conditions are satisfied.

Further, if a private acquisition is structured as a contractual offer under the CA 2006, the buyer can compulsorily acquire minority shareholders who have not accepted the offer once the buyer has acquired

© Law Business Research 2017

at least 90 per cent in value and 90 per cent of the voting rights carried by the shares to which the offer relates. If structured as a scheme of arrangement, a scheme binds all minority shareholders provided a majority in number representing 75 per cent in value of those shareholders attending and voting approve an arrangement that is sanctioned by the English Companies Court.

5 Specifically in relation to the acquisition or disposal of a business, are there any assets or liabilities that cannot be excluded from the transaction by agreement between the parties? Are there any consents commonly required to be obtained or notifications to be made in order to effect the transfer of assets or liabilities in a business transfer?

As a matter of English contract law, a buyer can generally choose which assets or liabilities it wishes to acquire in a transaction that is structured as a business or asset sale.

However, a buyer cannot structure a transaction as a business or asset sale with a view to avoiding responsibilities to employees engaged in the target business. The Transfer of Undertakings (Protection of Employment) Regulations 2006 (as amended) (TUPE) apply to the acquisition of a business in the UK, and require that contracts of employment are automatically transferred to the buyer of a business and that employee benefits must be honoured. There are very few exceptions to TUPE, and attempts to exclude its application will be void.

A transfer of assets or liabilities may require customary third-party consents: for example, a landlord's consent to the assignment of a lease or a counterparty's consent to the assignment or novation of a contract (see question 7).

6 Are there any legal, regulatory or governmental restrictions on the transfer of shares in a company, a business or assets in your jurisdiction? Do transactions in particular industries require consent from specific regulators or a governmental body? Are transactions commonly subject to any public or national interest considerations?

Selling shareholders may be subject to 'pre-emptive' and 'tag-along' rights. Pre-emptive rights require a shareholder to offer their shares for sale to other shareholders before they can be sold to a third party. Such rights may take the form of a right of first offer, whereby the selling shareholder must negotiate a sale with the other shareholders before approaching third parties, or a right of first refusal, whereby the selling shareholder must give the other shareholders the right to match the terms of a sale that has been negotiated with a third party. Tag-along rights restrict the ability of a selling shareholder to transfer his or her shares in a transaction that excludes other shareholders.

Acquisitions of companies and businesses in the UK are subject to the merger control regime set out in the UK Enterprise Act 2002, pursuant to which the UK Competition and Markets Authority (CMA) may investigate transactions that satisfy certain jurisdictional thresholds, either upon receipt of a notification from the parties or on its own initiative. The UK Enterprise Act 2002 provides two jurisdictional thresholds:

- a 'share of supply' test, which is satisfied when a transaction creates or enhances a 25 per cent share of supply or purchases of any goods or services in the UK (or in a substantial part of it) (this is not a market share test, and the CMA has a wide discretion in describing the relevant goods or services); and
- a 'turnover test', which is satisfied when the enterprise over which control is acquired has generated turnover in the UK in the preceding fiscal year exceeding £70 million.

Notification of a transaction to the CMA is voluntary. However, in practice, a large number of transactions are notified to give parties legal certainty, since the CMA may commence an investigation on its own initiative and subsequently refer a transaction to a 'Phase 2' review.

The CMA has a duty to refer transactions for a Phase 2 review where it believes there is, or may be, a relevant merger situation that has resulted in or may be expected to result in a substantial lessening of competition in the UK. If a transaction is subject to a Phase 2 review, without the CMA's consent, parties to a completed merger are prohibited from undertaking further integration, and parties to an anticipated merger are prohibited from acquiring an interest in shares in each other. The CMA also has power to accept undertakings or make orders preventing parties from taking an action that might prejudice the outcome of a Phase 2 reference.

In addition, a mandatory notification to the European Commission is required in respect of transactions meeting the turnover thresholds set out in the EU Merger Regulation.

The UK does not subject the acquisition of companies, businesses or assets to general national industry considerations, although the Secretary of State has the power:

- under the UK Enterprise Act 2002 to intervene in transactions giving rise to public interest concerns relating to national security, media quality, plurality and standards and financial stability; and
- under the Industry Act 1975 to prohibit the acquisition by an overseas person of an important manufacturing undertaking if it would be contrary to the interests of the United Kingdom (although, to date, this power has not been exercised).

7 Are any other third-party consents commonly required?

The need to obtain a third-party consent will turn on the law governing the transfer of the relevant assets and liabilities. With respect to assets and liabilities governed by English law to be transferred in connection with the acquisition of a business, the agreement of the counterparties to contractual arrangements will be required to transfer obligations of the seller to the buyer and the assignment of the benefits of contractual arrangements may be subject to counterparty consent.

The consent of landlords to transfer English leasehold property and the consent or waiver of rights of lenders to transfer English law-governed loans is ordinarily required in connection with the acquisition of a company, business or assets. Where security has been granted pursuant to English law over the assets of a company or business, releases and non-crystallisation certificates will normally be required.

Where certain assets to be transferred are required to be registered under English law, the transfer of ownership will only be completed once the relevant register is updated.

8 Must regulatory filings be made or registration fees paid to acquire shares in a company, a business or assets in your jurisdiction?

Where shares in an English company are to be transferred, the new holder of the shares will not be entered in the register of members of the company (see question 3) until all stamp duty has been paid (see question 31).

Where certain assets to be transferred are required to be registered under English law (see question 7), registration may not be completed by the relevant authority until the relevant registration or filing fees have been paid. These fees are generally of a nominal amount.

Advisers, negotiation and documentation

9 In addition to external lawyers, which advisers might a buyer or a seller customarily appoint to assist with a transaction? Are there any typical terms of appointment of such advisers?

Parties will typically appoint a financial adviser and accountants to assist with a transaction. The financial adviser will provide strategic and valuation advice, and the accountants will assist with accounting matters, financial and tax diligence and tax structure. Strategy and business consultants may also be engaged to conduct commercial due diligence. If a party to a transaction has securities listed on a stock exchange, public relations advisers are often appointed to coordinate announcements that may have to be made to the public market.

Most professional advisers have standard terms of engagement that they will agree with the buyer or seller, as the case may be. The level of fees will typically depend on the monetary value of the deal, the complexity of the issues, the timetable for the transaction and the nature of any required work product. In aggregate, a buyer's financial, accounting and legal advisory fees may amount to several percentage points of the monetary value of the deal.

10 Is there a duty to negotiate in good faith? Are the parties subject to any other duties when negotiating a transaction?

English contract law does not impose a general duty to negotiate in good faith, so parties to a transaction are permitted to pursue their own

© Law Business Research 2017

self-interest. It is, however, possible for parties to impose an obligation to act in good faith, for example, pursuant to binding heads of terms.

While there is no general duty to act in good faith, directors of a UK company are subject to fiduciary and statutory duties that include the duty to act in a way that such director considers, in good faith, promotes the success of the company for the benefit of its members as a whole, and financial advisers are subject to certain standards of professional conduct monitored by the UK Financial Conduct Authority.

11 What documentation do buyers and sellers customarily enter into when acquiring shares or a business or assets? Are there differences between the documents used for acquiring shares as opposed to a business or assets?

When acquiring shares, a business or assets, parties to a transaction will customarily enter into:

- a confidentiality agreement governing the exchange of confidential information relating to the transaction;
- a sale and purchase agreement setting out the terms of the transaction, which will be substantially similar whether shares, a business or assets are being acquired except that in respect of a business or asset acquisition there will be detailed provisions defining the scope of the assets and liabilities that are to be transferred to the buyer, and mechanisms (a 'wrong pockets' clause) to address the misallocation of assets and liabilities between the seller and buyer;
- a disclosure letter in which general and specific disclosures are made by the seller qualifying the warranties included in the sale and purchase agreement;
- a transitional services agreement specifying the basis upon which the seller will ensure the continued provision of certain services to the target company or business by the seller or its affiliates following completion of the transaction; and
- documents to transfer or register title to assets that, in respect of the acquisition of shares in a UK company, will consist of a stock transfer form and, in respect of the acquisition of a business or assets, will consist of notifications to update registers of, for example, real property and intellectual property.

In addition:

- a buyer will often deliver one or more offer letters to a seller expressing its interest in the transaction and the terms, including the price, upon which it would be willing to proceed;
- in a bilateral transaction, the parties may negotiate heads of terms in an attempt to ensure that resources are not wasted evaluating a transaction before key terms are agreed; and
- key members of management in the target business may enter into new employment agreements to secure their continued employment following completion of the transaction.

12 Are there formalities for executing documents? Are digital signatures enforceable?

English law draws a distinction between the execution of simple contracts and the execution of deeds. Certain documents must be executed as deeds, including transfers of interests in land, mortgages and charges and powers of attorney. The failure to observe any applicable formalities for execution could cause a document to be invalid and unenforceable.

Simple contracts require the signature of a suitably authorised person to be effective. Additional formalities must be observed for the execution of deeds, which include, in respect of execution by a natural person, execution in the presence of a witness and, in respect of execution by a company incorporated under the CA 2006, execution by two directors, a director and a company secretary, or a director, in the presence of a witness. It is best practice to be able to demonstrate that execution occurred when the relevant document had been finalised and fully assembled, either physically or electronically, in accordance with guidance issued by the Law Society of England and Wales ('Execution of documents by virtual means').

Electronic signatures are enforceable pursuant to the EU eIDAS Regulation (910/2014/EC), although wet-ink original documents are normally required, for example, by HM Revenue and Customs, where documents are submitted because stamp duty applies. The Law Society of England and Wales has issued guidance regarding the use of electronic signatures ('Execution of a document using an electronic signature').

Due diligence and disclosure

13 What is the typical scope of due diligence in your jurisdiction? Do sellers usually provide due diligence reports to prospective buyers? Can buyers usually rely on due diligence reports produced for the seller?

Due diligence provides potential buyers with the opportunity to evaluate the legal, financial, tax and commercial position of a company, business or assets. Legal due diligence will typically confirm title to the company or business, the legal structure, terms of financial obligations, ownership and use of information technology, intellectual and real property, physical assets, employee arrangements, litigation and compliance with law.

Vendor due diligence reports are a common feature of controlled sales processes in the UK, enabling a seller to accelerate the sale process, minimise disruption to the target business and access to management, and explain any complexities associated with the transaction. It is customary for a successful buyer, and its lenders, to be able to rely on certain of such vendor due diligence reports, although buyers will often also complete confirmatory due diligence to complete their evaluation of a transaction.

14 Can a seller be liable for pre-contractual or misleading statements? Can any such liability be excluded by agreement between the parties?

A seller can be liable for pre-contractual misrepresentations although, except with respect to fraudulent misrepresentations, sale and purchase agreements usually limit a seller's liability to claims for breach of contract and exclude liability for pre-contractual and misleading statements.

15 What information is publicly available on private companies and their assets? What searches of such information might a buyer customarily carry out before entering into an agreement?

English companies are required to make extensive filings with the Registrar of Companies that are made publicly available online, including:

- the company's articles of association;
- audited financial statements;
- details of the board of directors and people with significant control over the company;
- special shareholder resolutions (requiring approval by at least 75 per cent of participating shareholders);
- details of changes to the company's share capital;
- mortgages over the company's assets; and
- an annual confirmation statement confirming that all required information has been delivered to the Registrar of Companies.

Details of the ownership of real property, mortgages and charges and other attributes of real property are available at Her Majesty's Land Register and through local authorities responsible for the area in which the real property is located. Details of registered intellectual property, such as patents and trademarks, can be obtained from the UK Intellectual Property Office.

A buyer of a company will typically carry out a search of the information filed with the Registrar of Companies and confirm with the Companies Court that a winding-up petition has not been lodged in respect of the company. Searches may also be performed in respect of those registered assets that are regarded as being material to a transaction. Nominal fees are generally payable to carry out such searches.

16 What impact might a buyer's actual or deemed knowledge have on claims it may seek to bring against a seller relating to a transaction?

A buyer's knowledge at the time of entering into an acquisition will preclude a claim for breach of implied title covenant (see question 3). Otherwise, if a buyer is not explicitly precluded by the sale and purchase agreement from claiming in respect of matters about which it

© Law Business Research 2017

has knowledge at the time of entering into the agreement, then a claim would not be expected to be automatically excluded.

However, it is arguable that if a buyer has actual knowledge of a matter at the time of entering into a sale and purchase agreement, a claim cannot be preserved through a specific contractual provision. Accordingly, a sale and purchase agreement would usually specify whether a buyer's actual, constructive or imputed knowledge will qualify the seller's warranties.

Pricing, consideration and financing

17 How is pricing customarily determined? Is the use of closing accounts or a locked-box structure more common?

Closing accounts and locked boxes are commonly used to determine pricing. Auctions of companies, particularly conducted by private equity funds, typically use locked-box pricing, as this forces a buyer to diligence the accounts before agreeing the deal and provide greater certainty for the seller on an exit. Closing accounts may prove more suitable where a company or business is being carved out from the seller's group.

18 What form does consideration normally take? Is there any overriding obligation to pay multiple sellers the same consideration?

Cash is the most common form of consideration in private M&A transactions. Other forms of consideration are principally driven by the tax position of the seller, who may defer a capital charge by receiving securities.

There is no obligation to pay multiple sellers the same consideration in respect of an acquisition by way of a sale and purchase agreement. However, if the transaction is structured as a contractual offer, the same consideration must be paid to all shareholders in order for the buyer to avail itself of the statutory squeeze-out mechanism. If shareholders are offered different consideration in connection with a transaction structured as a scheme of arrangement they will comprise different classes, with each class participating in the scheme of arrangement having the opportunity to approve the proposal made to them.

19 Are earn-outs, deposits and escrows used?

Earn-outs and deposits are not common features of transactions. Earn-outs may be negotiated where pricing reflects expectations of significant growth, and deposits may be used if a buyer is based in a jurisdiction where there is a degree of uncertainty about its ability to proceed to completion. Escrows are commonly used as security for warranty claims.

20 How are acquisitions financed? How is assurance provided that financing will be available?

Bank-led acquisition financing is a common feature of private M&A transactions. However, buyers increasingly borrow from alternative finance providers such as direct lending funds and institutional investors. Where an acquisition is highly leveraged, payment-in-kind instruments may be included in the financing structure, and for acquisitions of a sufficient size, high-yield bond financing may be a financing component employed by a buyer.

In a controlled sales process, financing is often required to be provided on a 'certain funds' basis, broadly mirroring the approach taken on public takeovers in the United Kingdom. However, unlike in the context of public takeovers, there is no regulatory regime to comply with or oversight by a financial adviser with respect to certainty of funding, so documentation, conditionality and flexibility can vary significantly from deal to deal.

Where a newly incorporated entity is to be the buyer and requires capital, for example from a private equity fund, the seller will typically be provided with a directly enforceable equity commitment letter that will be conditional upon satisfaction of the conditions set out in the sale and purchase agreement and any debt financing arrangements. An equity commitment letter will typically require the buyer to draw on any debt financing that has been negotiated, but the provider of equity capital to the buyer will not usually be required to increase its equity contribution in the event that a lender defaults on its commitment to advance finance.

21 Are there any limitations that impact the financing structure? Is a seller restricted from giving financial assistance to a buyer in connection with a transaction?

English private limited companies and public limited companies are prohibited from giving 'financial assistance' in connection with, among other things, the acquisition of shares of public limited companies. Financial assistance is not specifically defined, but includes the giving of a gift, a guarantee, security and an indemnity, waiving or releasing obligations and advancing a loan. It may be possible to avoid the consequences of this prohibition by reregistering a public limited company as a private limited company, provided that in giving any financial assistance that is not otherwise prohibited the directors of a private limited company could conclude that doing so was consistent with their duty to promote the success of the company.

Conditions, pre-closing covenants and termination rights

22 Are transactions normally subject to closing conditions? Describe those closing conditions that are customarily acceptable to a seller and any other conditions a buyer may seek to include in the agreement.

Signing and completion of transactions can occur simultaneously in the absence of legal or regulatory obligations to satisfy before completing the transfer of title to shares or assets. A seller will accept conditions relating to such legal or regulatory obligations.

A buyer may seek conditions regarding the accuracy of fundamental (relating to a seller's title, capacity and authority) and business warranties at completion and the absence of any material adverse change since entering into the transaction, although often a seller will only accept extending conditionality to include the accuracy of fundamental warranties.

It is very unusual for English law-governed transactions to be subject to any financing conditions.

23 What typical obligations are placed on a buyer or a seller to satisfy closing conditions? Does the strength of these obligations customarily vary depending on the subject matter of the condition?

All parties will be expected to exert at least their reasonable efforts to ensure the satisfaction of any closing conditions. A 'best efforts' standard may be agreed that is more onerous and can require the expenditure of money, but it is not an absolute obligation to achieve the specified outcome.

A seller, particularly when conducting an auction process, will typically seek to impose a 'hell or high water' standard obliging the buyer to take whatever steps may be necessary to ensure the approval of applicable regulators. This could include disposing of parts of its business, parts of the target business and commencing litigation.

24 Are pre-closing covenants normally agreed by parties? If so, what is the usual scope of those covenants and the remedy for any breach?

A seller will typically agree to operate the target business in the ordinary course of business consistent with past practice, and will commonly agree to specify pre-closing covenants including:

- not to alter the share capital or make distributions to shareholders;
- not to acquire or dispose of assets, incur liabilities, enter into material agreements or commit to capital expenditure in excess of a specified value;
- not to create encumbrances;
- to maintain, without alteration, insurance policies;
- not to alter terms of employment or benefit entitlements or hire new employees on salaries in excess of a specified amount;
- not to commence litigation or waive any claims;
- to conduct the business in accordance with applicable law; and
- to grant access to the target company's books, records and premises.

A seller may also agree not to solicit competing proposals, to notify the buyer of any unsolicited approaches in respect of the target company or business and in respect of an auction process, with effect from closing, and to assign the benefit of any confidentiality agreements entered into with other potential buyers.

© Law Business Research 2017

Update and trends

In June 2016, a majority of voters in the UK voted in a national referendum in favour of the UK's exit from the European Union (Brexit) and on 28 March 2017, the UK gave formal notice under Article 50 of the European Treaty of its intention to leave the European Union. The impact of the political and economic uncertainty arising from Brexit (and the outcome of the UK general election on 8 June 2017, which resulted in no political party having a majority) on transaction activity and on valuations is still an open question. It is worth noting that according to the UK Office for National Statistics, there has been a significant fall in the number of successful transactions involving the acquisition of UK companies by foreign companies in Q2 of 2017 (44 transactions worth £2.9 billion) as compared to Q1 (70 transactions worth £9.5 billion). In terms of successful transactions involving the acquisition of UK companies by other UK companies in Q2, there were 66 transactions worth £4 billion as compared to Q1 (94 transactions worth £3.2 billion).

Another interesting trend is the fall in the number of transactions involving the acquisition of UK companies by Chinese companies in 2017 after a very active 2016. This appears to be the result of a crackdown by Beijing on outbound investments since Q4 2017 through restrictions imposed on capital outflows from China. In September 2017, the Chinese government introduced three new classifications for Chinese overseas investments: banned (eg, gambling), restricted (eg, property and entertainment) and encouraged (eg, industrial upgrades). It remains to be seen whether this will have an impact on Chinese acquisitions of UK companies. It is also worth noting that despite the outcome of the recent UK general election, the UK government still intends to take forward its manifesto pledge to implement plans for tighter screening of foreign investments by China and other countries to address concerns that such investments could compromise national security.

In addition, the parties also typically undertake not to solicit senior employees, to maintain the confidentiality of the transaction and only to make public announcements relating to the transaction with the other party's consent.

A breach of covenant will result in a claim for damages, which unlike a claim for breach of warranty is typically uncapped. An English court may make an order for specific performance to the extent that damages are not an adequate remedy.

25 Can the parties typically terminate the transaction after signing? If so, in what circumstances?

Consistent with the concept that risk with respect to the company, business or assets passes to the buyer from the date of entering into the sale and purchase agreement, typically parties cannot terminate a transaction in advance of a negotiated long-stop date, except to the extent that any condition is, or becomes, incapable of satisfaction. It is very rare that a breach of warranty or covenant permits a buyer to terminate a transaction.

26 Are break-up fees and reverse break-up fees common in your jurisdiction? If so, what are the typical terms? Are there any applicable restrictions on paying break-up fees?

Break fees are not common in the acquisition of private companies, businesses and assets. It is possible for an English company's constitution to restrict or prohibit certain transactions, including the giving of break fees. If not so prohibited, directors of an English company must be satisfied that agreeing a break fee is consistent with their fiduciary and statutory duties, including to promote the success of the company for the benefit of its members as a whole. A break fee may constitute unlawful financial assistance (see question 21) to the extent it results in a material reduction of net assets of an English public limited company. A reduction greater than 1 per cent is considered material.

The payment of a break fee by a listed company subject to the UK Listing Rules may constitute a class 1 transaction if the amount payable exceeds 1 per cent of the market capitalisation of the listed company.

Representations, warranties, indemnities and post-closing covenants

27 Does a seller typically give representations, warranties and indemnities to a buyer? If so, what is the usual scope of those representations, warranties and indemnities? Are there legal distinctions between representations, warranties and indemnities?

A seller will typically give warranties and, subject to the negotiating position of the parties and specific issues arising from due diligence, indemnities but not representations.

Warranties given by a seller typically address:

- the capacity and authority of the seller to enter into the sale and purchase agreement;
- in respect of the acquisition of a company, the share capital of the target company and its direct and indirect shareholdings;
- the basis of preparation of the target's financial statements;
- the absence of changes to the condition of the business since the date of the warranted financial statements;
- operational aspects of the business relating to employees, pensions and benefits, real property, financial commitments, commercial contracts, litigation and investigations, compliance with law, intellectual property and information technology; and
- in respect of a business acquisition, the condition and adequacy of the assets to be acquired.

Where a company or business is sold in an auction process, a narrower scope of warranties would be expected. If the seller is a private equity fund, it will typically limit its warranties to title, capacity and authority, and a buyer may negotiate with the target company management to provide business warranties in a separate deed (often referred to as a management warranty deed).

An inaccurate warranty will give rise to a damages claim for breach of contract whereby a buyer will have to prove that he or she has suffered a diminution in value of the asset purchased that is causally related to the inaccuracy of the warranty and is not regarded by law as being so remote that it would be unreasonable for the seller to incur damages, subject to a buyer's duty to mitigate its damages.

Subject to the negotiating position of the parties, specific risks identified through due diligence or disclosure are typically subject to indemnities (as a buyer is typically precluded from bringing a warranty claim in relation to a matter it is aware of signing). For example, specific indemnities may be given in respect of the outcome of ongoing litigation, the cost of remediating environmental damage prior to the buyer's acquisition or product liabilities in excess of an agreed level relating to the period prior to completion of the acquisition.

Subject to the particular drafting, an indemnity is an undertaking to pay in specified circumstances and so is not subject to the causation, remoteness and mitigation rules of a claim for damages.

Claims for misrepresentation can result in damages calculated on a tortious basis or under the UK Misrepresentation Act 1967, so a seller will typically exclude representations from a sale and purchase agreement.

28 What are the customary limitations on a seller's liability under a sale and purchase agreement?

A seller's aggregate liability under a sale and purchase agreement will customarily be capped at an amount equal to the purchase price. Business warranty claims will typically be subject to a separate regime whereby:

- each individual claim must exceed a materiality threshold (or de minimis) often up to 0.1 per cent of the purchase price;
- the aggregate value of claims must exceed a threshold, often between 1 and 2 per cent of the purchase price, with the entire value of claims then being recoverable;
- the seller's aggregate liability is capped, often at less than 25 per cent of the purchase price; and
- the ability to bring warranty claims expires 12 to 24 months after completion.

Fundamental warranties (see question 22) and tax warranties are often carved out of the limitation regime.

In addition, more general limitations on a seller's liability will customarily include:

© Law Business Research 2017

- knowledge qualifications in warranties and materiality qualifications in warranties and covenants;
- qualifying warranties with disclosure contained in the disclosure letter and all information contained in a data room;
- provisions granting the seller the conduct of claims brought by third parties; and
- barring double recovery and requiring the buyer to exhaust other available remedies.

29 Is transaction insurance in respect of representation, warranty and indemnity claims common in your jurisdiction? If so, does a buyer or a seller customarily put the insurance in place and what are the customary terms?

Warranty and indemnity insurance is a common feature of private M&A transactions in the UK, particularly in competitive auction processes or where the seller is looking for a clean break from completion of the transaction.

The insurance is intended to cover losses suffered by the policyholder where a successful claim can be made for breach of certain warranties or under a tax covenant. Typically, a policy will not provide the policyholder with protection in respect of specific indemnities that may arise as a result of due diligence by the buyer or disclosure by the seller. However, it is possible to negotiate insurance for known and specific contingent risks such as tax and environmental liabilities.

Insurance may be arranged by either a seller or buyer. A seller policy may be suitable where the seller is selling a company or business and intends to invest or distribute to its shareholders the proceeds of sale.

A buyer's policy secures greater financial recourse than is offered by a seller, which is of particular assistance in an auction where low caps on liability may be offered or the only financial recourse available in respect of business warranties comes from target management.

An English law-governed policy will typically exclude:

- issues that are known to the policyholder;
- financial obligations payable as a consequence of the selected pricing mechanism;
- fines and penalties that are uninsurable by law;
- financial obligations resulting from pension underfunding;
- liabilities arising from transfer pricing; and
- issues that are specific to a transaction, such as liabilities arising from the use of asbestos.

In addition, a seller's policy would exclude recovery in respect of fraud by the seller.

Subject to prevailing market conditions, the value of a claim under a policy will typically be limited to approximately 10 to 20 per cent of the enterprise value of the company or business being purchased and will be subject to a deductible in an amount equal to 0.5 to 1 per cent of the enterprise value. The premium to arrange a policy will often be equal to approximately 1 to 2.5 per cent of the value of the policy.

30 Do parties typically agree to post-closing covenants? If so, what is the usual scope of such covenants?

Parties will often agree not to solicit each other's senior employees (or extend beyond completion any such undertaking effective from signing) and a seller will often covenant not to compete with the company or business that has been sold. To be enforceable any non-competition covenant must apply to a reasonable geographic area for a reasonable time period typically considered to be up to two years.

Tax

31 Are transfer taxes payable on the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

Stamp duty (or stamp duty reserve tax) is generally payable at a rate of 0.5 per cent on the transfer of shares in a UK-incorporated company. Stamp duty land tax (or land and buildings transaction tax in Scotland) is payable on transactions involving UK land at varying rates depending on the nature and value of the property. These stamp taxes are subject to various reliefs and exemptions. Transfers of other business assets are not generally subject to stamp taxes.

32 Are corporate taxes or other taxes payable on transactions involving the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

A company or individual disposing of shares or of a business or other assets may be subject to tax on any chargeable gain arising (currently at a rate of 19 per cent for companies, and for most disposals at a rate of 20 per cent for individuals) subject to available exemptions or reliefs. Value added tax (VAT) is due (generally at a rate of 20 per cent) on supplies of goods or services that are not exempt for consideration by taxable persons for VAT purposes. Generally a sale of shares will be an exempt supply for VAT purposes. A sale of a business may be outside the scope of VAT if it qualifies as a transfer of a going concern for VAT purposes. The person liable to account for VAT will depend on the nature of the supply and of the parties, and on where the supply is treated as taking place for VAT purposes.

Employees, pensions and benefits

33 Are the employees of a target company automatically transferred when a buyer acquires the shares in the target company? Is the same true when a buyer acquires a business or assets from the target company?

The acquisition of an English company does not alter the employment relations a company has with its employees. Where a business in the UK is acquired, TUPE applies (see question 5) to automatically transfer to the buyer the employment and benefit obligations of the target business.

Davis Polk

Will Pearce — **will.pearce@davispolk.com**
Simon J Little — **simon.little@davispolk.com**
William Tong — **william.tong@davispolk.com**

5 Aldermanbury Square
London EC2V 7HR
United Kingdom

Tel: +44 20 7418 1300
Fax: +44 20 7418 1400
www.davispolk.com

© Law Business Research 2017

34 Are there obligations to notify or consult with employees or employee representatives in connection with an acquisition of shares in a company, a business or assets?

TUPE requires that the seller and buyer notify and, if suitable, consult with trade unions or employee representatives (in the absence of a trade union) in respect of employees who may be impacted by a transfer of employment resulting from the acquisition of a business in the UK. The obligation to consult is only triggered where it is proposed that actions are to be taken that will impact employees who are subject to the business acquisition. A failure to comply with the obligations can result in compensation being payable equal to 13 weeks of salary.

35 Do pensions and other benefits automatically transfer with the employees of a target company? Must filings be made or consent obtained relating to employee benefits where there is the acquisition of a company or business?

Pension and other employee benefit obligations remain the responsibility of a target company following its acquisition. The UK Pensions Regulator has the power to issue financial support directions (FSDs) or contribution notices (CNs) in respect of underfunded defined benefit pension schemes, which can be triggered by a change in control of a company that results in a material weakening of the employer covenant (ie, the ability of the employer with responsibility for the defined benefit pension scheme to honour obligations owing to pension scheme members).If a target company sponsors a defined benefit contribution scheme, it is possible for parties to a transaction voluntarily to apply for a clearance notice confirming that the UK Pensions Regulator will not exercise its powers to issue an FSD or CN in circumstances in which there is an event that is materially detrimental to the ability of the pension scheme to satisfy its obligations. Clearances can be in respect of a single transaction or on an ongoing basis (which are of assistance to private equity funds who may envisage a series of transactions following completion of an acquisition, as well as a disposal or listing to realise their investment).

© Law Business Research 2017

Getting the Deal Through

Acquisition Finance
Advertising & Marketing
Agribusiness
Air Transport
Anti-Corruption Regulation
Anti-Money Laundering
Arbitration
Asset Recovery
Automotive
Aviation Finance & Leasing
Aviation Liability
Banking Regulation
Cartel Regulation
Class Actions
Cloud Computing
Commercial Contracts
Competition Compliance
Construction
Copyright
Corporate Governance
Corporate Immigration
Cybersecurity
Data Protection & Privacy
Debt Capital Markets
Dispute Resolution
Distribution & Agency
Domains & Domain Names
Dominance
e-Commerce
Electricity Regulation
Energy Disputes
Enforcement of Foreign Judgments
Environment & Climate Regulation
Equity Derivatives
Executive Compensation & Employee Benefits
Financial Services Litigation
Fintech
Foreign Investment Review
Franchise
Fund Management
Gas Regulation
Government Investigations
Healthcare Enforcement & Litigation
High-Yield Debt
Initial Public Offerings
Insurance & Reinsurance
Insurance Litigation
Intellectual Property & Antitrust
Investment Treaty Arbitration
Islamic Finance & Markets
Labour & Employment
Legal Privilege & Professional Secrecy
Licensing
Life Sciences
Loans & Secured Financing
Mediation
Merger Control
Mergers & Acquisitions
Mining
Oil Regulation
Outsourcing
Patents
Pensions & Retirement Plans
Pharmaceutical Antitrust
Ports & Terminals
Private Antitrust Litigation
Private Banking & Wealth Management
Private Client
Private Equity
Private M&A
Product Liability
Product Recall
Project Finance
Public-Private Partnerships
Public Procurement
Real Estate
Renewable Energy
Restructuring & Insolvency
Right of Publicity
Risk & Compliance Management
Securities Finance
Securities Litigation
Shareholder Activism & Engagement
Ship Finance
Shipbuilding
Shipping
State Aid
Structured Finance & Securitisation
Tax Controversy
Tax on Inbound Investment
Telecoms & Media
Trade & Customs
Trademarks
Transfer Pricing
Vertical Agreements

Also available digitally

Online

www.gettingthedealthrough.com

Private M&A
ISSN 2515-3781

THE QUEEN'S AWARDS FOR ENTERPRISE: 2012

Official Partner of the Latin American Corporate Counsel Association

Strategic Research Sponsor of the ABA Section of International Law

© Law Business Research 2017