ALTANA
AVOCATS • PARIS

ACQUIRING A CARVED OUT BUSINESS IN FRANCE

"The usual suspects and the French touch"

JEAN-NICOLAS SORET
PARTNER (M&A)
ALTANA

MARIANNE FRANJOU
PARTNER (EMPLOYMENT)
ALTANA

Carved out businesses and spin offs in France require a particular attention, as certain rules differ from many other jurisdictions, in particular the US. Transfer of contracts, employees and personal data, assumption of liabilities, etc. are areas where Europe and the US are not aligned.

Acquisition opportunities with very favourable conditions can be found with groups seeking to dispose of a non core business. The pressure from the financial markets to have a clear strategy and generate high EBITDA is at the origin of the current trend for major European corporations to focus on their core businesses. Antitrust rules and the obligation to dispose of certain divisions in the context of a broader acquisition also are a frequent source of divestment.

"THE USUAL SUSPECTS" OF PURCHASING A CARVE OUT BUSINESS ARE THE CONDUCT OF THE DUE DILIGENCE, THE ASSESSMENT OF THE TAX IMPLICATIONS, AND THE SETTING-UP OF TRANSITION SERVICES

Purchasing a carved out business from a group can be seen as a common exercise, with similar features and constraints around the world (the "usual suspects"). Similar areas of attention include the conduct of due diligence, a strong focus on the tax impact, as well as the drafting of agreements designed to ease the transition.

1. Due diligence requires particular attention in the context of the acquisition of a carved out business, as the list of assets and liabilities to be transferred must be defined with great care. Certain assets are often difficult to isolate, such as trademarks used by the divesting group as well as the divested business.

2. Tax implications of each possible transaction structure must be identified; in particular any registration tax, capital gains, and the possible forfeiture of tax loss carry forward.

3. Transition services are often expected from the acquirer especially when the acquirer does not have its own structure in Europe. Consequently, spin offs commonly require the execution of a transition services agreement with respect to with respect to generally information technology, leasehold or trademark licences, whereby the seller provides services or authorizes the use of certain assets to the carved out business in order to facilitate its operation by the new owner.

"THE FRENCH TOUCH" MAINLY RELATES TO THE STRUCTURING OF THE TRANSACTION, EMPLOYEE PROTECTION, PERSONAL DATA AND CERTAIN REGULATORY HURDLES

The similarities in the conduct of spin offs should not however overshadow peculiarities of French law, that foreign investors should particularly be aware of (the "French touch"):

1. Structuring:
How to structure a transaction and deciding whether to proceed via an asset transfer or a share transfer are common questions with answers revealing the specificities of the French legislation.

Whereas an asset transfer can be seen as the safest structure for a buyer (as few liabilities are transferred by operation of law), such transaction structure has legal effects that often require using a more complex approach.

Under French law, contracts other than employment contracts and commercial lease agreements may not be assigned without the prior approval of both parties. Therefore, when purchasing a business, one will need to make sure that the prior approval of the key contracting parties has been secured. However, the same rule does not apply when the business is contributed in exchange for shares, through a "business contribution in kind", rather than sold for a cash consideration.

This is the reason why spin offs are often organized through a 2-step approach, with the contribution of the divested business to a wholly-owned newly formed subsidiary of the seller, followed by the sale of the newco's shares.

However, this 2-step approach is not systematically used, as a business contribution in kind implies the transfer not only of all assets attached to such business, but also of all liabilities.

Conversely, a pure asset transfer entails a limited transfer of liabilities (e.g. employee-related liabilities, environmental liabilities, etc.), as there is no general concept of "successor liability" under French law.

2. Employee protection:
This topic is one of the main peculiarities of carve-out transactions conducted in France.

In France, divesting a business requires informing and consulting the works council (as well as, in some cases, the health and safety committee). This is often time consuming and can become a difficult exercise, especially when the financial means of the acquirer are questioned, or when the acquirer is of a different business culture, for being a foreign entity or a private equity house. Faced with the recurrent attitude of certain works councils intentionally delaying significantly the rendering of their opinion in an attempt to block a contemplated transaction, the French legislator recently enacted a law limiting the time allowed to the works council to render its opinion (between one and four months depending on the situation).

As in most European jurisdictions, the TUPE regulation applies in France, which means that all employees working mainly for a given business unit are automatically transferred upon the sale or transfer of said business unit. This is a rule of public order, which has significant implications, especially when the operation of the divested business on a stand-alone basis requires job cuts. Any redundancy plan can be implemented only after the business transfer has occurred; otherwise, its validity could be challenged and the employees having been made redundant could request to be rehired or claim for damages. This often makes it difficult for acquirers who are expecting the seller to pay for part of the social cost. Sellers who seek to reduce the headcount without having to bear the burden of making massive layoffs often agree to factor the social cost in a lower purchase price. It is not unusual to find situations where the employee factor is the main driver to the spin off; in some cases it happens that the price becomes negative due to the transfer of employee-related liabilities (such a social benefits, pension schemes, etc.).

3. Transfer of personal data:
From the Safe Harbour to the Privacy Shield.

Whereas personal data could be easily transferred to a US-based acquirer until recently, the European Court of Justice recently ruled in October 2015 that the so-called Safe Harbour did not provide sufficient guarantees to the persons whose data were transferred, and declared the Safe Harbour illegal. Although a replacement scheme, known as the Privacy Shield, is expected to be implemented in the near future, the situation is rather unsecured in the meantime, as the legal framework according to which personal data can be transferred to the US is unclear.

4. Regulatory hurdles:
Specific regulatory hurdles, such as antitrust control and the control of foreign investments, also need to be taken into consideration when investing in France.

Control of foreign investments, similar in nature to CFIUS, is an issue that foreign investors should be particularly aware of. The investment in a number of sectors requires obtaining a clearance from the French authorities. Unsurprisingly, all activities relating to the defence industry are so regulated. More surprising can be certain other sectors forming part of a long list requiring such a clearance including, but not limited to, any activity relating to public health as well as the integrity, security and continuity of a transportation service network, an electronic communications network, activities relating to electricity, gas, oil or water supply, provided that they are of national vital importance in terms of public order, public security or national defence.

AUTHORS

Jean-Nicolas Soret
Partner, *Mergers & Acquisitions*
jnsoret@altanalaw.com

Marianne Franjou
Partner, *Employment*
mfranjou@altanalaw.com

ALTANA

Altana is a full-service business law firm with 60+ lawyers, offering tailor-made legal assistance in complex cross-border and domestic transactions and litigation.

Our M&A team has a very strong international focus and several of our attorneys are admitted both to the Paris Bar and to the New York Bar. We advise on public and private mergers, acquisitions, divestiture, joint venture and carve out transactions, as well as group reorganizations.

We work seamlessly with the other departments of the firm, including our employment, IT, IP and real estate departments.

KEY POINTS OF ATTENTION

"THE USUAL SUSPECTS"

- Identify all assets and staff to be transferred through extensive due diligence
- Identify the tax implications of each possible transaction structure
- Prepare customized transition services agreements, as well as other ancillary agreements

"THE FRENCH TOUCH"

- Structuring the acquisition through the purchase of assets or shares
- Beware of specific employee protection rights
- Caution is required when transferring personal data
- Control of foreign investment can delay or block the process