REGULATORY ISSUES IN DRAFTING M&A AGREEMENTS

M&A AGREEMENTS

Federated Press
Courtyard by Marriott Downtown Hotel,
Toronto, Ontario

MARK KATZ

September 23, 2013

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES

OUTLINE

- Key Regulatory Regimes
  - Competition Act
  - Investment Canada Act
  - Other Potentially Relevant Regimes
- Implications for M&A Agreements



COMPETITION ACT

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES

Merger Review Under the Competition Act

- Merger review is responsibility of Competition Bureau
  - Independent law enforcement agency within Industry Canada
  - Headed by Commissioner of Competition
- Two aspects to merger review under the Competition Act
  - Substantive review
  - Mandatory pre-merger notification

Substantive Merger Review

- Competition Bureau has the jurisdiction to review any "merger"
- "Merger defined to include any acquisition of assets, shares or other forms of "control" or the acquisition of a "significant interest" in whole or part of a business
  - Definition captures a broad range of transactions

Substantive Merger Review

- Bureau may challenge a merger if the transaction substantially lessens or prevents competition in any relevant market affecting Canada (i.e., could be an international market)
- Merger challenges adjudicated by Competition Tribunal, which can block a transaction from proceeding or order divestiture/dissolution if it has already closed
- Challenge can be brought up to 1 year following closing

Pre-Merger Notification

- Although the Bureau has the jurisdiction to review and challenge any "merger", transactions that exceed certain financial thresholds also must be notified to the Bureau in advance of closing
  - Each party to the transaction must file prescribed notification form
  - Required even if transaction raises no substantive issues

Pre-Merger Notification

- Five types of transactions are potentially subject to notification:
  - Asset acquisitions
  - Share acquisitions
  - Corporate amalgamations
  - Formation of non-corporate "combinations" (e.g., partnerships)
  - Acquisition of interests in non-corporate "combinations"
- Statutory thresholds must be satisfied:
  - "operating business"
  - "size of transaction"
  - "size of parties"
  - interest to be acquired

Timing

- Parties cannot close a notifiable transaction prior to expiry of statutory waiting period
  - 30 day initial waiting period triggered by filing
  - If Bureau issues Supplementary Information Request ("SIR"), cannot close until 30 days following submission of responses to SIR
- Waiting period may be terminated earlier if Commissioner issues "Advance Ruling Certificate" or "no action letter"
- Timing of substantive review based on Bureau service standards
  - 14 days for "non-complex" transaction
  - 45 days for "complex" transaction
- Possible for statutory waiting period to expire before substantive clearance received

INVESTMENT CANADA ACT ("ICA")

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES

ICA Review

- ICA review also has two aspects
- Net Benefit Review:
  - Acquisition of control of a Canadian business by a non-Canadian is reviewable if certain thresholds exceeded
  - Current thresholds based on value of assets of Canadian business
  - Thresholds can vary based on country of origin of investor (is it a WTO member) and type of business (is it "cultural")
  - Canadian government must be satisfied that reviewable acquisition is likely to be of "net benefit to Canada"
- National Security Review:
  - Much broader scope for potential application
  - Will transaction "be injurious to national security"?

Net Benefit Review Process

- Typically required to be completed pre-closing
- Timing:
  - Initial 45 day review period
  - Minister may extend unilaterally by 30 days
  - Additional extensions possible thereafter on consent of the Minister and the investor
- At end of process Minister either approves, remains silent (deemed approval) or denies approval

Undertakings

- "Net benefit" approach almost always conditional on undertakings by investor
- May include commitments re:
  - Head office location
  - Employment levels
  - Canadians in management and/or on board of directors
  - Capital expenditures
  - R&D investments
  - Resource processing in Canada
  - Technology transfers to Canada
- Term of 3-5 years
- Special considerations for "state owned enterprises" ("SOEs")

National Security Review Process

- Independent and parallel process to "net benefit" review
  - No acquisition of control required – minority interests can trigger review
  - Review process can be pre or post closing
  - Can take up to 130 or more days to complete if review process invoked
- Government may take any measures considered advisable to protect national security, such as prohibiting the investment, requiring divestiture, or imposing other conditions



OTHER RELEVANT REGULATORY REGIMES

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES

Other Relevant Regimes

- You may encounter a variety of other regulatory regimes that require pre-closing review or are relevant from other perspectives
- Principal Canadian regulatory regimes include:
  - Review of acquisitions involving "transportation undertakings"
  - Review of acquisitions involving telecom/broadcasting undertakings
  - Corruption of Foreign Public Officials Act
  - Eligibility rules for government contracts: e.g., Public Works and Government Services Canada
- Principal foreign regulatory regimes include:
  - HSR (U.S. antitrust)
  - CFIUS (U.S. national security review)
  - Anti-corruption: Foreign Corrupt Practices Act (U.S.), U.K. Bribery Act



IMPLICATIONS FOR M&A AGREEMENTS

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES

Implications for M&A Agreements

- Regulatory issues can be a key aspect of negotiating deal documents:
  - Representations and warranties
  - Indemnities
  - Covenants
  - Closing conditions
  - Termination
  - Conduct of target business pre-closing
  - Information sharing
  - Non-competition obligations

Representations and Warranties

- One main type of rep/warranty deals with non-applicability of review regime
- Depending on circumstance, provided by purchaser/vendor/both
- Competition Act
  - Vendor reps not an "operating business"
  - "Size of transaction" – vendor reps below asset/revenue thresholds
  - "Size of parties" – purchaser and/or vendor rep below asset/revenue thresholds
- Investment Canada Act
  - Purchaser reps is not a "non-Canadian"
  - Purchaser/Vendor reps is a "WTO Investor"
  - Vendor reps that Canadian Business is not a "cultural" business
  - Vendor reps that Canadian Business is below relevant asset threshold

Representations and Warranties

- Other main type of rep/warranty relates to non-violation of substantive regulatory laws, e.g.:
  - Competition Act
  - Anti-corruption laws
  - Eligibility rules for government contracts
- These reps/warranties are becoming increasingly common because of potential consequences involved
- Combine with indemnities for breach of rep/warranty

Covenants

- Three principal types:
  - Covenant to file necessary (or desirable) regulatory materials within prescribed timeframe
  - Covenant to cooperate during regulatory process
  - Covenant to obtain regulatory approvals
- Covenants to obtain approvals becoming more contentious as increasing number of Vendors insisting on "hell or high water" covenant, i.e., Purchaser must agree to take any step required by regulators in order to secure approval

Closing Conditions

- Typically involve, where applicable:
  - Competition Act
  - Investment Canada Act (net benefit/national security)
  - Canada Transportation Act
- Closing conditions usually for benefit of both Purchaser and Vendor
- In some circumstances, and where available, party may want to limit closing condition (e.g., close if relevant waiting period expires rather than require positive clearance or approval)

Termination

- Regulatory considerations for termination provision:
  - Extensions of closing date to accommodate regulatory review processes
  - "Outside" date for closing
  - "Break fees"

"Gun-Jumping"

- Competition authorities will be concerned about behaviour that facilitates pre-closing coordination between merging parties
  - Purchaser prematurely taking control of Target's business operations
  - Information exchanges that could be used to coordinate future behaviour if merger does not proceed
- Potential gun-jumping issues in M&A agreements:
  - Provision governing pre-closing conduct of Vendor/Target
  - Provision allowing Purchaser to access information regarding Vendor/Target

"Gun-Jumping"

- DO NOT include contractual provisions that entitle Purchaser to review, approve, participate in, manage or restrict Target's ordinary course business activities
- DO make access to information subject to "applicable laws" and any confidentiality agreement between the parties

Non-Competition Covenants

- Post-merger non-competition covenants typically given by Vendor
- Examples of recent enforcement actions
  - Telefonica/Vivo: Telefonica of Spain acquired interest in Vivo of Brazil from Portugal Telecom. Non-compete prevented competition between Telefonica and PT in Spain and Portugal, not Brazil
  - Siemens/Areva: JV in relation to nuclear power plants. Non-compete for 11 years after termination and covered products not part of JV
  - JCI Jones/Oltrin Solutions: Sale of customer list relating to bulk bleach business. Non-compete for 6 years following acquisition

Non-Competition Covenants

- Non-compete must be reasonable as between the parties and in the public interest
  - Reasonable:
    - interest entitled to protection
    - covenant is no wider than necessary (time and scope)
    - reciprocal obligations subject to greater scrutiny
  - In the public interest:
    - does not prevent or lessen competition substantially in a relevant market

REGULATORY ISSUES IN DRAFTING M&A AGREEMENTS

MARK KATZ
416.863.5578
mkatz@dwpv.com

PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE ▪ FOCUSED ▪ PROVEN ▪ INNOVATIVE

A superior line of thought

DAVIES