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Impact of COVID-19 on French M&A Transactions

COVID-19 and government measures to fight it may significantly affect M&A transactions.

On March 16, 2020, President Emmanuel Macron announced the implementation of unprecedented and extendable quarantine measures in order to limit the spread of the COVID-19 virus. Following this announcement, a new bill came into force on March 24, 2020, the purpose of which is to declare a state of health emergency and authorize the government to implement measures to support sectors of the economy impacted by this crisis. While further details on the content of such measures are yet to be provided, this *Client Alert* outlines key points to consider when carrying out a M&A transaction in France within the context of the COVID-19 outbreak.

Works Council Information-Consultation Process

Q: Can works council meetings take place under current circumstances, or does the situation constitute a valid excuse not to hold any works council meeting?

- The current Q&A delivered by the French Ministry of Labor with respect to the COVID-19 crisis states that, “*The use of videoconferences [with the works council] is encouraged, if necessary, in order to avoid physical contact.*” Companies are therefore advised to continue conducting works council procedures if required, but potentially in alternative ways.
- Works council meetings by videoconference are already possible, but, in practice, they could be difficult to implement in case of individual videoconferencing from home. Some works council members may not be technically equipped and videoconferencing with a significant number of participants, each in a separate location, quickly becomes difficult.
- The law enacted on March 24, 2020, allows that derogatory rules to the law be taken by urgent governmental ordinance. There is not yet clarity on the content: for example, will a telephone conference be acceptable, apart from videoconferencing? This should be known shortly after the enactment of the law.

- It is also advisable to ask local HR functions whether the “internal regulation” or the “collective agreement governing the functioning” of the concerned works council(s) contains any specific provisions in respect of videoconferencing for example.

Q: Given the current uncertainty, what are the recommended next steps?

- Parties should implement or pursue the works council consultation process as provided by the relevant contractual documentation, such as a put option agreement or a memorandum of understanding. Convening of the works council members should be carried out in the usual way and by e-mail. It is also advisable to ask works council members to confirm receipt of any e-mails and to activate the “acknowledgement of receipt” function in Outlook.
- It is likely that, for upcoming works council meeting(s) as from next week, the new ordinance “*modifying the modalities of employee representative consultation*” will have been adopted. Companies should then be in a position to hold that meeting in a legally compliant way.

Enforcement of French Law Binding Offer / Put Option Letters

Q: Can a seller require the enforcement of a put option letter towards the buyer if the latter is reluctant to sign the sale and purchase agreement?

- Under put option agreements or binding offer letters, the seller is generally entitled to exercise its option to sell within a certain timeframe after having obtained the opinion of the relevant workers’ representatives. This option translates into an obligation for the buyer to sign the relevant sale and purchase agreement if the seller exercises its option. In the COVID-19 context, certain buyers may be reluctant to sign the sale and purchase agreement.
- The seller should, in principle, be able seek specific performance of the unfulfilled obligation unless specific performance is impossible or if there is a manifest disproportion between the cost of specific performance for the bona fide buyer and its interest for the target. If this is the case, the seller would be awarded damages and not specific performance. Put option agreements often include provisions whereby the parties have agreed to specific performance and have excluded the right of the buyer to oppose to it.
- Specific performance requires the intervention of a judge, which may be challenging in the current circumstances, as French courts have largely been closed since March 16, 2020 — except for cases relating to fundamental rights and specific urgent matters. For instance, all current cases to be heard by French commercial courts have been delayed by six to eight weeks (until mid-April). Therefore, specific performance of a put option would, in practice, be difficult to obtain on an urgent and/or short-term basis.
- To the extent the put option actually includes that provision, sellers may be better off relying on the provision whereby the sale and purchase agreement should be deemed signed following the exercise date of the put option even if not actually signed by the buyer.

Handling of Extraordinary Decisions Between Signing and Closing

Q: How will COVID-19 affect the intermediary period between signing and closing of a transaction?

- Between signing and closing, selling entities or target companies may need to take decisions that fall out of the scope of their ordinary course of business to deal with the outbreak of the COVID-19 despite a contractual commitment not to do so without obtaining the prior approval of the buyer. This may raise concerns, in particular in circumstances in which the absence of breach of such management between signing and closing provision is a condition precedent to the closing of the transaction.
- When faced with such a situation, any party to an agreement must comply with the French law principle pursuant to which "*contracts must be negotiated, entered into and performed in good faith.*" This requirement implies a duty to cooperate with the buyer during the performance of the contract, in particular the timely disclosure of information or difficulties that could have an impact on the completion of the transaction.
- Parties should also scrutinize the terms of their agreement so as to determine the actions to take and the extent to which consent of the buyer is required prior to making a decision. Sellers should be able to rely on specific carve-out clauses in an emergency or disaster situation, which are often included in sale and purchase agreements. Irrespective of such clauses, sellers should try to minimize any adverse effect of the situation and of the decisions made to remedy the situation. Sale and purchase agreements may also include provisions whereby the consent of the buyer may not be unreasonably withheld or delayed, thus enabling the seller to execute urgent decisions if reasonably needed irrespective of the buyer's consent.

Purchase Price Mechanism

Q: Is the COVID-19 pandemic likely to impact SPA pricing mechanisms?

- In France, a significant number of transactions are entered into on the basis of the so called "locked box" mechanism whereby the price paid by the buyer on closing is determined on the basis of the accounts of the target available at the time of the signing of the sale and purchase agreement. Therefore the changes in the financial situation of the target between signing and closing are not captured, bar "leakages". Broadly speaking, leakages are payments made by the target to the seller, or seller-related parties, between signing and closing, such as distribution of dividends or the payment of fees that should have been borne by the seller and that therefore are deducted from the purchase price paid by the buyer.
- Given the impact of COVID-19 on the financial situation of many companies, investors are likely to refuse to agree to determine the price of a transaction on the basis of a locked box. Investors will want to capture such financial impact on the net debt and working capital situation of the target on closing, and will therefore want the price to include a net debt and working capital adjustment based on closing accounts.

- COVID-19 is also likely to have a negative impact on the multiples paid by investors, given the current uncertainty and that competition in processes is likely to decrease because financings may be more difficult to secure and certain investors may want to focus on managing their business instead of participating to M&A processes. Parties may also try to bridge their possible disagreement on the price of a transaction resulting from the current crisis through earn-out clauses or other forms of post-closing adjustments meant to capture the future financial performance of the target.

Possibility to Invoke a Force Majeure Event Preventing a Payment Obligation

Q: How and to what extent a buyer may rely on force majeure to avoid a payment obligation?

- Within the context of COVID-19, some buyers may argue that a force majeure event prevents them from fulfilling their payment obligation, particularly in cases in which they might not have access to financing to meet their closing obligations. It is, however, generally difficult to rely on force majeure under French law.
- Under French law, force majeure triggers the termination of a contract and discharges parties from their obligations, only to the extent that the prevention of the fulfilment of the obligation is permanent. If the prevention is temporary, the force majeure event only suspends the performance of the obligation for a limited period of time.
- In addition, French law denies debtors the ability to invoke the force majeure concept for payment obligations. Such rationale is explained by the fact that financing resources, as fungible goods, cannot be permanently and totally unavailable.
- Furthermore, sale and purchase agreements often include representations and warranties from a buyer, outlining responsibility for the financing of the transaction and confirming that no financing condition applies. In certain circumstances, the payment of the purchase price is guaranteed by the parent company of the buyer, making it more difficult for the buyer to invoke a force majeure event.
- Buyers could argue that the unforeseeable refusal from a financing party to make the required financing available constitutes a force majeure event. Buyers could also argue that the public restrictions on freedom of movement rendered the granting of the funds impossible within the agreed deadlines, but there is no certainty that French courts will consider that these are force majeure events. Another recourse that buyers may rely on are the hardship concept and material adverse change provisions included in the sale and purchase agreement but hardship is often waived under sale and purchase agreements and MAC clauses are relatively rare in French M&A transactions.

Hardship

Q: Can a party not comply with some or all of its contractual undertakings on the basis of hardship provisions?

- **French hardship legal regime:** a party may ask another party to enter into renegotiations if performance of the contract has been rendered extremely expensive because of a change in circumstances that was unforeseeable by the parties when they entered into the contract.
- **Scope:** the hardship legal regime provided by the French Civil Code automatically applies to agreements (i) entered into on or after October 1, 2016, and (ii) that do not expressly exclude the

application of Article 1195 of the French Civil Code to such agreement (it being specified that such rules do not apply by law to securities sale and purchase agreements entered into on or after April 20, 2018).

- **Consequences:** if the renegotiations fail or if the other party refuses to renegotiate the agreement, the judge will have the power to revise or terminate the agreement at the request of one party. In any event, performance of the agreement must continue during the renegotiations.
- **COVID-19:** as the French hardship legal regime is not applicable to transfers of securities unless expressly stated in the contract (since April 2018), and was often excluded from sale and purchase agreements prior to that date, it is worth checking whether the contractual documentation includes any hardship provision. In the event it does, and a party asks for renegotiation, only a judge can terminate the agreement, it being specified that due to the current suspension of judicial activities, obtaining a court hearing before a judge will be challenging in the coming weeks.

Material Adverse Change Clause

Q: Can the COVID-19 outbreak trigger the application of a material adverse change (MAC) clause?

- **MAC clause under French law:** Use of MAC is rather uncommon in French M&A deals. A MAC clause differs from force majeure provisions, as these clauses do not require evidence that performance of an agreement has become impossible but only less profitable for one party (usually the buyer). As there is no legal definition of MAC clause under French and very little case law, it is necessary to scrutinize the definition of “material adverse change” or “material adverse effect” in the relevant documentation.
- **Qualification:** MAC clauses typically provide that, to qualify as a material adverse change, an event, in this case the COVID-19 outbreak and/or the quarantine and lockdown measures ordered to mitigate it, must be non-foreseeable at the time of the contract and must have a long-term and material impact on the target taken as a whole, and not only to some of its divisions. Some MAC clauses refer to a threshold in terms of financial impact on the target which renders the analysis less subjective.
- **Carve-outs:** MAC clauses frequently include a list of events or circumstances that cannot be deemed to cause a material adverse change. Epidemics and disease outbreaks are sometimes included in such list of exceptions. Absent an express exception, a seller willing to force a buyer to close may argue that COVID-19 falls within more broadly defined carve-outs for changes in general economic condition, financial markets, events generally affecting an industry, natural disaster, or emergencies. Certain carve-outs only apply if the target is not disproportionately affected as compared to others in the same industry. In any event, the outcome in court will largely depend on the wording of the considered clause and the specific circumstances of the target.

Non-Performance by Another Party (*Exception d'inexécution*)

Q: If one party only is not in a position to perform its contractual obligations due to COVID-19, can the other party refuse to perform its own obligations?

- Under French law, a party is entitled to refuse to perform its obligations under an agreement if the other party has not performed its own obligations and such non-performance is considered as a

serious breach of the agreement. This implies that a party has already breached the agreement and that such breach substantially affects the other party.

- A party is also entitled to preventively suspend the performance of its contractual obligations to the extent (i) it is clear that the other party will not comply with its own undertakings in due course (on the basis of its public statements or evidence received from a third party, for example), (ii) such non-performance will have a serious impact on the other contracting party (e.g., impact on its capacity to perform its own obligations towards a third party), and (iii) notice is given as soon as practicable.
- In an M&A transaction, to the extent the seller complies with its obligation to transfer the securities of the target on closing to the buyer, it will be difficult for the buyer to invoke the absence of performance of the seller as the change in the situation of the target between signing and closing is independent from the seller's obligation to deliver the securities of the target to the buyer.

Electronic-Registered Letters with Acknowledgment of Receipt

Q: Is it still possible to send and receive letters with acknowledgment of receipt? What is the legal force of an electronic-registered letter?

- In the current context, despite post offices being in limited operation, there may be some difficulty in sending and/or receiving registered letters with acknowledgment of receipts. The French post office provides a certified online service allowing for the dispatch of electronic registered letters with acknowledgment of receipt (e-RLAR) [here](#).
- E-RLARs offer the same validity and probatory value as regular registered letters, with acknowledgment of receipt provided they comply with the requirements of Article 44 of Regulation (EU) No 910/2014 of the European Parliament and of the Council of 23 July 2014 on electronic identification and trust services for electronic transactions in the internal market and repealing Directive 1999/93/EC. It is recommended to use the online service provided by the French post office, which is certified as compliant with EU requirements.
- If the recipient of the e-RLAR is an individual, they must give their consent to the use of the service. In addition, the recipient should, within 15 days of being informed by the French post office of the dispatch of the e-RLAR, accept or refuse to receive this e-RLAR. If the e-RLAR is accepted, the post office will provide time stamp proof to the dispatcher in order to confirm the reception of the e-RLAR.

Impact on Restructuring or Insolvency Proceedings

Q: Considering the COVID-19 outbreak, is it possible to formulate restructuring or insolvency related requests before French commercial courts?

- Pending the orders that will be taken by the French government in this respect, each commercial court has adopted its own guidelines with respect to treating requests in relation to restructuring or insolvencies.
- With respect to Paris and Nanterre, for example, it should be possible to request the opening of *mandat ad hoc* or conciliation proceedings (court-supervised restructuring proceedings) by email and telephone and they are considering having at least one day in the week for hearings with respect to commencement of insolvency proceedings (*sauvegarde, redressement judiciaire* or *liquidation judiciaire*). Bearing in mind that it is expected that the 45-day period from the suspension of payments

(*cessation des paiements*) within which a manager should file for *redressement judiciaire* or *liquidation judiciaire* or request the commencement of conciliation proceedings should be extended by at least the duration of the lockdown.

If you have questions about this *Client Alert*, please contact one of the authors listed below or the Latham lawyer with whom you normally consult:

Pierre-Louis Clero

pierre-louis.clero@lw.com
+33.1.40.62.20.21
Paris

Alexander Crosthwaite

Alexander.Crosthwaite@lw.com
+33.1.40.62.20.79
Paris

Olivier du Mottay

Olivier.duMottay@lw.com
+33.1.40.62.23.39
Paris

Jean-Luc Juhan

Jean-Luc.Juhan@lw.com
+33.1.40.62.23.72
Paris

Matthias Rubner

matthias.rubner@lw.com
+33.1.40.62.21.17
Paris

Thibault Burnier (PA)

Thibault.Burnier@lw.com
+33.1.40.62.23.15
Paris

Arthur Rohmer

Arthur.Rohmer@lw.com
+33.1.40.62.23.43
Paris

Eric Loubet

Knowledge Management Lawyer
eric.loubet@lw.com
+33.1.40.62.20.24
Paris

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