Reviewing an SPA: Issue Spotting for Antitrust Lawyers

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On December 17, 2024, the International Committee of the American Bar Association's Section of Antitrust Law hosted a webinar on the role of antitrust lawyers in negotiating and marking up Sale & Purchase Agreements (SPAs). This was the second of a seven-session "Crash Course in Global Merger Control" organized by the International Committee and co-sponsored by the section's Mergers and Acquisition Committee. The series, which will run through the end of February 2025, is designed for junior lawyers and economists interested in international merger control. The series tackles the basics of merger control and review process in general, as well as outlines information specific to various jurisdictions around the globe.

This session explored what an SPA is and what are the particularly important aspects of SPAs that antitrust lawyers have to pay attention to (e.g., risk shifting provisions,

cooperation clauses, closing conditions) as well as provided tips for due diligence and negotiations. Moderated by Ildikó Magyari, an economist at Cornerstone Research in New York, U.S. and adjunct faculty at Columbia University, the panel featured two speakers: David Feldman of Stikeman Elliott LLP in Toronto, Canada and Trudy Dargeviciute of Covington & Burling LLP in London, United Kingdom.

Ms. Dargeviciute began the webinar by outlining the key components of an SPA. One fundamental area is the representations and warranties given by the seller, which provide recourse for the buyer by way of a breach of warranty claim, while facilitating the disclosure of essential information about the target company. The seller also leverages this opportunity to disclose known business problems to limit its liability. To that end, Ms. Dargeviciute highlighted a set of example qualifications for the drafting of representations and warranties that protect the seller's interest by diluting the scope of the warranties and preventing a buyer from exercising recourse too easily and readily: (i) qualification by limiting the statement to the knowledge of the Seller; (ii) qualification by materiality; (iii) qualification by disclosure; and (iv) qualification by time.

Another key component of the SPA is precedent conditions. They specify conditions for closing relating to (i) antitrust and Foreign Direct Investment (FDI) clearances; (ii) regulatory and shareholder approvals; and/or (iii) third-party consents. Ms. Dargeviciute specifically emphasized the Material Adverse Change (MAC) mechanism that allows the buyer to terminate the SPA if certain events that have significant and detrimental effects on the target's business occur before the completion. There is substantial scope for variation in MAC across jurisdictions. For example, in the United States, there is a special principle derived from case law that a MAC must be narrowly construed and that the burden is on the party wishing to invoke it. On the other hand, in the United Kingdom, as exemplified by a recent case, [1] this special principle does not apply, and the MAC is just one of the many risk allocation provisions in the SPA to be applied using the ordinary principles of construction and interpretation under English law.

Ms. Dargeviciute closed her discussion by describing two other key components: covenants and effort clauses. Covenants ensure that appropriate actions are taken or refrained from being taken to facilitate the consummation of the acquisition and preserve commercial value of the target business in the interim period. For example, a positive covenant can stipulate that the buyer and seller must cooperate in a particular and timely manner on regulatory filings. A negative (or a restrictive) covenant can stipulate that a seller cannot undertake certain business decisions that risk eroding the value of the target business without the buyer's consent. Finally, effort clauses define effort levels by the seller and the buyer in achieving stated objectives. According to Ms. Dargeviciute,

attorneys, courts and jurisdictions apply different meanings and different standards to "reasonable efforts", "commercially reasonable efforts", and "best efforts", which can lead to uncertainty in contract interpretation and performance. As such, where possible, it is advisable to define the efforts standard in the agreement to avoid this uncertainty.

During his discussion, Mr. Feldman addressed antitrust risk-shifting considerations related to the key components of an SPA that Ms. Dargeviciute introduced. For instance, the purchaser may achieve greater certainty of the absence of post-closing antitrust risk by stipulating as a condition precedent the absence of pending litigations, injunctions, or any threats tied to regulatory clearance. Similarly, parties can allocate antitrust risk through efforts clauses containing obligations relating to remedies. For instance, the buyer can be required to exert its "best efforts" to remedy any antitrust concerns through some form of divestiture.

Mr. Feldman further explored the inherent tension in the buyer's and seller's interests that underpin negotiations on these key components of an SPA. In the context of information access and regulatory cooperation covenants, for example, the buyer's primary objective is to get access to information from the seller relevant for potential advocacy. On the flip side, the seller seeks to maintain confidential the ordinary course of business to hedge against the deal falling through. In addition, it is in both parties' interest to limit the scope of flushing out of commercially sensitive information, to avoid gun-jumping risk. To achieve this, there is usually an agreement where the seller's competitively sensitive information is shared only with a "clean team" (i.e., a designated group of individuals on the buyer's side removed from direct operational and business dealings such as the chief financial officer) or with an outside counsel. Such practices, as Mr. Feldman noted, also help with mitigating risk of subsequent antitrust litigations.

When it comes to ordinary course covenants, buyer stipulations are usually focused on material contracts and capital expenditures. Mr. Feldman highlighted that the timing of the long-stop date (i.e., the date upon which the buyer and the seller can both walk away if closing is not fulfilled) is salient for these covenants. A protracted plant refurbishment coupled with a restrictive covenant on capital expenditures for example, can severely impact the business viability of the seller's targeted assets in the interim. Most crucially, Mr. Feldman emphasized the need to meticulously review and excavate any potentially gun-jumping and anti-competitive agreements. However, he stated that the standards for gun-jumping agreements can vary substantially across countries and various jurisdictions.

With regard to non-frustration or "clear skies" provisions, sellers generally seek commitments from the buyer group to refrain from engaging in unrelated acquisitions or other activities during the interim period that could complicate or delay regulatory approval for the subject transaction. The buyer on the other hand should be cognizant of

covenants prohibiting conflicting transactions that could hold up the buyer's adjacent business interests. Mr. Feldman cautioned that this is especially important if the buyer is owned by a parent entity or fund where information on related acquisitions is not necessarily immediately visible, and flexibility is of immense value.

Mr. Feldman then detailed the more nuanced considerations relating to antitrust risk shifting and sharing between the parties in an SPA. He discussed that the seller often desires the buyer to bear most of the risk, to be reimbursed for its cost of merger review and compensated with a breakup fee if the deal falls through. On the most seller favored end of the spectrum of possibilities, the seller can also obtain a so-called "hell or high water" provision where the Buyer agrees to "best efforts" in providing any necessary remedy. However, this does not always materialize in an outcome that is completely seller friendly. Mr. Feldman emphasized that jurisdictional context matters: in various jurisdictions different remedies or divestitures may be feasible in theory but can be blocked by regulatory or political bodies. In addition, he added that "best efforts" clause can signal anticompetitive issues to regulatory authorities, which would be to the detriment of the seller as well.

In connection with "control of process" clauses, Mr. Feldman described how shifting all economic risk to the buyer also commonly comes with the seller having to concede control because ownership of risk serves as ground for the buyer taking greater ownership of strategy and decision making in the review and advocacy process. This frequently takes the shape of provisions outlining the buyer's access to seller data as well as full control over communications with authorities. Under these circumstances, Mr. Feldman suggested that the seller ought to negotiate for at least some visibility in the review process because a failure of clearance can have important impacts on the target's subsequent independent business viability as well as the seller's adjacent holdings. In short, Mr. Feldman suggested avoiding a completely adversarial approach and instead applying a meticulous consideration of the tradeoffs involved (mainly because antitrust risk is inherently shared between both parties, with successful clearance and closing ultimately in the collective interest of both parties). Thus, in addition to protecting the represented party, Mr. Feldman emphasized that it is crucial to also focus on cooperative provisions between the buyer and seller pertaining to the likes of timing of filings, nuances regarding filing in various jurisdiction, ensuring there is sufficient time for compliance with investigations and allowing an appropriate buffer for litigation and the negotiation of remedies.

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Washington D.C. The views expressed herein are solely those of the authors, who are responsible for the content, and do not necessarily represent the views of Cornerstone Research.

Endnotes

1. BM Brazil I Fundo De Investimento Em Participacoes Multistrategia v Sibanye BM Brazil (Pty) Ltd EWHC 2566)

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