CLIENT ALERT

A Few Trends and Developments in Belgian M&A Practice

June 2, 2021

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The M&A practice is ever evolving and we have selected and outlined below a few recent legal developments that might be relevant for actors in M&A transactions in Belgium. We will start with some general trends as a consequence of the current health crisis, followed by a highlight of the main findings of the 2021 M&A Survey, and by some questions raised in due diligence in the context of the transition to the new Belgian company law. Finally, we will address the impact of the new Belgian rules prohibiting abusive clauses on M&A transactions, as well as recent examples reminding us about the importance of the directors' confidentiality obligations.

General M&A Trends in Today's Particular Circumstances

The COVID-19 pandemic has had a significant impact on M&A practice in a variety of ways:

- difficulties in the valuation of the target company, since its historical financial figures may not be representative of its future performance and, consequently, the related need to draft earn-out clauses and avoid locked-box mechanisms;
- the growing need to negotiate material adverse change (MAC) clauses;
- a more cautious approach to due diligence (risk-based approach);
- difficulties in the process of negotiation and due diligence investigations in a remote working environment, and delays from regulatory bodies and within financing processes; and

- increased state interventionism (*e.g.* foreign direct investment (FDI) control).

The current crisis might also provide new opportunities for investors. There is, for example, strong interest from investors, whether private or institutional, in life sciences and biotech companies, as well as in the TMT sector. There are also opportunities to invest in distressed companies (*e.g.* in the context of bankruptcy or judicial reorganisation proceedings).

On the other hand, the pandemic has also revitalised classical legal concepts allowing, under certain conditions, for the acquiring party to either walk away from the transaction or to renegotiate some of its conditions (force majeure, hardship, MAC clauses, good faith renegotiation clauses, etc.).

All these consequences of the coronavirus are global and not particular to the Belgian M&A market.

M&A Survey – Notable Evolutions

The fifth edition of the Belgian M&A survey, made by the law firm Contrast, has recently been published. This survey is based on an analysis of around 450 transactions in Belgium between the period of 2016 and 2020 to present the practices and uses in share purchase agreements in the context of company acquisitions. Willkie Farr & Gallagher participated in this survey, as it has done for previous editions.

For most aspects, results are consistent with previous editions and show a stable market practice despite economic and market changes.

However, a few interesting evolutions must be noted:

- a noticeable increase in the use of competitive auction, especially in larger deals (deals with a transaction value of more than 100 million €) where around 75% were preceded by a competitive auction;

- the locked-box mechanism for setting price (*i.e.* no price adjustment based on the situation on the closing date) is heavily favoured compared to price mechanisms based on closing accounts (*i.e.* price adjustment based on the situation on the closing date). However, we might wonder whether closing accounts mechanisms will come back in the future due to the uncertainty brought on by the COVID-19 crisis;

- the use of deferred purchase price payments (including earn-out mechanisms) is steadily increasing. The deferred part of the purchase price usually represents less than 25% of the total purchase price and becomes payable between one and three years after the closing of the transaction;

- a surge in the use of specific insurance policies to cover part of the risk in relation to the representations and warranties, or specific indemnities, can be observed. This tool, which was only used marginally in Belgium previously, is now used more frequently, especially in larger deals (deals with a transaction value of more than

100 million €), where it was reported to have been used in 27% of such transactions. Furthermore, the results show that such warranty and indemnity insurance is particularly used when private equity or venture capital firms are involved in the transaction. It seems that such insurance shall become an increasingly important element in Belgian M&A practice, as it already is in other countries.

Transition Period of the New Belgian Company Law: Some Questions Raised in Due Diligence

In Belgium, the switch since 2020 from former to new company law inevitably raises questions and uncertainties as to which rules should apply to M&A situations that overlap the two regimes.

The Belgian act introducing the new Belgian Code on Companies and Associations (or BCCA) expressly solves many questions concerning the transition period. Other situations, however, are not explicitly discussed and therefore remain debatable.

For instance, when performing due diligence involving contracts concluded before 2020, one could defend today's validity of contractual change of control clauses that were deemed invalid in the past, as well as the absence of liability of a seller of shares in a Belgian private limited liability company (SRL/BV) that have not been fully paid-up.

For further developments in this regard, we refer to our contribution to Chambers and Partners' 2021 Global Practice Guide in Corporate M&A, available here.

Prohibition of Abusive Clauses in M&A Transactions

Introduction

The Belgian Act of 4 April 2019 (the Act), which entered into force on 1 December 2020, introduced a set of rules on unfair or prohibited B2B contract clauses which may have an impact on the M&A process.

These rules are inspired by the existing prohibition of abusive clauses in B2C contractual relationships.

This new Act has a broad scope and shall apply to any agreement between any type of enterprise, concluded, renewed, extended or amended as from 1 December 2020, such as, in the M&A context, share purchase agreements, shareholders' agreements or non-disclosure agreements. It is to be noted that a company's articles of association might be qualified as an agreement (between shareholders) and, in such view, be subject to the Act. As to the concept of enterprise, it may be interpreted as excluding non-profit organizations, as well as natural persons managing their own wealth. This would create uncertainty, for instance, if one party to a (share purchase or shareholders') agreement is a natural person and the other party thereto is a company.

The protection offered by the new rule applies to all enterprises regardless of their size or whether they are in a dependent relationship with their counterpart.

Protection Offered

The Act introduces a general “fairness” principle as well as a “black list” and “grey list” of clauses which are deemed abusive.

According to the general principle, a clause is deemed abusive if it creates, alone or in combination with other clauses, a clear imbalance between the rights and obligations of the parties.

This imbalance must be legal, and not economic, and must be assessed taking into account, inter alia, the general scheme of the agreement or the usual trade practices in the relevant sector. In addition, the Act is not applicable to the core clauses of the agreement, such as the adequacy of the price paid in consideration for the services rendered.

Assessing in each specific case whether such imbalance exists will be challenging, as the legislation is quite vague and will raise complex interpretation issues. However, it can be said that the fact that a clause is simply unfavourable to one party will not be sufficient; a clear and manifest imbalance is needed.

To help with such assessment, the legislation contains two non-exhaustive lists of clauses.

Firstly, the “black list”, which contains clauses that are abusive and prohibited in all cases, no matter the context. This list includes, for example, “potestative” clauses (*i.e.* clauses in which the execution depends solely on the will of one of the parties, for instance, clauses providing that the agreement is “subject to satisfactory due diligence at the sole discretion of the purchaser”). This may raise issues in share purchase agreements or shareholders’ agreements for put or call options exercisable at the discretion of one of the parties, or earn-out clauses if it can be considered that the earn-out price is decided based on the actions of the purchaser, in each case assuming that such clauses cannot be considered “core” to the agreement.

Other “black list” clauses include clauses giving one party the right to unilaterally interpret any clause of the agreement, clauses requiring one party to waive any means of recourse against the other party in the event of a dispute, or clauses that aim to establish irrefutably the other party’s knowledge or acceptance of terms of which that party did not have actual knowledge before the conclusion of the contract.

Secondly, the “grey list” contains clauses which are deemed abusive unless proven otherwise. The proof to the contrary could, for instance, be given by showing the background of the negotiation process. This “grey list” includes, for example, the following clauses (which might impact M&A practice):

- clauses that place the economic risk on a party when this risk would normally be borne by another party, without counterpart. Belgian doctrine has already highlighted that putting such clauses into the grey list is potentially a major source of legal uncertainty in Belgian M&A practice. Indeed, the contractual risk allocation between different parties to a share or asset purchase agreement is a typical and main negotiation topic in M&A deals. So, for instance, the following provisions or mechanisms could, as the case may be, potentially be viewed as falling under this grey list clause: representations and warranties and/or specific indemnities, earn-out systems, material adverse change (MAC) clauses, and fixed price put options;

- clauses that aim inappropriately to exclude or limit the legal rights of a party in the event of total or partial non-performance or defective performance of the other enterprise's contractual obligations. This is a catch-all clause that, as such, potentially impacts Belgian M&A. Indeed, M&A contracts frequently contain clauses limiting or excluding liability, such as liability caps or thresholds, specific time limitations for claims, force majeure clauses, or also "exclusive remedies" clauses. All such clauses could potentially fall under this grey list clause, although there is room for uncertainty, given the unclear wording of the clause;

- clauses that purport to tacitly extend or renew an agreement of definite duration without providing a reasonable notice period. Parties to such agreement (*e.g*. a shareholders' agreement) could therefore usefully provide a reasonable notice period in which each party can refuse any renewal or extension, as well as a reasonable notice period once the contract has been renewed or extended, respectively; or

- clauses relating to the duration or termination that do not provide for a reasonable notice period. With respect to contracts concluded for a definite duration (*e.g.* shareholders' agreements or non-disclosure agreements), this is a big, and controversial, change in Belgian contract law. Strictly speaking, it could basically mean that any such contracts could now (a) be terminated at any time, even after a few months, by one party by merely complying with a reasonable notice period, and/or (b) be declared null and void for not having provided a reasonable notice period to enable unilateral termination. Although this new rule is strongly criticized in Belgian doctrine and eventually may be declared unconstitutional, it nevertheless so far exists.

Keeping in mind that, even if a clause is not included in one of the two above-mentioned lists, it may still be considered abusive on the basis of the general principle.

Sanction

In the event a clause is deemed abusive, that clause shall be declared null and void, meaning that the agreement as a whole will remain enforceable with the exception of the abusive clause (save as otherwise provided in the agreement).

What To Do

These rules must be taken into account in the negotiation and drafting of agreements at every step of an M&A transaction.

If the agreement is subject to Belgian law, the Act, as mandatory law, cannot be excluded by the parties; any provision to that effect shall be deemed unenforceable and even if the parties decide to choose the law of another jurisdiction, the control by the Belgian courts of this aspect of the agreement may not be completely excluded.

Accordingly, it may be prudent to document the negotiation and drafting process to be able to prove, in the event of a dispute, that the clause in question is not, in this specific context, abusive and that there is no imbalance in this case.

This may be done by keeping a record of the different drafts of the agreement and keeping track, as far as practicable, of the requests made by each party, as well as the concessions made in return. Furthermore, the preamble of the agreement may include an explanation of the motivation of each party, as well as of the general context of the transaction.

While these steps are certainly useful, these rules are still untested and it remains to be seen how these provisions will be applied by Belgian courts and whether they will be sufficient in the event of a dispute. Since this Act creates a lot of uncertainty as to what shall constitute an abusive clause, there is a risk that disputes shall arise with respect to its application and interpretation and that it may be used by parties to try to escape their contractual obligations.

Directors' Confidentiality Obligations

In an M&A process, it is also worth noting that, independently of any contractual confidentiality undertaking, the directors must be very careful to avoid breaching their duty of discretion.

Illustrative in that respect is a recent French decision (Paris Commercial Court, 10 November 2020).

M. X, director of the French listed company SCOR (representing SCOR's shareholder COVEA), has been provided, in his capacity of director attending various meetings within SCOR, with confidential information relating to a possible merger of SCOR with a competitor.

M. X is also "PDG" of COVEA, which was then working on a possible takeover bid on SCOR. M. X. decided to communicate this confidential information to his team within COVEA, as well as to the investment bank assisting COVEA in the preparation of such possible takeover bid on SCOR, with the view of accelerating the launching of the takeover bid and bypassing the project of merging SCOR with a competitor.

Without going into all the details of the case, it is interesting to underline that the tribunal held that M. X breached his duty of discretion and sentenced him to pay an indemnity amounting to around 500.000 €, as well as, jointly with COVEA, an indemnity of around 20 million €, with COVEA being sentenced for participating in the breach of the director's duty of

discretion. An investment bank assisting COVEA has been sued in the UK, with SCOR alleging that it has violated its confidentiality obligation, as well as the business secrets of SCOR. Finally, M. X is also being prosecuted before the criminal tribunal of Paris for “breach of trust” (*abus de confiance*).

The consequences of a breach of discretion within the framework of an M&A transaction can be very heavy!

As a reminder, under Belgian law and besides any contractual obligations, each director has, in addition to its general obligation of good conduct, a duty of loyalty that implies, inter alia, a duty of discretion. According to such duty, board members may not use the information obtained in their capacity as board members, for purposes other than for the exercise of their mandate.

Such duty of discretion applies, in principle, vis-à-vis any third party. Should the director represent, *de facto*, a shareholder, it is nevertheless acknowledged that the director may communicate to the shareholder that he/she is representing certain information, to the extent that such communication is required, to allow the shareholder to provide the director with instructions to participate in the deliberation of the board, or to control the way the director is performing his/her mandate. In any case, it remains strictly forbidden to communicate confidential information, should such communication breach public order rules such as market abuse regulation.

More generally, board members should handle the confidential information received in their capacity as board members with the utmost care, and disregard their personal interest in the use of such information.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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