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BREXIT AND M&A: THE FINAL ROUND

On March 25, 2019, ***The M&A Lawyer*** *spoke to Matt Evans, a partner in Jones Day's London office, and Philipp Werner, a partner in Jones Day's Brussels office, on M&A and antitrust implications for the United Kingdom leaving the European Union (just as this issue went to press, the EU agreed to a six-month extension for Brexit).*

M&A Lawyer*: It's an unanswerable question at the moment, but let's try: where do things stand now? What are the most likely scenarios you're seeing, in re the UK and Brexit, as of today?*

Matt Evans: That's the million dollar question. At the moment, as things stand, the UK is leaving the European Union on the 12th of April, unless the UK Parliament approves the withdrawal agreement negotiated in Strasbourg between the UK and the EU 27 or the EU 27 agree to extend the date on which the UK is scheduled to leave the EU. There have been two votes so far and it's been rejected by Parliament twice [since this interview, it has been rejected a third time]. In the absence of a vote on that deal, then the UK will leave the EU on the 12th of April unless Parliament comes up with an alternative plan, which it can then discuss with the EU 27 to enable a further extension to the discussions. But if the withdrawal agreement is passed by Parliament, the UK will leave by the 22nd of May, which is the deadline the EU 27 has given the UK to enable it to pass the necessary legislation to implement the withdrawal agreement.

MAL: "No deal" at one time seemed like a worst-case scenario. Now it's seemingly one of the few options left.

Evans: It is certainly a possibly and it looks to be a greater possibility than it appeared six or seven weeks ago. We should remember that the UK Parliament has voted to prevent a "no deal" exit but it's not clear how it could do that, should the Theresa May deal be rejected.

MAL: So for parties planning upcoming mergers, whether it's cross-border or internal to the UK, what sort of things should these companies and their advisors be expecting?

Evans: The easy one to deal with is if the withdrawal agreement is passed and the UK leaves the EU in May. In that case, there will be no change in the filing requirements and treatment of mergers until the end of 2020.

The more complicated scenario is if the UK leaves the EU without a deal. The first thing to be aware of is that the European Commission will no longer act as a merger control one-stop shop for mergers between large companies as regards the UK. In addition to the European Commission, the UK will also now have its own jurisdiction, so one may find parallel merger reviews being done by the [UK's] Competition and Markets Authority (CMA). From the EU perspective, the European Commission issued a communication on 25 March on how they would deal with antitrust cases in case of a no-deal Brexit.

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If your deal hasn't yet been signed, the assessment as to whether it meets the EU revenue thresholds may change. It may be advisable for companies to start discussions now with the CMA, seeing if their deal might raise competition concerns, and whether the UK might want to look at that deal. Many of these discussions are happening every week now. The CMA has set up a parallel review team and are gaming current EU mergers and scenarios.

Another thing that merging companies should be aware of is that on exit day, even if they've already notified their deal to the European Commission, the UK is reserving its right to open a post-exit day investigation into that deal. You might think that as the UK is still a member of the European Union, there's no risk that the UK authority will open a review into that deal. But you should remember the quirky voluntary nature of the UK regime. The UK has the right to review a completed deal four months after the deal's completion. So you could find yourself, even though you notified your deal to the European Commission prior to exit day, learning two months later that the UK authority has the right to open a review into that deal. So it's important to be discussing deals with the CMA at this point.

Philipp Werner: If a deal fits the EU-wide market definition and doesn't raise problems and the EU agrees that the market is EU-wide, would the CMA agree normally that's the proper geographic market definition? Or do you think after Brexit, they would look at the UK market?

Evans: That's a good question. If the UK leaves without a deal and that gives rise to tariffs, some sort of customs duty on trade, between trade for the EU and UK, then we could see market definition changing—seeing the UK taking a different approach and identifying more markets as being UK-wide. We anticipate in the event of a no-deal exit relevant geographic markets under UK merger control becoming narrower and being more likely to be confined in the UK, especially if there are tariffs on trade between the UK and the European Union.

MAL: Are there any indications as to what's going to be changing with the CMA post-Brexit, regardless of the type of exit?

Evans: There have been some speeches by senior CMA figures about what the CMA may see changing in terms of UK merger control. A number of ideas have been proposed. One is for a move potentially to a mandatory merger filing system for deals that exceed a certain threshold, whether it's a transaction size test, like under the U.S. Hart-Scott-Rodino Act, or some sort of higher revenue threshold above which deals notification will be mandatory. The CMA have already significantly increased the number of staff they have, as they expect a 30%-50% increase in the number of merger notifications in UK. They've been on a recruitment drive and continue to build numbers in order to cope with what's expected to be a bigger workload.

From a UK perspective, the most radical proposed

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change would be mandatory filing for certain deals. The purpose for that would be to provide certainty both to the CMA and merging parties, particularly for deals being looked at by a number of regulators around the world, like the European Commission and FTC or DOJ. The CMA will be looking at the same deals, at the same time, and they will likely discuss any potential impacts with their fellow regulators in the hope everyone can reach some common view.

MAL: Do you see the tendencies of a post-Brexit antitrust regime in the UK to be more aligned with U.S. antitrust, or will it have more affinities with the European regime?

Evans: In merger control, I'd say the UK is already closer to the DOJ/FTC than it is the EC. The UK tends to take a more economic approach to merger control than the EC does. The UK is not particularly interested in market definition. It views it as a useful tool to frame investigations but it's not particularly wedded to it and not particularly hung up on market shares. What it focuses on more, particularly in mergers between competitors, is closeness of competition. I think that is more akin to the approach taken in the U.S., while in the EC, market shares still play an important role in merger review.

Werner: I'd agree with that, even though the EU and other countries in the EU are also adopting a more economic approach. Without the UK, and under the German and French influence, the EU could possibly move a bit away from that approach, so that there would be a gap between enforcement in the UK and the EU because of changes in the EU.

Evans: In antitrust generally, again in the UK, economics plays an important role in antitrust enforcement. I would expect over time to see a divergence from the EU antitrust regime, in particular from one important element of the EU regime, which is the political considerations to protect the integrity of the single market: the idea that customers should be able to obtain goods and services from someone thousands of miles away, on the other side of the European Economic Area, just as easily as they can from a supplier down the road. The idea is that "we're one big market without borders." So there are areas of antitrust driven by that sort of political imperative.

Over time I would expect there to be a loosening or even a removal of those considerations from the UK law, because the UK will not have the same political imperatives. Those laws that dictate when, say, a supplier can restrict their reseller from selling across borders in the European Union, or what kind of restrictions there are on online sales. That was always driven by single market imperatives and not necessarily by economics.

MAL: In terms of other CMA/EU divergences, what else could be expected from a post-Brexit CMA's take on future deals?

Evans: One main change will be in analysis. There's a potential change in market definitions and therefore consideration of how many competitive constraints a party would face if they decide that the UK is the relative geographic market, rather than the European Economic Area. There may be another practical consideration, which is that the UK has an incredibly extensive power to intervene in markets it thinks don't work effectively for consumers. This is their "market investigation" power. They can launch studies into particular markets, and put participants to great cost in responding to requests from information to help the CMA understand how those markets work. And at the end of that review, the CMA may take the view that although no one's infringing antitrust laws, there are still features of this market that don't work well from a competitive point of view, so they're still going to take radical action. The most radical action they'll do is break up companies, even though those companies haven't broken any laws.

We anticipate that the CMA may be reluctant to open such investigations currently because they are very resource-intensive. The CMA expects such an increase in merger control and cartel investigations as a result of Brexit that it may not have resources to undertake these extensive and potentially intrusive market investigations. But over time, they may well do just that. That's the sort of tool they may ultimately use to review, and if necessary to break up, big tech giants, for example: a big topic in antitrust circles at the moment.

MAL: There have been recent cases where the CMA exercised its authority to go after consummated transactions, such as giving unwinding orders.

Evans: There are two ways in which the CMA has used

its powers in completed mergers. The first is that CMA has the power to unwind premerger integration pending the outcome of a UK merger control review. They used that power for the first time recently in a transaction involving the Swedish company Tobii and its target Smartbox. In this case, the parties as part of their pre-deal discussions had appointed each other as their distributors, the target agreed to stop distributing some product lines, and they entered into other related agreements so as to make integration run more smoothly. The CMA opened a Phase 2 investigation and has ordered the companies to unwind some preliminary steps they'd taken, so Smartbox must reintroduce some product lines, for example. So that's one way in which the CMA can intervene.

The more radical way is that the CMA may actually prohibit the deal: they could force the unwinding of a deal if necessary, with a fire sale of the acquired or acquiring business. The CMA has used that power in a number of mergers over the years. They used it in a very niche area in relation last year to [a merger of two companies that] supply and manage laundry services to higher education providers. They opened a Phase 2 review, prohibited the deal, forced it to be unwound. A much more high profile case was a [2016] vertical merger where ICE acquired Trayport. Trayport is used by most brokers, and that deal was prohibited—ICE had to unwind that deal.

Werner: There's one other thing that clients need advice on regardless of the final shape of Brexit, and that concerns their European-wide distribution systems, including bricks and mortar shops and e-commerce. Many companies have tried to create a uniform distribution system across the EU and also have uniform compliance programs across the EU. Now they may have to think whether or not to maintain that system following Brexit. Because even if the rules remain the same, in terms of the main aspects of vertical relations post-Brexit, the single market imperative may not remain in place. The question becomes can a supplier impose more restrictions on UK distributors, as compared to the rest of Europe?

Evans: Yes, that's a question we're advising on weekly for U.S. clients, particularly brand owners. If the UK leaves the EU without a deal, there may be some scope to put certain barriers and protections around UK trade which could result in cheaper or more expensive trade without spilling over into impacting resale strategy in the rest of Western Europe.

MAL: Given the ongoing uncertainty about what actually will happen with Brexit, has that had an effect on UK M&A volume?

Evans: The data suggests that the volume of M&A activity in the UK is down considerably in the first quarter as compared to last year, which was already a poor year. So it's fair to say the uncertainty is significantly impacting on M&A activity. We have seen in the past few weeks an uptick in interest from U.S. investors in the UK economy, because ever since the [2016] referendum the pound has dropped quite a bit, so I think some investors are seeing good value in the UK and are willing to invest.

MAL: Is there anything else to keep an eye on as Brexit enters its (presumably) final stages?

Evans: Another area of antitrust enforcement which is relevant for companies buying UK companies is state aid. It's a standard question in due diligence to know if the target business has received government aid or aid from a state resource within the EU, what the terms of this aid are, and what are the risks that it might need to be repaid. We've seen in due diligence sometimes that aid is granted under the requirement that the recipient is to be an establishment in the EU. So it's worth checking. The UK is introducing its own state aid regime that will mirror the EU's regime, so from a practical point of view, the only change is one will now go through the approval process with the UK, rather than the EC. But you need to check the terms on which aid was granted to ensure there's no risk of that aid needing to be repaid.

Werner: It's going to be interesting to see how this state aid regime works in the UK. One reason why [countries] have established supranational regimes is that governments find it hard to commit to not grant certain types of subsidies to their national companies. There's always the issue that they feel forced by political pressure to do that. In the EU, it's the European Commission who stops governments from doing that.

Evans: The most important thing for companies and

advisors in the next few months, whether it's a UK target or UK sales, is that although you may have done your merger control jurisdictional assessment early on and have a good idea where you need to file (and may have incorporated that analysis into your deal terms), it will be really important to redo that assessment and game it again, on the assumption that the UK is leaving the EU and that it may happen before you close your deal. You may find your deal no longer meets the EU thresholds. That means some uncertainty of timetable and possibly greater costs. If the transaction would interest a regulator such as the UK, then go and speak with authorities now and tell them about the deal and gauge their appetite for reviewing it. You don't want any unpleasant surprises.

MAL: Would you say that most companies are taking the right steps and are fully aware of Brexit's implications by now?

Evans: Large international companies will be on top of this and acting accordingly. There will always be some companies who are less used to dealing with regulators and who may not have thought through the implications. But for the big internationals, Brexit is just an added cost to doing a deal. If there needs to be a parallel review in the UK, it's just an additional regulatory hurdle to a deal that's already subject to many regulatory hurdles. It will cost a bit more; it can add some more time to a deal's timetable. But for a company with less experience in front of the regulators, it could have a disproportionate impact on their planning and costs.

MAL: If a company's determination to file in the EU was based on EU-wide revenue, and suddenly you take out the UK, does the EU Commission still have jurisdiction if you fall below the threshold—what happens to those deals? Do you have to refile?

Werner: Yes, people have to take into account if you're just barely above the threshold and the requirement in the EU depends on your UK revenue, you may well need to make alternative plans. If you're in the planning stages, Brexit happens and then you notify, it could become a problem. You may have to see whether to you need to go to one or two national authorities.

MAL: What does this change about EU review: will there be less EU-wide filings or more country filings?

Werner: Theoretically there could be fewer filings, although filings to the EU are so big that they typically don't depend on UK turnover being added. I think in the near future there will be no change in the review process. But in the medium and long term, there may be some shift away from the more economic approach that the UK advocated and more towards either the structural approach that the Germans have used traditionally, or a more political approach that the French would like to see. Some [in the EU] may be looking with sadness at the UK leaving, because there are different tendencies in antitrust, and they believe that the UK stood for a liberal, more economic approach as opposed to some other countries in the EU.

DUMPING A DEAL AFTER THE DROP-DEAD DATE: NO DUTY TO WARN IN DELAWARE

By Michael Darby

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On March 14, 2019, the Delaware Court of Chancery ruled that rent-to-own industry leader Rent-A-Center had validly terminated its $1.36 billion deal with private equity firm Vintage Capital. Rent-A-Center abandoned the deal by notifying Vintage after the outside termination, or "drop-dead," date in the merger agreement had passed. This provision allowed either party to terminate the deal if antitrust approval had not been obtained within six months of the June 17, 2018 signing date. Although Vintage could have extended the drop-dead date beyond December 17, 2018, the Court determined that it had not properly provided Rent-A-Center with the necessary extension notice. The Court held that Rent-A-Center had validly exercised its right to terminate the deal, despite the fact that Vintage was under the impression, based on the parties' actions up until that date, that Rent-A-Center was otherwise proceeding to close the merger after the drop-dead date.

Background

In June 2018, Rent-A-Center agreed to be acquired by an affiliate of Vintage Capital. The parties anticipated that the