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Do Not Be Afraid Of The French M&A Process

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Foreign buyers engaged in a merger and acquisition process concerning, directly or indirectly, a French target are frequently worried by the involvement of the French works council (comité d'entreprise). This is the case because share purchase agreements triggering a change of control in a French target may not be executed until the French works council information and consultation process is completed, which may take up to three months.

In addition, since July 2014, M&A transactions — where the sale of more than 50 percent of the share capital of a French company is contemplated — may not close before French employees have been informed of the contemplated sale and afforded the right to make an offer.

Both mechanisms have commonly been viewed by foreign buyers as significant hurdles when engaging in a French transaction, capable of derailing the process or at least significantly delaying it.

Recent regulation has, however, taken up these criticisms and laid down a much less constraining legal framework. Practitioners also have crafted specific solutions to ensure that acquirers and sellers are bound during the works council consultation process with an aim to achieve deal certainty.

Involvement of the Works Council in a French M&A Transaction

Share purchase agreements involving a change of control in a French target may not be executed until the French works council information and consultation process is completed, which may take up to three months. Practical solutions exist, however, to bind acquirers and sellers during the process and achieve deal certainty.

Which French companies have a works council?

A works council is mandatory in every French company having a minimum of 50 employees during 12 months (whether consecutive or not) over the preceding three years.

How is the French works council involved in the context of an M&A transaction?

The works council must be informed and/or consulted with regard to the general organization, management and operation of the company.[1] More precisely, information and consultation of the works council is required with respect to decisions regarding a change in the economic or legal structure of the company (article L. 2323-19 of the French labor code). This includes, as a matter of example, the sale or acquisition of a subsidiary or branch of a French company.[2] A change in the legal structure of a French company includes also a change in the control of the company itself. As a consequence, the works council of a French target must be informed of and consulted upon an M&A transaction involving a change of control in a French target.

What form must the information and consultation of the works' council take in the context of an M&A transaction?

The process is twofold. First, the employer must make available to the works council information regarding the contemplated transaction. Based on this information, the works council is then consulted on the proposed transaction. At the end of the consultation process, the works council hands down a favorable or unfavorable opinion.

When must the works council information and consultation take place?

With respect to changes in the economic or legal structure of the company, the works council must be informed and consulted prior to the implementation of the decision. With respect to M&A transactions where the target is a French company, this means that the share purchase agreement may not be executed[3] before the works council has been informed and consulted, i.e., before it has handed down its opinion. Otherwise, the target's management could face sanctions, the works council could try to delay the transaction until the opinion is handed down, and the new shareholder could face difficulties dealing with the works council in the future.

What is the timeline for the works council to hand down its opinion (when may the share purchase agreement be executed)?

Until recently, no timetable was set for the works council consultation period. As a result, it could delay its opinion by several weeks or months. This meant that prospective transactions could be significantly delayed or even blocked by the works council.

Since the end of 2013, French law provides for a fixed one-month consultation period starting from the date the employer (the French target) has provided the works council with the necessary information.[4] Before handing down its opinion, the works council may request additional information and/or the appointment of an expert or accountant tasked with assisting it to assess the information provided by the employer. If an expert is appointed, the consultation period is set to two months.[5]

Once the consultation period has expired, the works council is now deemed to have been properly consulted and to have issued a negative opinion.

May the share purchase agreement be executed before the works council is informed and consulted if it includes a condition precedent that the consultation will be completed before closing?

Practitioners usually strongly advise against such solution on the grounds that the opinion of the works council must, at least in theory, be taken into account and may thus weigh on the terms of the

contemplated transaction. If the share purchase agreement is executed with a condition precedent, regardless of the works council opinion, its terms would likely not be amended.

How may an acquirer or a seller achieve any certainty and bind the other party during the information and consultation process?

Since the share purchase agreement may not be executed prior to the French target's works council being informed and consulted, the seller(s) may not enter with the acquirer into a binding sale and purchase agreement.

For the parties, the solution is usually twofold.

First, the acquirer grants a put option to the sellers on their French target shares. The unexecuted share purchase agreement is annexed to the put. The put may be exercised for a duration (usually two to three months) limited to the time required for the target's works council to hand down its opinion. Once the information and consultation has been completed, the put is exercised. Upon exercise, the share purchase agreement annexed to the put is executed.

Second, the sellers grant an exclusivity to the acquirer for a sufficiently long duration such that they would not be enticed to look for other offers. Breach of exclusivity would give right to liquidated damages on part of the sellers and/or the target. In addition, breakup fees may be agreed to if the sellers do not (1) cause the French employer to properly and timely conduct the information/consultation of the works council or (2) exercise the put despite completion of the works council consultation process. Breakup fees are not standard and may put the sellers/target management at risk vis-a-vis the works council depending on the amount of the breakup fee. Such would be the case if, given the amount of the breakup fee, the sellers/target management had no choice other than to exercise the put and execute the share purchase agreement.

The sellers are protected by the put. During the course of the consultation process, the acquirer may not walk away and once the put is exercised the acquirer is bound by the share purchase agreement.

What type of information must be provided to the works council?

The employer (the French target) has the duty to provide all necessary information required by the French labor code to support the consultation by the works council. In the context of an M&A transaction, information to be provided does not include the draft share purchase agreement or its terms and conditions, including with respect to price. Information usually focuses on the identity of the acquirer and its group, the general strategy it is pursuing and information as to a potential changes in working conditions. Works councils also frequently ask for clarity as to whether the transaction will result in a decrease in workforce or restructuring of the enterprise. Finally, the works council may ask to hear the acquirer's representatives.

Is the acquirer compelled to take undertakings vis-a-vis the works council?

The works council may ask for undertakings by the acquirer. These may include commitments not to proceed with redundancies of French employees for a defined period of time or to develop certain businesses in France. The acquirer is not compelled to take any commitment vis-a-vis the works council, including with respect to job preservation or future developments.

What if the works council hands down a negative opinion?

The opinion of the works council's is not binding on the employer or the acquirer. Even in case of a negative opinion on the contemplated transaction, the put may be exercised and the share purchase agreement executed.

Are the members of the works council bound by confidentiality obligations?

Members of the works council are bound by confidentiality obligations. In several instances, it has been noted, however, that these are not fully complied with. As a consequence, upon the start of the consultation process, to avoid any risk of unprepared disclosure to the market, public buyers usually tend to announce the entry into negotiations regarding a prospective acquisition of the French target.

Are there ways to avoid the involvement of the French works council?

The general opinion is that if the management of the French target is not involved at all in the M&A transaction, then the share purchase agreement may be executed without the works council first having been informed and consulted. In practice, this is rarely the case because the management of the French target is involved at least in setting up the data room.

If the target is a foreign company holding a wholly owned French subsidiary with a works council, must the French works council be consulted?

Current case law rules that a mere indirect change of control does not trigger the obligation to inform and consult the French target's works council, provided that the transaction does not entail modifications to the management, capital structure or business of the French company.

If the target is a pure holding company conducting no operational business and holding shares in a French company only, the general view, however, is that the works council must be informed and consulted. The reason is that this type of indirect change of control will have for French employees consequences similar to that of a direct sale of the shares of the French company.

The situation is less clear if the target is a pure holding company but carries holdings in several companies. In these situations, a case-by-case analysis needs to be conducted, and information and consultation of the works council may be required if (1) the indirect change of control results in a change in management, capital structure or business of the French company, (2) the French company's management is involved in the negotiation of the transaction, or (3) the transaction affects the employees (number of employees, working conditions, etc.).

Offer by French employees

Since July 2014, M&A transactions — where the sale of more than 50 percent of the share capital of a French company is contemplated — may not close before French employees have been informed of the contemplated sale and afforded the right to make an offer. Practical solutions may exist, however, to prevent this legislation from delaying the M&A process.

Are all French targets concerned?

The legislation applies only to small and medium-size French companies incorporated under the form of

a limited liability company (société à responsabilité limitée) or a stock company (société par actions, including the société anonyme and the société par actions simplifiée).

Small and medium-size companies are defined as companies that are (a) not required to set up a works council (in summarized terms, companies with less than 50 employees) or (b) required to set up a works council, provided that (1) they have less than 250 employees and (2) at close of the preceding fiscal year, their annual turnover does not exceed €50 million or their total balance sheet does not exceed €43 million.[6]

Are all M&A transactions covered?

The application of the 2014 law is triggered by any sale in a single transaction by one shareholder[7] of more than 50 percent (including equity securities) of the share capital.[8]

Are intragroup transactions concerned?

This remains unclear. Out of an abundance of caution, given the sanctions, it may be advisable to comply with the process even in the context of intragroup sales.

Does the identity of the seller or the buyer matter?

No, except where the transactions involve two companies of the same group (see above). The relevant criteria mentioned above are assessed at the level of the French target only.

How does this law impact the timeline of an M&A transaction?

In companies without a works council, information on the contemplated transaction must be given to each employee no later than two months before the expected date of ownership transfer. In other words, closing of the contemplated transaction may not occur prior to the earlier of (1) the expiry of a two-month time period from the date at which information was provided to all employees or (2) as described below, the date at which all employees have expressly waived their right to make an offer.

In companies with a works council, the information must be given no later than at the start of the information and consultation of the works council with respect to the contemplated transaction. In other words, information must be given to employees before execution of the share purchase agreement. In addition, closing of the transaction may not occur prior to (1) the expiry of a two-month time period from the date at which the information was provided to all employees or (2) waiver by all employees of their right to make an offer.

What information must be given to employees so they can make an offer?

Information provided to employees is very limited in scope. Employees need only be informed: (1) of the circumstance that a sale is contemplated and (2) that they may, at their option, make an offer to purchase the target shares. No other information needs to be disclosed, including with respect to the target itself or the potential transaction, whether it be its terms and conditions or the identity of the potential acquirer.

How must the information be given to employees?

Any means may be used.[9] The information process will, however, be deemed complete only if the company holds evidence that each company employee has been informed of the contemplated transaction. To avoid situations where employees would refuse to acknowledge receipt of the information, recent regulatory changes provide that, if informed by way of a registered letter with an acknowledgement of receipt requested, the employee is deemed informed as of the date of first presentation of the letter (whether or not the employee has accepted the letter).

What is the period of time opened to employees to make an offer?

Each employee may make an offer during a two-month period of time starting from the date at which he or she has received the information regarding the contemplated transaction.

May employees waive their rights to make an offer?

Employees may waive their rights to make an offer once they have been informed of the potential transaction. Early waivers before any information has been provided to employees would likely be invalid. Closing of the contemplated transaction may occur prior to the expiry of the two-month time period if all employees have waived their right to make an offer.

Must the seller(s) accept offer(s) made by employees?

No. All employees may submit an offer but no employee benefits from any preference or priority right. The seller is free to accept or refuse employees' offers, even if on better terms.

May the share purchase agreement be executed before employees have been informed?

In companies with a workers council, no. This is the case because (1) employees must be notified of the contemplated transaction no later than at the start of the works council consultation process and (2) the share purchase agreement may be executed only at completion of the works council consultation process once it has handed down its opinion.

In companies without a works council, literally, the information must be given to each and every employee no later than two months before the date of transfer of ownership, i.e., closing of the share purchase agreement. Information could, thus, be given to employees after execution of the share purchase agreement. This option could abide by the spirit of the law provided that two protections are built in the share purchase agreement.

First, it must provide that closing may not occur prior to the earlier of expiry of the two-month period opened to employees to make an offer or waiver by all employees of their right thereto. Second, it should provide that the seller may accept any offer made by employees. If this option is chosen, the acquirer should ask for significant breakup fees, which the seller should likely accept. This solution would significantly reduce the timeline if the share purchase agreement is subject to conditions precedent, regulatory or otherwise: the two-month time period running until closing will be used to satisfy these conditions during which time employees may make offers (if they did not previously waive their right to do so).

If the target is a foreign company holding a wholly owned French subsidiary, does the law apply?

In case of an indirect transfer of a French target, the law does not apply.

What are the sanctions?

Initially the law provided that failure to comply with these obligations could lead to the nullification of the sale. In 2015, the French Supreme Court ruled that any sanction should be capped at 2 percent of the sale price. This solution was enacted in August 2015.

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[1] The works council is also in charge of all cultural and welfare activities within the company (e.g., preferential fees for cultural activities granted to employees, allocation of "holiday checks," which are partly funded by the workers council, etc.).

[2] Other prerogatives regarding the organization of the company include, as a matter of example, projects resulting in a decrease in workforce or restructuring of the enterprise, implementation of new technologies in the workplace, change in working conditions, working hours, etc.

[3] And not only closed. Signing an agreement subject to the completion of the works council information and consultation process would be viewed as a violation of the existing legal provisions (see below).

[4] In the absence of any other agreement in the duration of the consultation period that may be negotiated between the employer and the works council.

[5] The one- and two-month time periods are extended to three months in case of consultation with one or more health and safety committees.

[6] On a company basis, not a consolidated basis.

[7] A sale of a majority of the share capital by more than one seller, when none of them holds the majority of the share capital, does not trigger the application of the law, nor does (except in the case of fraud) the sale over time by one seller of the majority of the share capital.

[8] Also concerned asset deals concerning business going concerns.

[9] Such as (1) an information meeting with employees executing an attendance sheet, (2) information displayed on a board with list executed by employees having read the display, (3) registered letter with acknowledgment of receipt or (4) e-mail with acknowledgment of receipt, (5) letter handed directly with the signature of the recipient, or (6) any other means certifying the date of receipt by the employee.