Chapter 3

Legal, Financial, Social, and Political Interdependencies with Cross-Border Integration

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Chapter Learning Objectives—In This Chapter, You Will Learn:

➤ An introduction to the macroeconomic, legal, and social impacts on cross-border M&A and integration
➤ Recent regulatory, tax, and political concerns that are impacting cross-border carve-out and integration activity
➤ What integration teams should look out for to avoid some of the pitfalls, some of which can be very public and value destructive

Chapter Summary

This chapter introduces the key legal, financial, social, and political influences on, and implications of, cross-border mergers, acquisitions, and divestitures. It puts cross-border M&A programs in context within and between the jurisdictions and societies where the companies operate.

Introduction

M&A is a complex world. From negotiation, valuation, and rationale, through to completion and integration, we are reminded with each transaction that every deal is different, and each integration will require specific skills and face different challenges. However unique the deal may be there are always numerous interjurisdiction, macroeconomic, and social variables surrounding transactions that affect not only the deal itself but also the success of the subsequent integration program.
Figure 3.1 illustrates that generically these factors impact the transaction, which of course will shape the objectives and specifics of the integration, which in turn will have legal, financial, social, and possibly political ramifications. This chapter provides an overview and introduction to some of these factors under the four groupings noted above; namely legal, financial, social, and political, and how they impact and influence M&A deals and integrations.

Well-prepared companies will have an understanding of this causal cycle in relation to the specific factors relevant to potential deals within target jurisdictions, plan accordingly, and be prepared to adapt the deal structure, deal objectives, or integration plans as necessary. Local factors are likely to be well understood, but where a company is acquiring or operating for the first time, or expanding or changing the nature or scale of its business in a foreign jurisdiction, extra attention is needed to ensure a comprehensive understanding of the potential requirements and pitfalls.

Companies headquartered in countries with well-developed legal and regulatory frameworks may find those of other countries ambiguous or worse—this should not preclude M&A activity in such markets, but a risk-based approach to the deal synergies and integration planning is advised, and allowance for the unknown is prudent. Global PMI Partners asked M&A professionals, with collective experience of cross-border integration across 36 different countries, which geographies had the highest and lowest levels of legal, regulatory, and political challenges. The weighted average results are given in Figure 3.2, showing China and India with the most cross-border challenges and the United Kingdom and Australasia with the least.

In the rush to get deals signed, some of the influences and implications can be overlooked or bad assumptions made about them. Case studies on failed cross-border M&As are littered with examples of such failures to recognize and act upon what in retrospect are relatively simple oversights. These can cause risks and issues during integration, erode or destroy deal
synergies or, at worst, materially harm the reputation and the market position of the combined business. For this reason, professional advice and support should always be sought, for both the hard (legal and tax) and the softer (political and social) interdependencies referenced in this chapter.

In this chapter an attempt is made to describe the four factors and trends separately for simplicity; however, as Figure 3.3 illustrates, these should not be taken independently, nor should they be seen as exclusively one of these categories. Together they provide the context within which cross-border deals are done, the complexity that surrounds such deals, and some of the implications for integration. They highlight global trends that can precipitate international cooperation, change laws, form public opinion, topple politicians, and affect jobs and lives.

For example, taxation is a financial matter within a jurisdiction, yet the implications of tax differences between states, government incentives on the
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national or regional level, and tax departments’ judgments and exemptions are the key determinants of deal structures and optimal legal entity structures. As the level of media coverage and subsequent legislation in America around “tax inversion” has shown, legitimate corporate M&A activity designed to optimize taxes can have huge public and political ramifications as well, putting M&A on the front pages of tabloid newspapers all around the world and putting taxes on the political and social agenda in many countries.

**LEGAL IMPACT**

When it comes to mergers and acquisitions, there are many basic legal and regulatory aspects that need to be considered, but the focus will be on these three:

- Deal structure and legal entities
- Competition
- Sector-specific regulation
In Global PMI Partners’ 2015 survey on cross-border integration, corporate law and sector-specific regulation were the top two areas impacting the integration of the respondents’ cross-border deals.

**Deal Structure and Legal Entities**

Cross-border acquisitions can be structured in different ways according to the commercial objectives of the acquirer, and these can have major implications on the subsequent integration program. First, business deals can be structured as either asset deals, where specific assets and liabilities are purchased, or stock deals, where the owners’ shares of the legal entity are traded.

**Asset Deal.** The seller retains the legal entity and the acquirer purchases specific tangible or intangible assets such as manufacturing facilities, offices, equipment, licenses, contracts, intellectual property, brand rights, or inventory. Asset sales can provide specific tax benefits and increase cash flow, while minimizing liabilities transferring with the sale.

**Stock Deal.** The acquirer purchases the stock directly, obtaining partial or full ownership of the seller’s legal entity itself. All assets and liabilities, contracts, and permits held by the entity at the time of the sale are retained by it and come with the deal.

Buyers often prefer asset deals whereas sellers prefer stock deals reflecting the benefits and risks to the relative parties, but of course for a successful deal, both parties must agree. The majority of acquisitions are in fact stock deals, and the ratio increases with the size and complexity of the deal. For this reason, most cross-border transactions are stock (also called equity) deals rather than asset sales.

Set against this, though, are rules in some countries about foreign ownership, which will require an alternative structure or approach. Russia, for example, has a law on foreign investments restricting foreign ownership and control in business entities of strategic importance to national defense, national security, or over strategic companies.

Some of the high-level implications of stock and asset deals are compared in Table 3.1.

Whether the acquisition is a stock or an asset deal, the acquirer can, and may need to, restructure the legal entities at deal close, or during the integration. The most common path is to acquire a legal entity in a country where the multinational company already has a subsidiary of some kind.

If there already exists a full legal subsidiary, then the legal, tax, and finance work streams normally plan an appropriate integration path for these entities, taking into account all of the assets and liabilities, the sales
Cross-Border strategy and deal Planning contracts, supplier contracts, tax credits or liabilities, and the assignability of all of these. Transfer of these may be in one go or phased, and eventually one of the entities can be closed.

If the acquisition is a geographical expansion and the acquirer has just a branch office, sometimes referred to as a sales and marketing entity, or no entity at all, then the target can become the legal subsidiary in that market relatively simply.

The emergence of rapidly growing technology, consumer, and gaming companies that may rely solely on the Internet to reach consumers and

### Table 3.1 Integration Implications of Stock versus Asset Business Sales

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<tr>
<th>Stock Deals</th>
<th>Asset Deals</th>
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<td>Simpler transaction structure and procedure, with one sales and purchase agreement.</td>
<td>Since contracts are with the selling company, not its assets, third-party consents are required for many contracts or other asset types, slowing down the integration, making it more complex, or requiring phased purchases.</td>
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<td>More tax efficient for the seller.</td>
<td>Potential tax advantages for the buyer, but risk of double taxation for the seller.</td>
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<td>All liabilities transfer with stock. Liabilities and risks need to be carefully analyzed during due diligence and mitigated during integration.</td>
<td>Since the deal has probably purchased assets but left liabilities, the risks for due diligence and integration are likely to be lower. Any transferring liabilities are usually time-limited.</td>
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<td>The acquirer may choose to settle outstanding lawsuits or claims to avoid publicity and management distraction.</td>
<td>Asset preparation is required, including compliance with local requirements related to asset divestments.</td>
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<td>Target company’s operations continue to be performed irrespective of the change in ownership (unless change of ownership clauses apply).</td>
<td>Where the asset is a division or a business unit, it is likely to require a carving-out, which may require transition services.</td>
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<td>Transfer of employment is usually permitted, allowing employees to continue under existing contracts.</td>
<td>A legal entity is required to transfer the assets into. This will normally be one or more of the buyer’s existing entities, but could require setup of a new legal entity. New employment contracts will be required, effectively making transferees new employees of the buyer. Due diligence can be more onerous in an asset deal.</td>
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contributors, with no need for local brick and mortar operations, provides an interesting new dimension to the previous model. The debate over the tax optimization of these companies, where they do make profits, in recent years has highlighted to the public the operating models of such companies, and their tax status can rely upon having no local operations. Small bolt-on acquisitions of talented teams or specialized products anywhere in the world may require special planning and careful integration to avoid disproportionate tax implications to the acquirer.

Coming back to the implications of these various deal and legal entity structures upon cross-border integration, the integration needs to be very aware of, and plan around, the transfer dates of sales, supplier, and employment contracts between entities. Particularly in countries with stronger labor laws provisions, the operational restrictions around employee transfers can be surprisingly impactful. Where integrations have a major integration milestone, these are often largely determined by the legal transfers occurring on those dates.

**Competition Authorities**

A competition authority is a government agency that regulates competition laws and enforces them within a certain jurisdiction. There are a couple of multinational regulators that oversee antitrust issues across a trade bloc, most famously the European Commission’s Directorate-General for Competition, but most are national regulators.

The number and scope of rules and regulators is changing and expanding rapidly at the moment, with major changes over the last few years in the United Kingdom, Brazil, China, Russia, the Common Market for Eastern and Southern Africa (COMESA), India, and Turkey. The most influential regulators tend to include those where M&A deal activity is high, consumer protection laws are more mature, or where national protectionist measures are in place, and we will focus more on these:

- Brazil—Conselho Administrativo de Defesa Economica
- China—Ministry of Commerce
- European Union—European Commission (Directorate-General for Competition)
- France—Autorité de la concurrence
- Germany—Bundeskartellamt
- India—Competition Commission of India
- Israel—Israel Anti-Trust Authority
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Japan—Japan Fair Trade Commission
Russia—Federal Antimonopoly Service of Russia
United Kingdom—Competition and Markets Authority
United States—Department of Justice Antitrust Division and the Federal Trade Commission

For a full list of national competition regulators, see Figure 3.4.

Objectives and Political Intervention of Competition Authorities

The regulators’ explicit aim is to protect the rights and interests of local consumers by identifying potentially monopolistic behaviors and to put in place rules, regulations, and measures necessary to prevent these. Authorities follow state laws, regulations, and merger guidelines that cover different types of integrations. Competition direction, however, and sometimes specific judgments, can be subject to government or political intervention, and therefore can be used as a cover for protectionism. China, where anti-trust enforcement has increased significantly in the past few years, is frequently cited as using anti-monopoly legislation to penalize or prohibit foreign acquisitions, investment, and control in China, whether state-controlled or corporate, and protect indigenous Chinese businesses. Of course, China’s competition laws differ from those of most Western governments because China is establishing “an aggressive antitrust policy that takes into account Confucian norms of ethics, morals, and fairness, and seeks to inspire increased corporate social responsibility” within an explicitly socialist market economy, as opposed to Western authorities’ “neutral and scientific neoclassical economic model,” which separates law and politics. Even in the United States, the Committee on Foreign Investment can prohibit transactions involving either potential foreign control of sensitive American entities or critical infrastructure or technology assets (especially related to energy, import/export, and communications).

There has also been a growing concern from free-market and free-trade campaigners over the last few decades about the balance between competition enforcement and unproductive constraint of successful and legitimate businesses, and what is really in the interests of the consumer. In response to Western governments’ anti-trust actions against such companies as Intel, Microsoft, Visa, and MasterCard, 240 economists wrote an infamous open letter to President Clinton in 1999, stating that anti-trust protectionism means “open market competition is displaced by bureaucratic and political decisions. More of the energies of firms are directed to politics, less to production and innovation. Successful innovators are penalized, scale economies are lost, and competition is thwarted, not enhanced.” The debate has
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**Figure 3.4** National Competition Regulators
only escalated since then on both sides of the Atlantic, most notably with the European Union’s long-running argument with Google over anti-competitive practices employed by Google’s search engine. While these competition investigations and legal cases don’t directly relate to M&A practice, they generate negative publicity and distract management from other matters, including acquisition integration, which Google itself is busy with all the time. Google’s acquisitions are also certainly scrutinized carefully for impact on competition.

**The Process of Anti-Trust Approval**  In terms of the anti-trust approval process, merging or acquiring parties now always need to identify required anti-trust filings, where there are regulatory bodies, the need for a pre-signing opinion from the competition authority and potential risks before signing any deals. The parties that may be obligated to notify include the selling shareholders in all cases, but also sometimes the target (in the United States) or even the nonselling shareholders if they continue to exercise control over the target (in the European Union). For this reason, while companies will only pursue cross-border M&A activity that they believe will be approved, the requirements for anti-trust filings and successful obtainment of anti-trust approvals are always inserted into sales purchase agreements now, in case competition clearance is not given.

Criteria set down by the relevant competition authority are used to determine the significance and potential impact of a specific transaction, and over specific thresholds, the parties may be obligated to notify the authority. Commonly used criteria include the parties’ revenues, assets, market shares, and the transaction value. The concept of the “relevant market” within which to assess market share is a particularly contentious aspect of this calculation.

Competition lawyers can provide guidance and risk predictions, help prepare submissions, and provide transaction approval timetables, around which close dates and integration activities can be planned. They know that the European Commission and China have strict timelines for the review process, whereas the U.S. authorities have the ability to extend the timeline vastly. However, the variety of obligations between authorities, and indeed the differences between the jurisdictions a cross-border deal may straddle, cause the entire anti-trust process to be one of the biggest risks to integration planning, and a frequent cause of delay. The acquisition of Sauflon Pharmaceuticals by CooperVision is one example of this. The companies were unexpectedly issued an Initial Enforcement Order by the newly combined UK Competition and Markets Authority in September 2014, after the deal had closed. This halted all integration activity and mandated the running of the businesses separately in the United Kingdom until clearance came through three months later.
This was because it is not mandatory to notify in the United Kingdom. In most jurisdictions, including the United States, India, and the European Union (EU), as Jay Modrall writes, “Notification is mandatory for transactions meeting the relevant thresholds. In some jurisdictions, including Australia, New Zealand, and the United Kingdom, however, notifications are voluntary. Merging parties may choose not to notify, bearing the risk that the authorities may later open an investigation on their own initiative. After a transaction becomes public, authorities in such voluntary filing jurisdictions may proactively request that a notification be filed.” Mandatory jurisdictions are usually suspensory, requiring notification in advance, but some such as in COMESA are mandatory but nonsuspensory, placing potentially unwinding burdens on the business post-close if not approved, and increasing the importance of good legal advice.

The European Commission cannot investigate mergers or acquisitions that it cannot argue put a company above the threshold for notification, but in the United States and China, the competition authorities reserve the right to investigate any transactions they wish, whether meeting the thresholds and notified to them or not. Again, this increases the potential for anti-trust implications post-close during integration.

**Implications of Anti-Trust Rulings** Risks to integration commencement and progress are referred to above, but the most impactful implication of competition authorities on M&A programs can come from the judgments and remedies of the regulators. Outright prohibitions of merger and acquisition transactions are rare given that competition guidance is quite transparent, precedents are usually established, and therefore lawyers have a good grasp of when clearance is unlikely. Far more common are contingent approvals upon some stated remedy, which may be negotiated or simply mandated by the authority. Frequently this requires “fixing” a competition problem generated by a merger, while at the same time preserving its economic rationale. Papandropoulos and Tajana believe that “divestiture commitments tend to be preferred by competition authorities because they are expected to restore competition without requiring constant monitoring,” but intellectual property, licensing or other changes may also be possible.

The impact on the integration of such a remedy can be extensive, depending on the size of the deal relative to the carve-out, and the complexity and level of dependence of the carved-out business on other parts of the business. When Kraft acquired Danone in 2007, the European Commission agreed to the deal on the condition that Kraft divest a number of brands and a manufacturing facility, and to provide transition services to the divestment. A dedicated team was brought in to manage the divestiture at the same time as the acquisition, significantly increasing the complexity of the program.
In most cases, such divestments will not have been fully envisaged by the acquirer’s deal team as necessary when the deal was agreed, and integration planning, synergies, resourcing, and timelines will all need to be reconsidered in light of the remedy. The parties are not obliged to accept the remedy and continue with the deal, subject to constraints within their purchase agreement, of course, and at this stage many deals, already in the public domain by this stage in the process, fall through.

**Sector-Specific Regulation**

The scope and mandate of sector authorities is another broad topic, but in regard to cross-border acquisition and integration, the relevant regulators to the buyer, seller, and the target may all need to be informed and often consulted before or after deals are signed. In heavily regulated industries such as financial services, health care, education, pharmaceuticals, and defense, they can also proactively put pressure on businesses to merge or divest if they judge there to be justification to do so.

In many jurisdictions, competition authorities work with sector regulators and share anti-trust powers with them, and regulators have separate legal authority over M&A transactions within their sector. In the United Kingdom, for example, the CMA works with Ofgem in energy, Ofcom in telecoms, ORR in rail, and Ofwat in water. In the European Union, both competition rules and those pertaining to sector regulation mandate the need for agencies to confer with each other, giving behavioral issues to the competition agency and structural issues to the sector regulator. There is a worldwide trend for regulators, themselves often growing and maturing, to take a much more active role in M&A.

Competition and merger guidelines tend to tell companies what they should not do, while sector regulation tells organizations what they have to do, and regulators have a much broader remit to question the parties, including sometimes aspects like management bandwidth, the identity of controllers, financial positions, and so on. Regulators are well placed to take such a broader view because of the depth of knowledge they have of the sector and history of the parties involved, who are likely to have been scrutinized by the regulator in the past through inspections, audits, and so on. When it comes to M&A approvals, “the best approach is one which involves cooperation between sector regulators and competition authorities,” combining the expertise of both.

However, the involvement of regulators in transactions lengthens the transaction approval process, increasing the risks to the parties of proposed transactions being rejected or remedies proposed. In some cases, it can materially affect the willingness of executives to attempt M&A because of
“concern[s] about ‘hanging out there in the market’ for prolonged periods of
time due to difficulties in obtaining regulatory approvals,”10 alluding to the
commercial impact that public knowledge of proposed transactions can have.

Regulators also add complexity for M&A parties, as valuable company
resources need to engage early with regulators to prepare information,
answer questions and respond to them. In large transactions this can be hun-
dreds of pages submitted through legal support under tight timelines, put-
ing a strain on the acquirer’s deal and management teams. Post-acquisition,
companies may be required to provide further information to regulators as
well, demonstrating that they are implementing certain recommendations.
The post-notification submissions can also be requested and challenged
by competitors as they are made public. Challenges include market defini-
tions of an impacted market, as a wider definition might put the transaction
below a threshold and a more narrow one above it.

Most acquirers turn to outside legal support for competition advice,
which must be carefully chosen. All law firms specializing in anti-trust
within a jurisdiction need to maintain good relationships with, and respect
of, the relevant authorities, which could conflict at times with the interests
of a client in a specific deal, for example, when it comes to remedies. The
top law firms might come in at a high cost, but they are able to use their
relationship and experience to negotiate and know when to stand firm.

The regulatory burden on transactions and during integration is par-
ticularly high in the financial services industry in the wake of the tighter
controls put in place all over the world after the financial and regulatory
crisis of the banking failures of 2007–2008. In this sector, regulatory reverse
due diligence, where a seller performs due diligence on the regulatory stand-
ning of the buyer, has become common for identifying regulatory concerns in
connection with a transaction.

In addition to their anti-trust roles, regulators have hundreds of other
administrative legal functions that may impact the operations of the busi-
esses during or after integration, and these should be considered during
due diligence and integration planning. Because these vary between jurisdic-
tions, and some of these may not be top of mind for executives and integra-
tion leads, companies need to ensure that the appropriate work stream leads
are receiving advice and planning accordingly.

Examples of some of the regulations that can impact cross-border inte-
grations include:

- Licenses to operate
- Professional accreditations and associations
- Local and international standards
- Health and safety certification
Cross-Border Strategy and Deal Planning

- Advertising regulation
- Food and drug licenses
- Banking regulation
- Environmental regulation
- Regulation and monitoring of pollution
- Regulation of acupuncture
- Sports and gaming regulation
- Telecommunication
- Vehicle licensing and regulation
- Wage regulation
- Cyber-security regulation

One note on the last point around information security and privacy to illustrate some of the potential impacts on integration. All organizations are now subject to complex regulation surrounding the protection of their own data, those of customers, suppliers, and employees, and especially those of the public. The numerous examples of information security flaws, leaks, hacks, and lost data make this important across all industries. Given the press and public interest in news of corporate failures in this area, there cannot be any complacency in this area. Management of data across borders is itself a complex area—Safe Harbor laws go some way toward enabling the free movement of data between countries that respect one another’s data protection laws, notwithstanding the EU's striking down of U.S.-EU Safe Harbor laws in October 2015. However, acquirers must ensure that data security and data handling are sufficient immediately after taking control. Furthermore, integration plans can presume data integration without taking these laws into account.

**FINANCIAL IMPACT**

Naturally, the financial implications of cross-border integration are impactful, principally due to differences between the jurisdictions of the parties with regard to taxes and financial accounting and reporting. This section describes these in some detail.

**Taxation**

All mergers, acquisitions, and divestitures have tax implications to buyers and sellers, and the importance of these is hard to overstate. The previous section describes how a principal differentiator of stock and asset transactions is often their tax treatment, but the implications of taxation go well
Beyond deal structure, and thorough tax integration planning prior to close is still too often overlooked in the rush to get the deal done.

Because of the variations in corporate tax levels and rules across different countries, it is one of the most important contributors to acquisition synergy models, even though it is rarely stated in public. In fact, tax efficiencies not only make or break synergy targets, they can become in some cases the sole rationale for M&A transactions. In recent years, governments in higher tax countries have been focusing more and more on tax optimization techniques, and one in particular related to M&A has been widely reported in the press—tax inversion.

Tax inversion is a term that describes a company’s restructuring or reorganization in order to reduce its tax obligations by legally moving to a lower tax country, often via acquiring a company headquartered there. This is done principally by moving a company’s headquarters out of the United States, which has the highest corporate income tax rate that is imposed on profits collected worldwide, into a jurisdiction with a lower or zero tax rate and a territorial system of collection. This allows the company to legally avoid a potentially enormous amount of taxes collected outside the United States and avoid some domestic U.S. tax as well through loaning profits to subsidiaries abroad.

The United Kingdom was forced to move from a worldwide to a local corporate tax system to avoid corporate emigration, but the United States maintains such a system for the moment. Although inversion has been around since the 1980s, it is only in the last decade that it has really taken off, and has moved from a tax matter to a public and political one, as discussed in the next section. Tax regulations in the United States followed public opinion and political pressure and started to adapt in 2014 by inhibiting tax inversion behavior—it is likely that tax inversion will be prohibited in the near future.

It is not just levels of corporate tax that need to be considered, as there are other related factors such as stamp taxes, value added tax (VAT), incentives for new investment, subsidies and tax relief, transfer pricing mechanisms, and so on. As well as impacting deal structure, the implementation and reorganization to support tax efficiency may impact the integration program.

Withholding tax and VAT leakage are common issues that need to be addressed during cross-border integrations and carve-outs. If transition services are required as part of a divestiture, and these are provided across borders, care needs to be taken to ensure that there is no leakage caused by those payments.

Tax accounting and reporting requirements continue until the integration is complete and the legal entity exists and is not in liquidation, and
therefore the accounting and tax information systems to support the tax function need to continue operationally until no longer required. If legal integration occurs prior to full IT integration, the additional complexity and inefficiency of reporting across multiple systems must be adequately resourced.

Another implication on taxation during integration, as in business-as-usual, are the decisions made by other areas of the business. Supply chain efficiencies are often tax-led, but operational decisions made about cross-border logistics, vendor consolidation, and importers of record have implications on tax and need to have oversight of integration plans in order to assess tax impact.

In summary, companies need to understand the economic conditions and applicable taxes wherever they operate, which are changing rapidly at the moment in all parts of the world. Multinational companies and those performing foreign acquisitions need to be especially aware, as the difference between jurisdictions provides an opportunity to maintain a tax advantage if well managed, and a serious threat to deal synergies and business profitability if not.

Financial Control and Reporting

International Financial Reporting Standards (IFRS) have been designed to provide consistent global rules for accounting and reporting on the financial positions and performance of companies. Although originating in the European Union, these are now widely used around the world, enabling convergence of local generally accepted accounting principles (GAAP).

For cross-border acquirers, these standards enable high-level due diligence of potential targets and reduce the complexity of financial integration, enabling reporting across the businesses immediately after close relatively easily as the elements defined by IFRS can be used to consolidate quickly.

However, the United States has not adopted IFRS, so U.S. companies may use standards set out by the U.S. Financial Accounting Standards Board, commonly referred to as U.S. GAAP, but not conform to IFRS, and non-U.S. companies are unlikely to conform to U.S. GAAP. While both U.S. GAAP and IFRS require reporting on an accrual basis (as opposed to cash basis), and share components such as balance sheets, income statements, and cash flow statements, there are still some significant differences between them, making cross-border reporting in and out of the United States more complex as the reporting has to be “translated” between one standard and the other. Chinese accounting standards are also somewhat different from IFRS and U.S. GAAP due to their origins under socialism, although they are converging with the former.
Acquiring companies need to be “bilingual” across these standards, and between close and full integration, translation is likely to be required in order to satisfy the acquirer’s reporting obligations.

**SOCIAL IMPACT**

The social impacts on, and implications of, M&A can touch upon public interest and public policy, environment factors, pro bono and social contributions, local investment in infrastructure, and often most acutely upon local employment. The objectives of a cross-border deal need to be transparently presented to stakeholders, and if there are difficult decisions that impact local communities around the acquired business or the wider public, these should be well considered, well prepared, and well justified. Preparations need to include thorough risk assessment and risk mitigation.

Corporate social responsibility (CSR) is a term that can be used to broadly define those aspects of a business where it attempts to take ethical decisions to improve the quality of life of employees, stakeholders, and the wider communities within which it operates, and may include policy areas covering waste and the environment, education and social causes, employment practices, and governance. It is possible to measure some of these areas of CSR and compare acquiring organizations.

It is interesting to note that organizations that score highly when it comes to the governance aspects of CSR are somewhat less likely to engage in M&A activity in the first place because deal-making is a centralized activity for CEOs and boards, often prone to personal bias and looking for personal reward over shareholder value. Therefore, companies with stronger corporate governance, and higher CSR scores, are less likely to sign M&A deals. This could lead to a somewhat cynical view of corporate M&A, but on the other hand, employee diversity, another key metric of CSR, makes a company more likely to pursue cross-border acquisitions, because the competitive advantage of this cultural diversity over competitors makes it more likely for the acquirer to make synergistic gains through the acquisition.

It is probably difficult to draw too much quantitatively about the impact of CSR and social factors on M&A, but the impact on integration is huge. Social concerns permeate the work streams of leadership, human resources (HR), communications, culture, operations, and research and development.

For example, an acquirer deciding to achieve synergies by radical changes to the target company’s environmental policy and waste procedures, even if aligning to its own, is likely to find itself quickly criticized by employees, locals, environmentalists, the press, and politicians. A company can quickly be perceived as draconian if it chooses to close down social or
charitable programs run by the acquired business, which are often as important to internal culture as to external and brand image.

Notable failures in cross-border integration have come when acquirers have ignored public sentiment or occasionally gone back on public commitments. Kraft’s acquisition of Cadbury in 2009–2010 is a well-documented M&A case study now, and a prime example of this. The hostile takeover of Cadbury, a cherished national brand, by the U.S. conglomerate elicited a media and political outcry. The Cadbury board felt it necessary to make a public ethical commitment that its Green & Black’s brand would be moving its entire range to Fairtrade days before signing the deal in order to force Kraft into this commitment. The acquisition itself became acrimonious, with the chairman of Cadbury stating that he would prefer any of the other potential industry buyers to Kraft, and the UK business secretary, Peter Mandelson, publicly warned Kraft not to try to “make a quick buck” from the acquisition of Cadbury.

To head off British public, union, and political pressure, Kraft’s CEO committed to various integration principles, including the maintenance of the Somerdale factory with 400 jobs, a decision that was reversed later. On top of a difficult and expensive integration, not least because of the cultural and productivity dip associated with hostile takeovers, it is likely that consumer backlash in the United Kingdom contributed to the difficult financial position of Kraft that year. The high profile of this acquisition resulted in changes to the UK Takeover Code to protect and empower potential M&A targets.

In general, acquiring companies, particularly those involved in cross-border acquisitions, will tend to be cautious when it comes to integration planning in these areas with social implications, for fear of value destruction, making decisions without information, and bad publicity. Announcements of cross-border deals, besides their financial and strategic goals, often focus on the social consequences of the integration, with commitments or intentions to maintain current ethical policies, staffing levels, locations, and so on. Unless the deal rationale is dependent upon major changes during integration, it is prudent for companies to come back to any changes that may be required, when the implications will be better understood and association with the acquisition removed. It also leaves time for communication with key local stakeholders such as local government officials.

**POLITICAL IMPLICATIONS**

Like the social factors, the political interdependencies with cross-border integration can be hard to predict. Generally, politicians and influence groups such as unions, campaign groups, and other nongovernment organizations
will be interested in cross-border M&A if the integration causes significant changes to causes that they are interested in, which will tend to be the legal, financial, or social factors listed earlier.

Stakeholder mapping is important here to identify all of the public and political organizations that may be interested in the M&A deal, at home and abroad, and to anticipate those aspects of the integration that will be of interest to them in advance. Political stakeholders will not be interested in synergies or corporate deal rationale, but rather with the public, social, environmental, and national implications of integration decisions. For this reason, a story is usually presented at announcement that addresses these wider social and political areas in a way that makes the deal positive or at least neutral to the wider stakeholder group.

It is usual for political intervention in cross-border M&A to focus on any negative impacts on the status quo, in response to announcements or integration activities. It was the announcement in July 2014 by AbbVie that it would acquire Shire for $55b so that it could move its tax base to Ireland and reduce its effective tax rate to 13% that precipitated U.S. government condemnation. President Obama called the move “unpatriotic” and the treasury secretary stated, “We should not be providing support for corporations that seek to shift their profits overseas to avoid paying their fair share of taxes.” The U.S. government subsequently revised the rules on inversion deals making offshore cash immediately taxable by the United States, causing the abandonment of the deal at a cost of $1.635b to AbbVie. AbbVie was correct in asserting that the U.S. government had “reinterpreted longstanding tax principles in a uniquely selective manner designed specifically to destroy the financial benefits of these types of transactions.”

The most common cause of political intervention, including unions, of course, is job losses. A foreign acquirer whose rationale entails cost synergies by making job cuts in the target market is a political and economic threat to the local country with little upside. While some back-office consolidation is understood and accepted politically, wholesale closure of offices or operating locations and movement of jobs offshore will be fiercely resisted unless it is obvious that there are no other options available, and those jobs would otherwise be under threat anyhow.

Another dimension, especially when doing business in emerging markets, is a consideration of the political links and dependencies of acquisition targets with politicians and political officials. Clifford Chance recommends performing “integrity due diligence” because “strong links with the government can be an asset but, if there is a change in political leadership, they can also become a liability.”

Political or special interest groups can and should be used to support and promote cross-border M&A where possible. Obtaining the support of
nongovernment organizations, trade associations, and politicians is a legitimate means of boosting corporate public relations activity around an M&A deal, and throughout the integration. Social media can also be used for this purpose to positively influence public opinion.

MANAGING EXTERNAL RISKS AND ISSUES

Being alert to, and advised upon, the impacts and implications of all of these legal, financial, and social factors is essential to cross-border integration. Deal structure planning starts very early in the M&A transaction life cycle, but assessment of the impact of all of these factors may require buyers and sellers to be flexible.

By announcement, the impacts and the implications on the deal and the integration should be well understood, and reflected in the deal structure and terms, but the work of the integration teams has just begun. Integration leads and work stream leads share responsibility for mitigating, monitoring, and managing risks and issues arising from the deal and the subsequent integration. Investor relations, public relations, regulatory, government affairs, and HR work streams should be monitoring their relevant stakeholder groups and engaging with them actively throughout the integration.

Companies acquiring in countries where they do not have existing business teams, operations, stakeholder relationships, or local knowledge are obviously exposed to greater risks than those performing vertical or horizontal acquisitions to build out their existing markets. Local knowledge and experience of the harder legal and financial aspects is important, but so too of the softer political, social, and media implications. Where there are greater cultural differences between buyer and target, and language barriers that make assessment and feedback more difficult, there are more likely to be issues arising.

Western companies with free press buying in emerging markets are especially vulnerable to public and political pressures, and need to be especially vigilant to issues such as corruption and bribery, environmental impact, and human rights within target acquisitions as media stories on such subjects could destroy deal and corporate value very quickly.

Risk management for all integrations should start as soon as integration planning does, during due diligence. Integration teams should be engaging with the deal team and external advisors continuously to identify risks, plan accordingly, and monitor these on risk registers.
CHAPTER CHECKLIST

- Companies planning cross-border acquisitions need to consider both the impacts on, and implications of, the deal.
- Both the deal structure and integration program need to adapt to the specific context of the transaction, as competition and other regulators in any jurisdiction have the authority to block deals or mandate significant changes to them.
- Integration planning for cross-border deals needs to start during due diligence, with integration risk management taking a holistic view of the legal, financial, social, and political implications of the integration.
- Internal and external communication should follow the rule that the company communicates as much as it can as early as it can, engaging with government, union, nongovernmental organizations, media, and other stakeholders.

NOTES

1. Global PMI Partners, Cross-Border M&A Integration Survey, Question 12—“Based on your general experience, identify geographies where you have experienced the greatest degree of cross-border challenges (legal, regulatory, political, etc.).” 2015.
2. Global PMI Partners, Cross-Border M&A Integration Survey, Question 10—“Which of the following areas impacted the integration of your most recent cross-border deal?” 2015.
4. Ibid.


