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Client Alert

Energy & Natural Resources

Energy and commodities asset acquisitions: post-acquisition issues

At a Glance…

This is the fourth and final article in our series on mergers and acquisitions in the energy and commodities sector. The first article covered headline issues when acquiring business assets; the second looked at considerations in the 'soft' commodities sector; and the third focused on the top 10 regulatory considerations for energy and commodities asset trading under English and EU law.

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In this article, we highlight the 10 main post-completion issues that businesses should bear in mind following any acquisition, to ensure that they can operate smoothly and successfully. Many of the issues highlighted will be pertinent to the post-acquisition stage of any acquisition of a business (whether a share acquisition or the acquisition of specific assets). However, we also have highlighted certain esoteric issues that will be relevant specifically in the energy and commodities sector.

	Issue	What to consider
1	Integration	The first 100 days after an acquisition are the most critical period of integration, and a probable indicator of the likelihood of success of the transaction, so it is important for the purchaser to have an integration strategy in place before the transaction closes. Integration of an acquired business should be specifically tailored to support the commercial objectives that warranted the acquisition in the first place. Bespoke objectives will drive the direction and pace of the integration. Consequently, it is important for the purchaser to appoint the right team to ensure integration is a success. Depending upon the sophistication of the purchaser, such integration team may be appointed internally or external advisors may be engaged. Generally, there are two models of integration which the purchaser can use: 1. 'light touch' integration, where the purchaser leaves most of the acquired business' operations and management intact; or 2. full integration, where the purchaser executes a comprehensive integration strategy across various workstreams to fully integrate the acquired business. Typical workstreams that are usually integrated include: HR, communications, sales, operations, marketing, IT, finance, accounting, legal and payroll.
2	Warranties	The sale and purchase agreement usually limits the time within which a warranty claim can be made. The statutory limitation period is six years in the UK, but the time limit agreed in the sale and purchase agreement is usually between one and three years. The purchaser should be aware of key milestones in relation to potential warranty claims under the sale and purchase agreement, including the date by which any warranty claims must be notified to the seller, and the date by which any proceedings must be commenced.

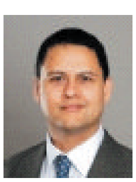
		The purchaser should also implement procedures to monitor matters covered by the warranties in the sale and purchase agreement to ensure that potential claims are identified, assessed, and promptly notified to the seller. This is most effectively done by appointing someone to monitor the acquisition documents, and make appropriate enquiries. When receiving notification of a breach of warranty claim, the seller should ensure that the notification complies with the prescribed content and time limits set out in the sale and purchase agreement. If the notification is non-compliant, it may be invalid, and the purchaser will be unable to bring that claim.
3	Novation and assignment	When an acquisition of specific assets has occurred (as opposed to a share acquisition) existing contracts, such as customer agreements, office and equipment leases, service agreements, distributor agreements, supply agreements and sales contracts, need to be transferred to the purchaser. Post completion, steps should be taken to effect the novations or assignments. These steps may range from giving a notice of assignment to all contractual counterparties, to agreeing tripartite novation agreements with the seller and the applicable counterparty. The steps that need to be taken will depend on the terms of each individual contract. Contracts should be reviewed at an early stage, to determine whether they are freely transferable or, if consent is required, what the nature of and process for that consent are. A novation and contract assignment exercise is labour- and time-intensive. This should be factored in when setting the transaction timetable, and estimating costs for the transaction.
4	New terms and contracts with counterparties	While reviewing existing contracts, the purchaser should consider whether the terms of these contracts are suitable for the acquired business going forward. If not, the purchaser could seek to negotiate new contractual terms with counterparties. Conversely, a counterparty also may consider the current contractual arrangement with the acquired business to be unsuitable, and either request a renegotiation of the contract (credit terms, termination provisions, etc.), or refuse to consent to a novation and terminate the contract. One of the reasons a counterparty may seek to renegotiate a contract is because the seller and buyer are different entity types (e.g., the seller is a bank, and the buyer is a utility), and this leads to changes in internal requirements for contractual terms. Existing contractual arrangements may have been tailored to the counterparty (e.g., the granting of prescribed credit limits), and so not be suitable for a different counterparty or where the counterparty is under new ownership. Purchasers should bear this in mind at the due diligence stage as a counterparty terminating a contract which is of material importance to the business, could have significant implications on the business going forward and, consequently, result in a decrease in the value of the business.
5	Transitional services arrangements	Transitional services agreements (TSAs) are entered into when the purchaser agrees to pay the seller for certain services that the seller will continue to provide in order to support the acquired business for a fixed period of time post completion. TSAs are usually entered into to ensure the seamlessness of core services such as HR, IT, accounting and sales, and generally result in a smoother integration process. TSAs are generally in force for a period of 12-24 months, starting from completion, giving the purchaser time to acquire or develop – or implement its own – capabilities to run the acquired business. Certain employees of the seller may be required to be seconded to the acquired business for a certain period of time, in order to provide the services under the TSA. Specific employment law advice should be sought in order to put ancillary secondment agreements into place, where required, and to ensure that the Transfer of Undertakings (Protection of

		Employment) Regulations 2006 do not apply (if that is indeed the intention of the parties). The purchaser should identify early on the systems and services that are currently used to conduct the acquired business, and reconcile those against its own systems and services, thereby identifying which will still be required post completion.
6	Ongoing regulatory considerations	The purchaser will need to review local laws to assess if it is required to obtain new licences, permits or approvals in order to carry out the day-to-day operations of the business post completion. *Registration requirements* For certain categories of assets, such as real estate, IP or vehicles, the change in legal title may have to be recorded with governmental or regulatory authorities to be effective. The transfer of shares will have to be recorded in relevant company records, and new share certificates will have to be issued. Purchasers should consider whether any foreign investment approvals or registrations are required, for example, the registration of new shareholders post completion. *Change of control* In a share sale, obtaining regulatory approvals for any change of control of a financially regulated target will typically be a condition of completion. Regulators will need to be notified once completion has taken place and will need to be kept abreast of the purchaser’s integration plans. *Capital requirements adequacy* Financially regulated firms are typically required to hold a certain amount of capital at all times. Purchasers that are regulated may need to make adjustments to regulatory capital if their permissions or risk exposure changes following the purchase.
7	Energy and commodities-specific refulatory considerations	*Environmental considerations* If the acquired business has an environmental permit, purchasers will need to apply to the Environment Agency to transfer that permit to the new business. Purchasers also should review the permit to ensure they comply with any notification requirements, for example, notification of a change of registered office. It is quite common for environmental permits to require a parent company guarantee. Purchasers should check if the permit requires a guarantee. If so, the seller’s parent company guarantee must be terminated, and a new guarantee entered into. *REACH* Under REACH, registrants are obliged to inform the ECHA about changes in their identity. The seller must initiate a legal entity change in REACH-IT to transfer the registration to the ECHA account of the purchaser. The purchaser must then pay a legal entity change fee to the ECHA in order to complete the transfer. *REMIT* Under REMIT, a market participant undertaking trades in wholesale power and gas is required to register as a market participant with an EU national regulatory authority, and must comply with reporting obligations in respect of trades in ‘wholesale energy products’ (as defined in REMIT). If the purchaser acquires a business that includes wholesale energy products, then it will need to register with the competent national authority in order to be able to continue to report trades in respect of those products. The sale and purchase agreement may also require reporting under REMIT if it constitutes a ‘trade’ of a wholesale energy product. *Euratom* If the purchaser has acquired a business in the nuclear sector, it should ensure that the acquired business complies with Euratom, and that the Euratom Supply Agency (ESA) consents to all supply contracts. The sale

		and purchase agreement may itself need the approval of ESA, as it may be considered a supply contract for the purposes of Euratom. *CFIUS* The Committee on Foreign Investment in the United States (CFIUS) reviews transactions involving foreign investment in the United States. A foreign investor and the target company will submit a joint notice requesting approval for the transaction. Given the lengthy timetable for reviewing the transaction (up to 30 calendar days, which can then be extended for an additional 45 days), this should be factored in when setting the transaction timeline. While CFIUS rarely rejects transactions outright, it can approve a transaction, subject to the implementation of certain conditions (e.g., requiring U.S. citizens to handle critical functions of the business, or imposing reporting and audit requirements). While this is an important issue at the outset of a transaction, post completion of an acquisition, the buyer will have to ensure that it implements the conditions prescribed by CFIUS (to the extent applicable). *EMIR* A purchaser that has acquired a business trading derivatives contracts may be required to report the acquisition in accordance with EMIR, as the acquisition could constitute a modification of an existing contract. The purchaser should ensure it obtains a legal entity identifier prior to trading, and that it is able to report the details of all applicable trades, including novated trades, as soon as possible once the novations are entered into. *Position limits and position reporting* As the acquired position will form part of a new corporate group, it will be necessary to monitor the volume of trading done by the new business on trading venues, and all economically equivalent OTC contracts. (within the context of the acquiring corporate group), given that position limits are calculated on a corporate group basis. This will be particularly important where the legacy business was already close to the position limits. It will be essential to ensure that the new combined business does not result in any of the limits being exceeded. The trades undertaken on a trading venue, and the economically equivalent contracts, also will need to be reported. It will be necessary to ensure that all reporting channels are properly maintained, and information updated, to the extent required, following completion of the acquisition. Each of these issues is considered in more detail in our client alert entitled ‘*Due diligence for energy and commodity asset acquisitions: regulatory considerations*’.
8	Post-Brexit-to-dos	The exact nature of the UK’s withdrawal from the EU is still unknown. However, it is important to note that, in the event of a no-deal Brexit, certain regulations affecting M&A could change, or cease to apply. The ability to market a prospective transaction to potential EU customers may be impacted: UK teams will need to consider possible approaches to market a deal, which may include reverse solicitation, whereby the onus would be on the EU client to contact the UK market participant in respect of the proposed transaction. It should be noted that the precise conditions of the rules relating to reverse solicitation vary across EU Member States. Purchasers should note that in certain EU member states it is necessary to be an EU entity to obtain and maintain certain licences, for example, for gas and power trading. While the issue has been resolved in most EU member states, there are still a number of countries, mainly Eastern European countries and France, where the position has not yet been clarified. Purchasers should continue to review the requirements in the relevant member states to ensure the correct licences are obtained and maintained. Market participants in the EU Emissions Trading Scheme should review the acquired business’ emissions allowances and ascertain whether they are held in a UK registry account. If so, the market participant should consider opening and transferring them to a registry account in an EU 27

		member state. Purchasers should continue to review the EU Emissions Trading Scheme post-Brexit to ensure that they are aware of any changes in the status of the UK, which is currently a member of the scheme, as a result of Brexit. The impact of Brexit on the emissions market is considered further in our client alert entitled *'Brexit and the EU ETS – 10 things to consider'*.
9	Audits	A post-acquisition audit should be the final stage of the transaction. The purpose of this audit is to ensure that the new business corresponds to what the buyer is expecting, and what was disclosed by the seller. A thorough audit will help to identify any potential warranty claims. One of the audit team's main tasks is to audit the integration process, in particular to assess the acquired business' policies and procedures as well as information and communication lines. The audit will usually be based on a risk assessment and the corporate objectives set by the purchaser's management. This approach can help to identify the gaps in the acquired business' procedures and prepare a remediation or compliance plan to assist with the integration process. The purchaser should ensure that the internal auditors are closely aligned with the integration team, and that they have been involved throughout the transaction, as a lack of involvement can make it difficult for the auditors to gain an understanding of the newly acquired business' key risks and processes. By being involved throughout the transaction, the internal audit can reflect on the various stages of the process as well as make recommendations relating to project management and the documentation of internal controls and deficiencies.
10	Press announcements and confidentiality agreements	The parties should agree prior to completion whether a press announcement will be made, its contents, and who is responsible for releasing it. The parties should ensure that any post-completion announcements provide an overview of the deal itself and how the acquisition will benefit customers, suppliers and, potentially, employees. The parties can do so by communicating the key values and beliefs that underline the transaction, such as significant growth possibilities and opportunities for the acquired business as a result of the acquisition. The purchaser should ensure that any statement provided to the media by the seller or representatives of the acquired business aligns with any statements and announcements the purchaser has released. The purchaser should review any and all press announcements and statements before they are released to the media. The parties should also ensure that the confidentiality agreements entered into during the negotiation and due diligence phases of the transaction are sufficient to ensure that sensitive commercial information remains confidential post completion. If these are insufficient, new confidentiality agreements should be entered into to maintain this confidentiality. The purchaser is also likely to be subject to certain confidentiality obligations towards the seller; however, care should be taken to ensure that such obligations do not restrict the purchaser's ability to disclose information relating to the acquired business.

If you have questions or would like additional information on the material covered in this Alert, please contact one of the authors – listed below – or the Reed Smith lawyer with whom you regularly work.



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