

# International Comparative Legal Guides



Practical cross-border insights into private equity law

## Private Equity 2023

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Contributing Editors:

**Dr. Markus P. Bolsinger & Christopher Field**  
Dechert LLP



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# Expert Analysis Chapter

1

**2023 and Beyond: Private Equity Outlook for 2024**  
Siew Kam Boon, Sarah Kupferman & Sam Whittaker, Dechert LLP

## Q&A Chapters

4

**Australia**  
MinterEllison: Kimberley Low, Michael Wallin & Nick Kipriotis

14

**Austria**  
Schindler Attorneys: Florian Philipp Cvak & Clemens Philipp Schindler

25

**Brazil**  
Mello Torres Advogados: Carlos José Rolim de Mello, Roberto Panucci & Rafael Biondi Sanchez

33

**Canada**  
McMillan LLP: Michael P. Whitcombe, Brett Stewart, Enda Wong & Bruce Chapple

42

**Cayman Islands**  
Maples Group: Julian Ashworth, Patrick Rosenfeld, Lee Davis & Stef Dimitriou

50

**China**  
Han Kun Law Offices LLP: Charles Wu & Hanpeng (Patrick) Hu

57

**France**  
Vivien & Associés AARPI: Lisa Becker, Julie Tchaglass, Marine Pelletier-Capes & Julien Koch

65

**Germany**  
Weil, Gotshal & Manges LLP: Andreas Fogel & Benjamin Rapp

73

**Hungary**  
Moore Legal Kovács: Dr. Márton Kovács, Dr. Áron Kanti & Dr. Zsigmond Tóth

83

**India**  
Shardul Amarchand Mangaldas & Co.: Iqbal Khan & Devika Menon

91

**Italy**  
Legance: Marco Gubitosi & Lorenzo De Rosa

105

**Japan**  
Tokyo International Law Office: Dai Iwasaki, Yusuke Takeuchi & Tomo Greer

113

**Korea**  
Barun Law LLC: Min Hoon Yi & Si Yoon Lee

121

**Luxembourg**  
Eversheds Sutherland (Luxembourg) S.C.S.: Holger Holle, José Pascual & Rafael Moll de Alba

130

**Mexico**  
González Calvillo, S.C.: Jorge Cervantes Trejo, Bernardo Reyes Retana Krieger, Daniel Guaida Azar & Jerónimo Ramos Arozarena

138

**Nigeria**  
Banwo & Ighodalo: Ayodele Adeyemi-Faboya, Mavis Abada & Ibiyemi Ajiboye

149

**Norway**  
Aabø-Evensen & Co: Ole Kristian Aabø-Evensen

173

**Singapore**  
Allen & Gledhill LLP: Christian Chin & Lee Kee Yeng

182

**Spain**  
Garrigues: Ferran Escayola & María Fernández-Picazo

192

**Switzerland**  
Bär & Karrer Ltd.: Dr. Christoph Neeracher & Dr. Luca Jagmetti

201

**United Kingdom**  
Dechert LLP: Mark Evans & Sam Whittaker

213

**USA**  
Dechert LLP: Allie Misner Wasserman, Dr. Markus P. Bolsinger, Soo-ah Nah & Marie Mast

# France



Lisa Becker



Julie Tchaglass



Marine Pelletier-Capes



Julien Koch

Vivien & Associés AARPI

## 1 Overview

### 1.1 What are the most common types of private equity transactions in your jurisdiction? What is the current state of the market for these transactions?

Private equity (PE) transactions refer to investments achieved by PE investors at different stages of a company's life, from venture capital (VC) investments (pre-seed or seed stage), growth or expansion capital investments (early or late stage), to buyout investments (leveraged buyout (LBO), leveraged management buyout, buy-in management buyout, family buyout, etc.) and exit transactions. The French PE landscape, which has always been welcoming PE transactions, comprises PE funds focusing on LBO transactions involving mature companies and a multiplicity of VC funds interested in venture and growth capital transactions.

After the 2021 post-COVID peak, the LBO and VC transaction flow stayed strong until 2022, began to slow down and then fell as from the last Q22, with lower deal valuations, lower quantities of funds raised, and lengthier negotiation timeframes, even if it seems that PE activity in France has a bit bounced back in Q1 2023.

### 1.2 What are the most significant factors currently encouraging or inhibiting private equity transactions in your jurisdiction?

French economy has been able to show signs of resilience and maintain its appeal for PE transactions notwithstanding the current uncertain global economic environment (i.e., inflation, invasion of Ukraine, energy crisis, supply chain issues, increased market interest rates). Indeed, the political will to swiftly relocate strategic industries, the urgency of global warming, the rise of Web3 and deep tech companies, and the advancement of environmental, social and governance (ESG) goals, coupled with the French government's recent and promising initiatives (French Tech, France 2030, etc.) have been encouraging factors to PE transactions, despite the current worldwide inhibiting factors and some new regulations (such as foreign investment or antitrust) that may have curbed or prevented the completion of certain transactions.

### 1.3 Are you seeing any types of investors other than traditional private equity firms executing private equity-style transactions in your jurisdiction? If so, please explain which investors, and briefly identify any significant points of difference between the deal terms offered, or approach taken, by this type of investor and that of traditional private equity firms.

Industrial companies use the completion of build-up/PE or

VC-like transactions to adapt their activity to the market's new expectations (e.g., relocation of production activities, reduction of carbon footprints, or diversification of activities) by acquiring other companies or taking stakes in start-up companies. These transactions may combine M&A transaction philosophy and deal terms with PE or VC transactions financing and structure.

## 2 Structuring Matters

### 2.1 What are the most common acquisition structures adopted for private equity transactions in your jurisdiction?

Usually, acquisition vehicles (used for completing a transaction) are incorporated under the form of regular companies such as "société anonyme" (SA) or "société par actions simplifiée" (SAS) or specific companies such as VC companies (*société de capital-risque* – SCR), enjoying legal personality but still delegating the management of their funds to a management company.

Under French law, investments funds can be incorporated under the form of specific legal structures governed by the French Monetary and Financial code and the French Financial Market Authority (Autorité des Marchés Financiers – AMF), known as "alternative investment funds" (FIA). FIAs raise capital from investors to invest it following a predefined investment policy. The most commonly known structures are PE mutual funds, including VC mutual funds (*fonds commun de placement à risque* – FCPR), innovation capital mutual funds (*fonds commun de placement dans l'innovation* – FCPI) and other professional funds, such as professional PE fund (FPCI). These funds are deprived of legal personality and managed by a management company (*société de gestion*).

### 2.2 What are the main drivers for these acquisition structures?

The acquisition vehicles' structure may differ based on legal and tax considerations and depending on whether the transaction is organised as an assets deal, a share deal, a merger, etc., but are mainly incorporated under the corporate form of SAS (see questions 2.3 and 3.1 below).

The structure of the investment funds is mainly driven by: (i) the nature (either professional or non-professional) of their ultimate funders (i.e., opposing structures opened to non-professional funders, *inter alia*, FCPR, FCPI and *fonds d'investissement de proximité*, to those opened to professional funders, *inter alia*, FPCI and *société de libre partenariat*); (ii) the tax regime attached to the subscription of the securities issued by those structures and the capital gains achieved by said structures; and (iii) the sector, area of industry

and type of assets into which the investments are to be made, as specific types of funds must comply with certain investments ratios.

### 2.3 How is the equity commonly structured in private equity transactions in your jurisdiction (including institutional, management and carried interests)?

Regarding LBO transactions, PE investors usually acquire the entire issued share capital of the target company to fund its growth through, for instance, completion of build-up transactions. The acquisition is completed through a dedicated holding company (HoldCo), usually incorporated under the form of a SAS (see question 3.1 below), funded by the PE investor and other financial partners (such as banks) to acquire the target company.

PE investors often require the key managers to significantly invest or reinvest in HoldCo on a *pari passu* basis. PE investors may also invest in quasi-equity/debt-like securities, such as convertible or redeemable bonds, to allow the managers to benefit from a wider portion of the share capital of HoldCo with the same investment amount (sweet equity mechanism). The manager can also be granted free shares of HoldCo.

Managers' investments may be directly in HoldCo, or indirectly in a dedicated company (ManCo) itself investing in HoldCo on behalf of the managers. Then, the managers can be granted free shares of ManCo (instead of HoldCo).

Carried interest securities may benefit to the PE investors' managers, allowing them to have a share of the capital gain achieved by the funds upon exit. Under certain strict conditions, favourable capital gains tax exemptions may apply to these interests. Otherwise, they are tax-treated as regular compensation.

### 2.4 If a private equity investor is taking a minority position, are there different structuring considerations?

Under VC transactions, PE investors usually take a minority shareholding in the target company (start-up company) to fund the development of its business and activities, which are not yet mature, alongside other types of investors (business angels or family offices, for instance). Such investment is riskier than a buyout transaction involving an already mature company.

Therefore, PE investors usually subscribe to complex securities, such as shares with ratchet warrants attached, granting either protection of their investment against failure of the target company to achieve its project, or the opportunity to participate in the next fundraising round at preferential conditions. The investment can also be made by subscribing to quasi-equity securities (so-called "BSA Air"), allowing PE investors to convert their securities at the next liquidity event (mainly fundraising round) under preferential conditions.

For PE investors taking a minority position, it is important to negotiate specific rights under a dedicated shareholders' agreement (e.g., specific voting rights, reinforced financial information, tag-along right, anti-dilution). In particular, PE investors can be granted veto or supervisory rights, either provided in the shareholders' agreement and/or the company's bylaws or attached to preferred shares subscribed.

In such situations, the management/founders remain the majority shareholders and may benefit from free shares or founders' options (so-called "BSPCE").

### 2.5 In relation to management equity, what is the typical range of equity allocated to the management, and what are the typical vesting and compulsory acquisition provisions?

In LBO transactions, the package offered to managers aims at aligning their interests with the financing parties' interests. The management is often requested to invest (directly or through ManCo) in HoldCo on a *pari passu* basis with the PE investor regarding securities, capital gain perspective, and exit horizon. As a matter of trend, the managers usually hold between 5% and 15% of the equity.

If it is intended to grant free shares (*actions gratuites*) to key employees/managers, such granting may not result in allocating more than 10% of the issued share capital, nor for any allocatee to hold more than 10% of the issued share capital. Such allocation becomes definitive upon the expiry of a compulsory vesting period (which cannot be less than one year), and – if the shareholders so decide – a holding period. The combined vesting and holding periods may not be less than two years. Some exceptions may, however, apply to the 10% threshold and the vesting/holding period (e.g., percentage can be increased up to 30% if the allocation of free shares is made to all salaried employees).

In VC transactions, BSPCE allocations are generally preferred. They must comply with certain conditions laid down in the French tax code. The BSPCE have no mandatory vesting and holding conditions or allocation cap, but market practice generally considers a four-year vesting period (with a one-year cliff) to be appropriate.

### 2.6 For what reasons is a management equity holder usually treated as a good leaver or a bad leaver in your jurisdiction?

Usually, a resignation or a termination for any reason before an initial time period fixed with the financial investor, the termination of the manager's functions for gross or wilful misconduct or the violation of provisions of the bylaws or shareholders' agreement, are considered a bad leaver departure. When the departure results from an unintended event (death, invalidity, termination without cause) or when the resignation takes place after the expiry of the initial time-period, it is usually treated as a good leaver departure.

Good and bad leaver provisions are less prevalent following the recent decisions of the French Tax Court on management incentive plans (see question 10.4 below).

## 3 Governance Matters

### 3.1 What are the typical governance arrangements for private equity portfolio companies? Are such arrangements required to be made publicly available in your jurisdiction?

Portfolio companies are commonly structured as an SAS, benefiting from limited liabilities of shareholders and great freedom in corporate governance. The main drawback is that the shares of an SAS cannot be listed on stock exchanges – but the SAS can be converted into an SA just before an initial public offering (IPO).

A board with oversight powers is usually established to oversee the management, comprising members appointed by the investors (PE investors are generally reluctant that their nominees be provided with management powers). Subject to limited exceptions, the existence of the board, its functioning rules and the

identity of its members can remain fully confidential by being only stipulated in the shareholders' agreement. The board can also be disclosed or fully regulated in the articles of association of the company, which are publicly available.

**3.2 Do private equity investors and/or their director nominees typically enjoy veto rights over major corporate actions (such as acquisitions and disposals, business plans, related party transactions, etc.)? If a private equity investor takes a minority position, what veto rights would they typically enjoy?**

Board veto rights on major corporate actions are typically granted to director nominees of PE investors with significant shareholdings. PE investors holding only a few percentage points of share capital do not typically enjoy veto rights. This, however, mainly remains a matter of negotiations.

**3.3 Are there any limitations on the effectiveness of veto arrangements: (i) at the shareholder level; and (ii) at the director nominee level? If so, how are these typically addressed?**

Veto arrangements are rather uncommon at the shareholders level because usually organised at the board level through the members representing PE investors. Violations of veto arrangements are strongly sanctioned. Managers can be held liable for the breach and/or be dismissed. Should the breaching party be shareholder, the shareholders' agreement usually includes specific penalties, such as bad leaver clauses or financial sentences.

As a principle, limitations of management's powers (such as veto arrangements) are, however, unenforceable against third parties, even when included in the company's articles of association. This means that any transaction implemented by a manager in breach of a veto with a third party will remain valid, including if this third party was aware of such breach. Management decisions made in violation of veto arrangements can only be cancelled if: (i) they do not fall within the corporate purpose of the company, as stipulated in the articles of association; and (ii) the third party was aware – or, in view of the circumstances, could not have been unaware – that the decisions were beyond the corporate purpose of the company.

**3.4 Are there any duties owed by a private equity investor to minority shareholders such as management shareholders (or vice versa)? If so, how are these typically addressed?**

All shareholders are prohibited from acting in their own interest for a purpose that goes against the company's interest and with the aim of negatively affecting other shareholders (*abus de majorité* and *abus de minorité*).

In addition, managers have, a duty of loyalty towards the shareholders, which originated from case law. This duty of loyalty is, however, restricted to information known by the manager and that is likely to have a significant influence on shareholders' consent.

**3.5 Are there any limitations or restrictions on the contents or enforceability of shareholder agreements (including (i) governing law and jurisdiction, and (ii) non-compete and non-solicit provisions)?**

Shareholders' agreements can be drafted with extensive freedom. Still, they should refrain from derogating from the

company's articles of association to avoid difficulties, and they must comply with public order provisions. Subject to the above, shareholders' agreements may include all types of provisions, such as non-competition and non-solicitation, which shall also comply with applicable case law.

**3.6 Are there any legal restrictions or other requirements that a private equity investor should be aware of in appointing its nominees to boards of portfolio companies? What are the key potential risks and liabilities for (i) directors nominated by private equity investors to portfolio company boards, and (ii) private equity investors that nominate directors to boards of portfolio companies?**

PE investors must always ensure that their nominees have the legal capacity to act as board members.

The liability of board members is mostly collective: should a decision made by the board be improper and a source of liability, all the board members are deemed jointly and severally liable unless they can prove that they behaved with proper care and opposed the contested decision. This mainly explains why PE investors sometimes avoid appointing representatives to the board. If they must do so, they generally require the portfolio company to subscribe to liability insurance covering the board members' liability (see question 11.6 below for insurance protection mechanism).

As far as PE investors are concerned, they are not exposed to liabilities as such, being shareholders, provided they do not excessively interfere with the company management and have not commingled their assets with those of the portfolio companies, otherwise their corporate veil of the limited liability may be pierced.

**3.7 How do directors nominated by private equity investors deal with actual and potential conflicts of interest arising from (i) their relationship with the party nominating them, and (ii) positions as directors of other portfolio companies?**

French law provides a basic procedure to handle conflicts of interests from the angle of related-party agreements (*conventions réglementées*). However, this procedure is insufficient to deal with all conflicts of interest. We advise portfolio companies to set up internal rules regarding conflicts of interest.

## 4 Transaction Terms: General

**4.1 What are the major issues impacting the timetable for transactions in your jurisdiction, including antitrust, foreign direct investment and other regulatory approval requirements, disclosure obligations and financing issues?**

Main issues impacting the timetable for French transactions generally are:

- before signing (binding agreement): prior-consultative opinion of the employees' representative bodies and/or prior information of employees (in companies with less than 250 employees qualifying as SMEs);
- before closing: clearances from (i) the French Competition Authority (Autorité de la Concurrence) or the EU Commission as the case may be, (ii) the AMF for listed companies, or (iii) the Ministry of Economy, Finance and Recovery in the case of investment in companies operating in sensitive industries; and

- usual practical issues, on a case-by-case basis, such as due diligence or financing structures (requiring equity and debt commitment letters with certain funds commitments).

#### 4.2 Have there been any discernible trends in transaction terms over recent years?

While economic and geopolitical uncertainties are weighing on transactions in all Western countries, the French economy seems to show signs of resilience, even though there was a deceleration in PE activities in France in 2022, reflecting the reluctance of banks to finance certain transactions and rising interest rates.

## 5 Transaction Terms: Public Acquisitions

#### 5.1 What particular features and/or challenges apply to private equity investors involved in public-to-private transactions (and their financing) and how are these commonly dealt with?

Although PE actors have expressed more interest in publicly listed companies (mainly due to lower valuation than non-listed assets), these transactions remain uncommon in France because the AMF will generally reject any offer conditional upon reaching the squeeze-out threshold. Indeed, PE investors would usually carry out public-to-private transactions by: (i) acquiring shares of the target listed company to reach the 90% threshold of the share capital and voting rights, typically by resorting to leverage; and then (ii) triggering the squeeze-out procedure to acquire the remaining shares of the listed company.

#### 5.2 What deal protections are available to private equity investors in your jurisdiction in relation to public acquisitions?

Unlike private acquisitions (see question 6.8 below), break fees are common in public transactions. The target can provide exclusivity undertakings to the bidder, but the board of directors must consider any offer from alternative bidders. Undertakings from key shareholders to tender their shares are also lawful, but they must be disclosed and automatically terminated if a competing bid is launched.

## 6 Transaction Terms: Private Acquisitions

#### 6.1 What consideration structures are typically preferred by private equity investors (i) on the sell-side, and (ii) on the buy-side, in your jurisdiction?

While the completion accounts' structure remains the most used, the locked-box mechanism has become increasingly popular. Most of the transactions involving PE investors are based on locked-box whereas trade sellers generally use completion accounts.

Sellers tend to prefer the locked-box due to the simplicity and increased certainty of this mechanism, while purchasers tend to prefer the completion accounts, ensuring the price's accuracy. In situations where the closing date is expected to be very distant, the completion accounts mechanism makes more sense for all parties.

Regardless of price structure, deferred purchase price through earn-out clauses is common in PE transactions but is a breeding ground for litigation.

#### 6.2 What is the typical package of warranties / indemnities offered by (i) a private equity seller, and (ii) the management team to a buyer?

PE sellers typically refuse to provide warranties and indemnities beyond fundamental representations (such as title to shares, power and authority, or the company's capital structure). Managers are usually key as part of the transaction. Negotiating warranties with them is a sensitive matter, and they tend to offer rather limited warranties to the buyer.

#### 6.3 What is the typical scope of other covenants, undertakings and indemnities provided by a private equity seller and its management team to a buyer?

As a principle, PE sellers try to resist providing any kind of restrictive undertakings, but no leakage covenants in case of "locked-box" deals and undertakings in connection with the conduct of business until closing are typical. Managers are commonly bound by non-competition and non-solicitation undertakings.

#### 6.4 To what extent is representation & warranty insurance used in your jurisdiction? If so, what are the typical (i) excesses / policy limits, and (ii) carve-outs / exclusions from such insurance policies, and what is the typical cost of such insurance?

Representation & warranty insurance used to be very rare but has become much more popular, although there remains a significant margin for development. The cost and conditions of the insurance vary depending on target companies. We nevertheless notice that most insurance companies have their list of non-negotiable exclusions (e.g., criminal matters or risks identified in the due diligence) and that specific risks are excluded depending on the deal or target's industry.

#### 6.5 What limitations will typically apply to the liability of a private equity seller and management team under warranties, covenants, indemnities and undertakings?

Fundamental warranties are usually not subject to any limitations except a cap at the purchase price level. PE sellers and management teams usually refuse to be bound by other liabilities. If additional liabilities are necessary for the deal to go through (e.g., in the context of a purchase by a corporate buyer – see question 6.2 below), PE sellers and management teams will endeavour to restrict their liabilities as much as possible.

In the case of "locked-box" deals, any leakage will be recoverable from the sellers without a cap.

#### 6.6 Do (i) private equity sellers provide security (e.g., escrow accounts) for any warranties / liabilities, and (ii) private equity buyers insist on any security for warranties / liabilities (including any obtained from the management team)?

PE sellers are strongly opposed to providing security, which is correlated to the fact that they are usually only liable for breach of fundamental warranties, which rarely occurs in practice.

PE buyers usually request extensive representations and warranties from sellers and the management team, backed by a security such as escrow accounts or first-demand bank guarantees. However, in the case of purchase from PE sellers, such

as in the context of a secondary buyout, the representations and warranties tend to be very limited and, accordingly, securities are very rarely provided.

**6.7 How do private equity buyers typically provide comfort as to the availability of (i) debt finance, and (ii) equity finance? What rights of enforcement do sellers typically obtain in the absence of compliance by the buyer (e.g., equity underwrite of debt funding, right to specific performance of obligations under an equity commitment letter, damages, etc.)?**

PE buyers can provide comfort regarding the availability of financing by providing the sellers, together with their binding offers, with equity and/or debt commitment letters with certain funds commitments.

The extent of the enforcement rights depends on the contractual arrangements with the banks and investors. Investors generally irrevocably undertake to fund the acquisition vehicle under equity commitment letters. If the acquisition vehicle is sentenced by a court to pay damages in case of default/breach of its contractual undertakings, as per the equity commitment letter, the financial sponsors will be required to pay said damages. This risk is, however, remote as French courts are reluctant to award significant damages.

**6.8 Are reverse break fees prevalent in private equity transactions to limit private equity buyers' exposure? If so, what terms are typical?**

Reverse break fees are not prevalent in the context of PE transactions.

## 7 Transaction Terms: IPOs

**7.1 What particular features and/or challenges should a private equity seller be aware of in considering an IPO exit?**

French IPOs are generally considered a time-consuming and costly process, subject to various legal and regulatory constraints and specific rules regarding acquisition or disposal of shareholdings.

French listed companies are also subject to higher scrutiny in terms of transparency requirements, including for corporate governance practices.

Sellers must pay particular attention to financial market conditions. French IPOs are subject to market fluctuations and volatility, sometimes leading to a delay or termination of the process due to insufficient pricing conditions.

In terms of sellers' rights, any existing shareholders' agreement would be terminated as a result of the IPO. Accordingly, sellers' governance, financial and other specific rights would not be maintained, and share transfers restrictions would be terminated. A new shareholders' agreement, including sometimes board veto rights and potential shares transfer restrictions (such as lock-up – see below), may be implemented post-IPO.

Regarding selling conditions, the company must declare in the IPO prospectus certain disclosures, based on which its shareholders may obtain indemnification post-completion in case of misleading disclosures.

**7.2 What customary lock-ups would be imposed on private equity sellers on an IPO exit?**

Terms and duration of lock-up provisions vary depending on the company's particulars, market conditions and parties' negotiations, but sellers are generally asked to grant lock-ups for a duration varying from 90/180 days to 365 days.

**7.3 Do private equity sellers generally pursue a dual-track exit process? If so, (i) how late in the process are private equity sellers continuing to run the dual-track, and (ii) were more dual-track deals ultimately realised through a sale or IPO?**

In France, PE exits mostly occur through M&A transactions or secondary buyouts. Exits through IPOs have been limited on the French market in the past year and first trimester 2023 compared to 2021, mainly due to a shift in markets with inflation and rising interest rates, which explains why dual-track exit strategies are rarely pursued in France.

## 8 Financing

**8.1 Please outline the most common sources of debt finance used to fund private equity transactions in your jurisdiction and provide an overview of the current state of the finance market in your jurisdiction for such debt (including the syndicated loan market, private credit market and the high-yield bond market).**

The most common sources of debt finance used to fund PE transactions in France are debts provided by traditional lenders (banks) through syndications or clubs. This financing generally involves various types of loans including term loans to refinance the company's existing debt and revolving credit facilities.

Other debt products are increasingly used to fund PE transactions (exclusively or in addition to traditional senior secured bank loans), such as mezzanine loans, uni-tranche financing, second lien loan and/or quasi-equity instruments such as bonds (straight bonds or bonds into shares).

Transactions can alternatively be financed by private placements and/or high-yield bonds provided by institutional investors, such as pension funds, insurance companies, and asset management firms.

**8.2 Are there any relevant legal requirements or restrictions impacting the nature or structure of the debt financing (or any particular type of debt financing) of private equity transactions?**

French law prohibits the acquired companies and their subsidiaries from providing any financing or granting any guarantee or security interest over their assets to secure the purchase or subscription of their own shares (financial assistance rules). Therefore, it is generally the acquiring vehicle that provides guarantees or security interests over its own assets (including the target company's shares) and sometimes downstream guarantees.

**8.3 What recent trends have there been in the debt-financing market in your jurisdiction?**

The reduction of banking monopoly prohibitions has led to a surge in competition among lenders in the debt-financing market in France. Furthermore, as interest rates are continuously

increasing in France over the last months, it became costlier for PE funds to borrow and leverage expensive LBOs. This mainly explains the increase in the number of private debt funds and alternative lenders, providing additional sources of debt to support PE investments.

Unitranche financings (providing a simplified debt structure, which combines senior and subordinated debt into a single facility) are also increasingly popular in France.

Environmental and ESG considerations have gained importance in the debt-financing market (certain lenders increasingly incorporating sustainability criteria into their investment decisions and financing terms).

## 9 Alternative Liquidity Solutions

### 9.1 How prevalent is the use of continuation fund vehicles or GP-led secondary transactions as a deal type in your jurisdiction?

General Partner (GP)-led secondary transactions (where GPs decide to sell one or more portfolio companies from a fund they manage to a new investment vehicle (continuation fund) managed by the same GPs) have been increasingly considered since the pandemic, mainly due to downward valuation trends. This deal structure, however, remains challenging to execute mostly due to difficulties in establishing a market price (allowing a return) and in dealing with management teams and investors.

### 9.2 Are there any particular legal requirements or restrictions impacting their use?

Before implementing this process, it must be ensured that the assets transferred to the continuation fund are free from any third-party rights (pursuant to any shareholders' agreement or similar) and that the consent of the primary fund's advisory board is secured. Certain customary provisions of the contractual documentation (including tag-along and drag-along provisions) must be adjusted to cover risks related to the use of continuation funds and conflicts of interests that may arise in connection thereof.

Managers must then identify which of the LPs are willing to sell and receive their sale price in cash or to reinvest all or part of their proceeds – before determining the valuation.

## 10 Tax Matters

### 10.1 What are the key tax considerations for private equity investors and transactions in your jurisdiction? Are off-shore structures common?

PE transactions in France usually benefit from the combination of two favourable tax provisions:

- the buying and target companies may elect for the tax consolidation regime, notably subject to a minimum 95% holding requirement, under which: (i) the operational benefits of the subsidiaries are compensated with the tax losses usually incurred by the acquiring company; and (ii) the subsidiaries contribute the equivalent of the tax they would have incurred, had they not been included in the tax consolidated group, to the buying entity that can use that cash flow to pay the interest and/or principal of its acquisition loans; and
- interest incurred by the buying company, as well as acquisition and financing costs, are tax deductible even though

dividends or capital gains derived from its investments are mostly tax exempt. Anti-hybrid measures, thin capitalisation rules and transfer pricing requirements may, however, limit the effective amount of deductible interest.

Buying companies are frequently activated (holding *animatrice*) to allow VAT recovery on acquisition costs.

Off-shore structures are expected to become less and less frequent, following implementation of several European directives including DAC6 reporting obligations and ATAD III measures against shell entities, and the evolution of domestic case law enhancing tax authorities' powers to discard foreign holding companies lacking substance.

### 10.2 What are the key tax-efficient arrangements that are typically considered by management teams in private equity acquisitions (such as growth shares, incentive shares, deferred / vesting arrangements)?

Free share plans and, for start-ups, BSPCEs benefit from a relatively advantageous and, more importantly, reliable tax and social security regime.

Outside these regimes, a choice must be made between ordinary salaries, which are subject to high employer and employee social charges and up to 45% income tax, and capital investment, for which profits are only subject to a 30% flat tax (or an even lower one in certain investment plans (*plan d'épargne en actions*)). A 3% or 4% exceptional tax on high income may also apply in any case. Whilst very efficient, caution must be taken in structuring investment schemes aimed at applying the capital gains taxation regime, as these are often considered disguised remuneration by the French tax authorities, notably in the context of sweet equity schemes, preferred shares, deferred/ vesting arrangements, or good/bad leaver put and call options.

### 10.3 What are the key tax considerations for management teams that are selling and/or rolling over part of their investment into a new acquisition structure?

Rolling over part of their investment usually benefits from a tax deferral regime in the hands of the management teams, which can be a strong incentive. Selling shares triggers capital gain tax under the 30% flat tax regime; earn-out payments are usually efficient as they are only subject to tax when effectively due.

In the context of MBOs especially, the sale of shares to the new HoldCo by initial managers who retain a controlling interest in the new structure can trigger the application of an additional limitation rules, if a tax consolidation regime is implemented, on the tax deductibility of interest (*Amendement Charasse*).

### 10.4 Have there been any significant changes in tax legislation or the practices of tax authorities (including in relation to tax rulings or clearances) impacting private equity investors, management teams or private equity transactions and are any anticipated?

French tax environment has recently been relatively stable.

In 2018, business-favourable measures were adopted (e.g., the 30% flat tax on all investment income for individuals and the progressive reduction of corporate income tax).

PE deals were substantially impacted by recent decisions of the French highest Court on management incentive plans, which ruled that capital gains realised by managers qualify as employment income even when they invested money, at fair market value and at risk, if the gain realised is directly or



indirectly linked to the existence or execution of the employment/management contract. PE actors are thus increasingly turning to free share plans.

## 11 Legal and Regulatory Matters

**11.1 Have there been any significant legal and/or regulatory developments over recent years impacting private equity investors or transactions and are any anticipated?**

The antitrust and foreign investment regulations have been enhanced over the past few years and now apply to a larger scope of transactions, including PE transactions. Further, recent French case law relating to the tax treatment of management packages may cause difficulties in PE transactions. Finally, the current trend for ESG considerations, the implementation of the duty of vigilance regulation in France, the issuance of the EU taxonomy and sustainable finance disclosure regulations (SFDR), and the forthcoming EU corporate sustainability reporting directive regulation (CSRD) are likely to drive PE investments.

**11.2 Are private equity investors or particular transactions subject to enhanced regulatory scrutiny in your jurisdiction (e.g., on national security grounds)?**

As part of the growing interest in ESG considerations and the development of the socially responsible investment movement, PE funds are subject to further scrutiny regarding their application of the Taxonomy/SFDR regulations, which provide for a self-classification system to distinguish “green” investments from others. The AMF has recently issued proposals for a more rigorous regulation implementing at the EU level minimum environmental requirements, which financial products would have to meet to be classified as a green investment under Taxonomy/SFDR regulations to avoid any greenwashing practices.

**11.3 Are impact investments subject to any additional legal or regulatory requirements?**

Impact investments are primarily regulated by soft law under which PE actors or companies are looking to comply with some labels, such as Bcorp label, which is awarded to commercial companies that meet societal, environmental, governance, and public transparency requirements, or GreenFin label, which guarantees the green quality of investment funds. However, under the influence of the EU, the impact investment sector is increasingly subject to hard law regulations.

**11.4 How detailed is the legal due diligence (including compliance) conducted by private equity investors prior to any acquisitions (e.g., typical timeframes, materiality, scope, etc.)?**

Usually, PE investors require full due diligence reviews before buyout investments but may fix different materiality thresholds depending on the reviewed areas. Such DD reviews may last from four to six weeks. Regarding VC transactions relating to

early-stage companies, DD reviews may focus on specific areas, such as IP about tech companies, and are usually shorter (usually three to four weeks). Scope, materiality, and areas of the DD reviews may always vary from investor to investor.

**11.5 Has anti-bribery or anti-corruption legislation impacted private equity investment and/or investors' approach to private equity transactions (e.g., diligence, contractual protection, etc.)?**

Anti-bribery and anti-corruption French regulation has been strengthened over the past few years, including with the French act known as “Sapin II”, which requires large companies to implement a compliance programme to prevent acts of bribery and corruption. The EU Commission is also currently seeking to harmonise the anti-bribery between all its members, by setting minimum standards. Therefore, PE actors are paying greater attention to such compliance, as is the case for ESG compliance/considerations.

**11.6 Are there any circumstances in which: (i) a private equity investor may be held liable for the liabilities of the underlying portfolio companies (including due to breach of applicable laws by the portfolio companies); and (ii) one portfolio company may be held liable for the liabilities of another portfolio company?**

PE funds are careful and unlikely to exercise any management duties over the activities of the portfolio companies, to avoid attracting any liability (see question 3.6 above).

PE investors usually implement several protection mechanisms preventing them from being liable due to a breach of a portfolio company. HoldCo is usually incorporated under the form of a limited liability company. Further, the investor's representative may be appointed as a member of supervisory bodies within a portfolio company with limited powers, excluding any managerial power or function.

PE investors may require the portfolio company to, in any case, subscribe to liability insurance covering the members of its corporate bodies.

## 12 Other Useful Facts

**12.1 What other factors commonly give rise to concerns for private equity investors in your jurisdiction or should such investors otherwise be aware of in considering an investment in your jurisdiction?**

In the vein of France 2030 (i.e., a EUR 54 billion programme that aims at enabling France to close the industrial gap, invest massively in innovative technologies and support the ecological transition and the correlative French Tech label), French President Emmanuel Macron has recently announced a new EUR 500 million programme dedicated to artificial intelligence (AI). France intends to remain an attractive and active investment place in various sectors, focusing on tech, health, AI, and ESG-related sectors.



**Lisa Becker** is a Partner in the M&A/Corporate department of Vivien & Associés. Of French nationality, Lisa has been an Attorney-at-Law and member of the Paris Bar since 2013. Focusing her practice on corporate law and M&A, Lisa advises French and international groups in the context of domestic and cross-border acquisition (both buy-side and sell-side), restructuring (including merger, spin-off or partial asset contribution) and joint-venture transactions. She also regularly focuses on capital-investment transactions either alongside companies working on their development and growth, or investors.

**Vivien & Associés AARPI**  
3, rue de Monttessuy  
75007 Paris  
France

Tel: +33 1 45 02 39 50  
Email: [lisa.becker@va-fr.com](mailto:lisa.becker@va-fr.com)  
URL: [www.va-fr.com](http://www.va-fr.com)



**Julie Tchaglass** is a Partner in the M&A/Corporate department of Vivien & Associés. Of French nationality, Julie has been an Attorney-at-Law and member of the Paris Bar since 2013. Her practice focuses on international M&A, PE transactions including leveraged acquisitions (LBOs), capital investment transactions (advising both start-ups and investors), joint-ventures, and general corporate and commercial assistance, representing French and foreign buyers and sellers (whether listed or unlisted) and PE institutions.

**Vivien & Associés AARPI**  
3, rue de Monttessuy  
75007 Paris  
France

Tel: +33 1 45 02 39 50  
Email: [julie.tchaglass@va-fr.com](mailto:julie.tchaglass@va-fr.com)  
URL: [www.va-fr.com](http://www.va-fr.com)



**Marine Pelletier-Capes** is a Partner in the Tax department of Vivien & Associés. Of French nationality, Marine has been an Attorney-at-Law and a member of the Neuilly, then Paris Bar since 2000. Her practice focuses on French and international groups as well as groundbreaking start-ups for which she provides tax advice on complex acquisitions or reorganisation, and also more general corporate tax advice on daily management and structuring of the operations or in the context of tax audits or litigations. She has also developed individual taxation practices both in an international and in a domestic context, including regarding management packages.

**Vivien & Associés AARPI**  
3, rue de Monttessuy  
75007 Paris  
France

Tel: +33 1 45 02 39 50  
Email: [marine.pelletiercapes@va-fr.com](mailto:marine.pelletiercapes@va-fr.com)  
URL: [www.va-fr.com](http://www.va-fr.com)



**Julien Koch** is a Partner in the M&A/Corporate department of Vivien & Associés. Of French nationality, Julien has been an Attorney-at-Law and member of the Paris Bar since 2014. Julien regularly acts on behalf of French and international clients on cross-border and domestic M&A transactions (including acquisitions, disposals and intra-group restructuring), on capital-investment transactions (advising both start-ups and investors) and on industrial joint ventures and strategic alliances. Julien also intervenes in alternative dispute resolution processes as a mediator, mainly in the field of inter-company mediation.

**Vivien & Associés AARPI**  
3, rue de Monttessuy  
75007 Paris  
France

Tel: +33 1 45 02 39 50  
Email: [julien.koch@va-fr.com](mailto:julien.koch@va-fr.com)  
URL: [www.va-fr.com](http://www.va-fr.com)

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