THOUGHT LEADERSHIP

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LEGAL AND REGULATORY CONSIDERATIONS FOR MERGERS & ACQUISITIONS IN THE HEALTH & PHARMACEUTICALS INDUSTRY IN NIGERIA.

Introduction

> It has been reported that the increased investment by the Nigerian government in healthcare, pharmaceutical companies, product manufacturers and service providers in the health and pharmaceuticals (H&P) industry in Nigeria since the onset of the pandemic, has spurred great interest from private investors.[1]

These investments are quite important at a time like this when report by Knight Frank Research indicates that Nigeria falls short of the global average hospital bed-to-population ratio of 2.7 beds per 1000 people and requires significant investment in healthcare infrastructure. The country would require 386,000 additional beds and $82 billion of investment in healthcare real estate assets to reach the global average.

Over the years, mergers and acquisitions bring economies of scale that are not possible through organic growth. This article sets out the legal and regulatory considerations in a typical merger and acquisition transaction in the health & pharma industry in Nigeria. This article reviews the various legal considerations regarding M&A transactions in the H&P industry including legal due diligence, deal structure, transaction documentation, and regulatory approvals.

Legal due diligence

Legal due diligence is the process of collecting, understanding and assessing all the legal risks associated with a transaction. The legal due diligence process is extremely important as it affects the buyer's decision whether to invest in or acquire the target, on what terms, and for what price. legal due diligence may also be done on the buyer by the target in a transaction in which the target's shareholders are to receive shares of the buyer as part of the buyer's purchase price in acquiring the target.[2] Typically, companies involve in M&A in the H&P industry conduct legal due diligence on matters covering corporate, regulatory, financials, financings, personnel, intellectual property, tax, real and personal property, insurance, and litigation. During the course of the due diligence, issues discovered are either

1 https://www.cnbc.com/2021/01/04/nigerias-82-billion-health-care-gap-investors-stand-by.html
2 Mergers and Acquisitions: A Step-By-Step Legal and Practical Guide by Edwin L. Miller Jr.

resolved by the target and closed out or the buyer seeks protection under the provisions of the transaction documents or may even involve renegotiating the purchase price or some other terms of the transaction.

Deal structure

An important consideration in an M&A transaction in the H&P industry is the deal structure. There are different ways to structure an M&A transaction, the common basic structures are, asset sale, share sale and merger. An asset sale involves the sale of all or selected portion of the assets of the target to the buyer. In the H&P industry, such assets may include inventories, real estate assets, licenses, intellectual property rights, among others. In an asset sale, the buyer cherry picks the assets it will purchase and the liabilities it will assume. Share sale involves the sale of all or part of the shares of the target by its shareholders to the buyer. In a share sale, the assets and liabilities of the target remain with the target while ownership and title to the shares are transferred to the buyer. Merger involves the combination of two entities, in which only one entity survives as the merged entity, and the other entity is dissolved without being wound up. In a merger, the assets and liabilities of the dissolved entity is assumed by the surviving entity. Typically, the structure employed for an M&A transaction determines the kinds of documentation that would be prepared by the parties to the transaction.

Transaction documents

In an M&A transaction, parties in the early stages of discussion typically enter into a confidentiality agreement and a Term Sheet, these documents are not part of the transaction documents. They are basically documents to protect the interests of the target company and highlight preliminary understanding before the transaction is consummated. Confidentiality agreement is usually important to the target because the buyer at the discussion stage is likely to want to see a lot of information relating to the target, some of which may be confidential. The confidentiality agreement will deal with matters relating to confidentiality obligations imposed on the buyer, non-disclosure of discussions and information about the target, non-solicitation of employees, among others.

Term Sheet

The Term Sheet outlines the terms of the transaction that the parties have agreed upon in principle. Term sheet is interchangeably used as “Head of Terms” or “Head of Agreement” and it typically achieve the same objectives as a “Letter of Intent”. The Term Sheet only set out the key elements of the deal and are not supposed to bind the parties to proceed with the transaction. However, some provisions in the term sheet may be agreed by the parties to be binding, such provisions include confidentiality, exclusivity, governing law.

The key transaction documents in an M&A transaction are the share purchase agreement, asset purchase agreement, disclosure letter, scheme of merger.

Share Purchase Agreement

Share Purchase Agreement, also interchangeably used as a Share Sale Agreement or a Sale and Purchase Agreement sets out the obligations of the seller and purchaser in the acquisition of shares. It typically makes provision for the consideration agreed by the party, conditions to be fulfilled by the parties either before or after the completion of the transaction, the warranties of the seller and purchaser, limitation on liability, the mode of termination of the agreement, and other general terms. The share purchase agreement will usually have elaborate warranties as a schedule which are given by the seller. Where the buyer is acquiring an asset, the agreement entered will be an asset purchase agreement. However, where the target will be issuing new shares to the buyer, the agreement entered is a share subscription agreement. In a share subscription agreement, the seller is the target, and the target receives the consideration for the shares. There are instances where the share sale transaction involves both share purchase and share subscription, i.e., the buyers purchase shares from existing shareholders of the target and also subscribes to new shares issued by the target, the parties will usually enter into a share subscription and purchase agreement.

Disclosure letter

The Disclosure letter is a letter prepared by the seller in the transaction and includes general and specific disclosures regarding the seller's warranties in the acquisition agreement. The buyer will usually agree that the seller will not be liable for a breach of warranty where the matter giving rise to the breach was disclosed in the disclosure letter. A bundle of documents is usually attached to the disclosure letter to support the seller's disclosures.

Shareholders' Agreement

The shareholders' agreement is an agreement entered into between the shareholders of the target which provides definitive terms and conditions which will govern their relationship and participation in the target, as well as their respective responsibilities towards the financing and management of the operation, business and affairs of the target. In an event where the buyer is not acquiring all the equity stake of the company, the buyer will usually enter into a shareholders' agreement with existing shareholders.

Scheme of Merger

The scheme of merger is a court-approved agreement between the two merging entities. It makes provisions for the consideration of the merger, the mechanism for transfer of assets and liabilities, conditions precedent, benefits of the merger, treatment of employees of the merging entities, among others. The conditions precedent for the merger will typically include ratification of the merger by shareholders of the merging entities, the sanctioning of the merger by the court, among others. Mergers can also be achieved by way of Merger Agreement, Business Combination Agreement, Amalgamation Agreement.

Regulatory Framework

Parties involved in M&A transactions in the H&P industry in Nigeria require regulatory approvals before the implementation of the transaction. The regulatory approvals to be sought typically depends on the structure of the transaction, the parties involved and the consideration. Whilst some M&A transactions in the H&P industry may require seeking regulatory approvals from certain regulatory agencies, some others may not. Typical regulatory approvals required in respect of M&A transactions in the H&P industry in Nigeria are discussed below.

FCCPC Approval

Mergers, acquisitions, and joint ventures involving companies in the H&P industry in Nigeria are regulated by the Federal Competition and Consumer Protection Commission (FCCPC). The FCCPC is, by the relevant provisions of the Federal Competition and Consumer Protection Act (FCCPA), saddled with the responsibility of approving merger transactions subject to threshold set by the FCCPC. Accordingly, a proposed merger, acquisition and joint venture in the H&P industry must before being implemented first be notified to and approved by the FCCPC.

Under the FCCPA, only direct or indirect acquisitions of shares or assets that result in change in control of the target qualify as merger for merger review purposes. The FCCPA makes provisions for what constitutes control.

Foreign mergers in the H&P industry in Nigeria are also covered under the regulatory purview of the FCCPC. However, to be under the FCCPA, the foreign merger must, (i) involve foreign companies (though not registered in Nigeria) who produce goods and services sold into Nigeria, (ii) involve foreign companies that have a local nexus such as having subsidiaries in Nigeria.

To be notifiable, mergers must pass the turnover test. Under the Threshold Regulation,[3] a merger is notifiable if, in the year preceding the merger, (a) the combined turnover of the acquiring undertaking and target undertaking (combined figure) in, into or from Nigeria equals or exceeds One Billion Naira (N1,000,000,000), or (b) the annual turnover of the target undertaking in, into or from Nigeria equals or exceeds Five Hundred Million Naira (500,000,000). Thus, a small merger is a merger with a

3 Notice of Threshold for Merger Notification Pursuant to Section 93(4) issued by the FCCPC.

value at or below the threshold stipulated in the Threshold Regulation and is not required to be notified under the FCCPA, while a large merger is a merger above the threshold stipulated by the Threshold Regulation.

The FCCPC determines whether or not the merger is likely to substantially prevent or lessen competition and assesses the strength of competition in the relevant market and the probability that the undertakings in the market, after the merger, will behave competitively or cooperatively, taking into account any factor that is relevant to the competition in the market.

The parties to a notifiable merger may notify the FCCPC by paying the appropriate merger filing fees, providing such information in the prescribed manner and form as may be required by the FCCPC and submit all relevant documents to the FCCPC. Within 60 days of fulfilling the notification requirements, the FCCPC having after considered the merger in line with the provisions of the FCCPA will issue in the prescribed form, (a) approving the merger, or (b) approving the merger subject to conditions, or (c) prohibiting implementation of the merger.

NHIS Approval

The National Health Insurance Scheme (Now National Health Insurance Authority) was established under the NHIS Act 2004 by the Federal Government of Nigeria to improve the health of all Nigerians at an affordable cost, and it regulates private health insurance operated by Health Maintenance Organizations (HMOs). HMOs are key players in the H&P industry in Nigeria and their activities are regulated by the NHIS. Mergers and acquisitions by HMOs in the H&P require the approval of the NHIS. The NHIS by virtue of its power under the NHIS Act issued the NHIS Reviewed Operational Guidelines, 2012 (the Guidelines). The Guidelines provides that no HMO shall merge with, transfer to or receive from any other HMO its business or lives without the approval of the NHIS (Now National Health Insurance Authority) in writing.

The NHIS (Now National Health Insurance Authority) has a protocol for the approval of acquisition of HMO in Nigeria. The NHIS approval process is in milestones and the parties are required to complete all milestone requirements before the final approval is given.

According to the Guidelines, where an HMO transfers its business or is acquired or merged with another HMO without the approval of the NHIS, it shall not be given fresh accreditation.

SEC Approval

Public companies in the H&P industry involved in a merger, divestment, or take-over, are required to obtain the prior approval of the Securities and Exchange Commission (SEC) by virtue of the provisions of the Amendment to the Rule on Mergers, Take-overs and Acquisitions issued by SEC on 30th August 2021 (SEC Merger Amended Rules).

The prior approval of SEC is required for the purposes of undertaking a transaction in relation to:

i. merger, acquisition, combination, or other affected transactions between or among companies, involving acquisitions of shares, assets, business, or subsidiaries of a public company.

ii. disposal by the public company of a controlling stake or material assets, being assets, which value constitutes 15% or more of the total assets of the company.

iii. Take-over which involves the direct or indirect acquisition of 30 percent or more of the voting rights of a public company

Public companies in the H&P industry involved in a merger, acquisition, or divestments are required to file a notice accompanied with the relevant documents with the SEC.

The approval for mergers or acquisition is given by SEC if it is satisfied that all shareholders are fairly, equitably, and similarly treated and given suit client information regarding the transaction.

FIRS NO Objection

Companies involved in mergers, takeover, transfer or restructuring of its business are required to obtain prior direction and clearance from the Federal Inland Revenue Service (FIRS) in respect of taxes. Section 29 (12) of the Companies Income Tax Act provides that no merger, take-over, transfer or restructuring of the trade or business carried on by a company shall take place without having obtained the FIRS' direction and clearance with respect to any tax that may be due and payable under the Capital Gains Tax Act.

Conclusion

As highlighted above, there are several legal and regulatory requirements considered by parties in an M&A transaction in the H&P industry. These considerations help parties identify and determine the length of the transaction, the associated costs and ultimately inform the parties on the best structure to utilize for the transaction.

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