



WHAT M&A LAWYERS FIGHT ABOUT

Closing Your Deals on the Best of Terms

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Closing Your Deals on the Best of Terms



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SO WHAT EXACTLY DO M&A LAWYERS FIGHT ABOUT?

- As taken from the SRS 2019 Deal Points Study
 - 1,200 deals from 2014 to 2019
 - » Most undisclosed
 - 60% were \$100M or less; 40% greater
 - Link to SRS and ABA are in the handout
- Also from our collective experience

A COUPLE KEY POINTS ABOUT DEAL POINTS STUDIES

- They are backward looking and may not be relevant to your specific facts
- The more leverage one party has the more likely they will have the result in the study that skews to their favor
 - If the other side needs the deal, you may prevail despite the stats: you can be more firm in your negotiating position

MARTY: CONSTRUCTIVE VS. ACTUAL KNOWLEDGE: WHO HAS TO KNOW?

- 89% of deals use constructive knowledge
- 52% use a “reasonable” or “due” inquiry standard (they’re deemed to know what they’d know if they conducted “reasonable / due inquiry,” whether they did or not).
- 21% have a role-based constructive knowledge (you’re deemed to know what someone in that role would usually know)
- Risk allocation function

TIM: NO UNDISCLOSED LIABILITIES REP: 60/40 BUYER VS. SELLER-FRIENDLY DEFINITION

- Pro-buyer: covers any liability
- Pro-seller: limited to liabilities that should be on the financials
- Lots of things can be contingent liabilities not usually disclosable on the balance sheet
- Again, risk allocation

PAUL: 91% OF DEALS HAVE A MATERIALITY SCRAPE

- What's a scrape? (see handout)
- 37% for determining damages only (more seller-friendly)
- 47% for determining both breach and damages (buyer-friendly)
- Separates diligence from indemnity
- Minimum claim sizes also on the rise

TIM: DEDUCTIBLES GROWING; FIRST DOLLAR SHRINKING

- 31% of deals had deductibles in 2015; now 50% of deals
- Buyers acknowledging reality they don't want to pursue small claims
 - Small dollars
 - Don't want to upset key employees
- And basket size shrinking: 93% of deals at 1% or lower
 - Function of larger deals

PAUL: WHAT'S A “FUNDAMENTAL” REP?

- Fundamental reps are:
 - excluded from the basket
 - have higher caps (at the purchase price)
 - typically survive longer
- They usually include:
 - Capitalization
 - Due authority
 - Taxes
 - Fraud (but less on intentional misrepresentation)
 - No conflicts only at 39%

STEPHANIE: ESCROW / HOLDBACK SIZE

- Trends around 10%
- Larger for deals under \$50M
- Length of escrow: 12, 18 months?

ALL: STUFF WE FIGHT ABOUT POST-CLOSE

- Bonus: not in the study!
- Founder issues can make deals more risky / problematic:
 - Poor record keeping leads to more risk on the buyer, deals taking longer
 - Sellers need good advisors to understand what's market and how deals work
 - Employment agreements can be key to avoid “founder flight”

MORE ON FOUNDER / SMALL COMPANY ISSUES

- Founders can become emotionally attached to their “baby”; may want to dictate post-closing processes: important to be very clear about expectations in the document
- Different risk tolerances than sophisticated buyers—may not understand the risks they are being asked to take are typical
- Difficulty living in a corporate environment with more policies and procedures: important in the agreement and practice
- Founders are typically used to running the show, not having to report to corporate
 - Importance of non-competes: 3 vs. 5 years (people do leave)
 - Big company vs. entrepreneurship cultures
- Good internal processes: e.g., control download of sensitive info

OTHER POST-CLOSING ISSUES

- Earnout calculations
 - Failure to meet earnout targets can result in hurt feelings / litigation
- Integration issues: cultural mesh?
 - Potentially the biggest issue in M&A
 - Different industries have different cultures
- Transition of knowledge from deal team to the integration / day-to-day management team
 - Who owns the knowledge? Employment terms; earnout terms.

Thank you!



Questions? Please feel free to
contact me any time for guidance.

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