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# Introduction to Accounting

### Sources of Accounting Standards

|  |  |
| --- | --- |
| **Generally Accepted Accounting Principles (GAAP)** | **International Financial Reporting Standards (IFRS)** |
| * Industry accepted accounting terms * The law doesn’t just come from one source * Sources include:   + CPA Handbook (primary source)   + Emerging Issues Committee Abstracts   + Foreign Accounting Recommendations   + Textbooks, Articles and Journals   + Common Practice in a Particular Industry   + Accountant’s Professional Judgment applying fundamental accounting principles * \*\*Don’t limit definition exclusively to CPA Canada Handbook as you may miss a source | * Accounting standard set by the International Accounting Standards Board * IASB has 14 members form a diverse range of countries * Since Jan 2011, all publicly accountable enterprises in Canada are required to apply IFRS   + Including some Crown Corps |

Despite many people thinking so, IFRS has NOT replaced GAAP

Accounting for lawyers is important for a number of reasons:

* Due Diligence 🡪 spotting red flags
* Valuation methods 🡪 Shareholder agreement provisions
* Financial definitions of contracts 🡪 Ratio definitions for debt-incurrence covenants, borrowing bases etc.
* M&A purchase price adjustments and earn-outs 🡪 Post-closing working capital adjustment, shareholders equity or net worth adjustments
* Securities offerings or lending transactions 🡪 Annual financials, quarterly financials, pro-forma financials
* Bankruptcy proceedings
* Review potential liabilities, reserves and contingencies 🡪 to assess risk management, accruals/reserves, litigation etc.
* Personal balance in family disputes 🡪 Lists of assets and liabilities for purposes of determining allocation of property
* Litigation involving accounting fraud or non-compliance 🡪 Settlement offers
* Tax 🡪 transfer pricing

### General Accounting Principles

The Account

* **Account**: files for storing financial info
* **General Ledger (G/L)**: filing cabinet for all the different accounts
* **Financial Statements**: organized summary of the raw financial info contained in the G/L accounts

Fundamental Accounting Principles serve to present fairly and accurately all types of statements:

* **Historical Cost**: Assets recorded and reported in FS at original cost to the business, NOT at FMV of current asset
* **Matching (Accrual)**: Revenues and expense matching to the periods in which they were earned/incurred, NOT received
* **Conservatism**: if uncertainty of whether either expenses, liabilities, or losses have been incurred, they should be recognized in the FS
  + When in doubt, choose the option that will be at least likely to overstate assets income
  + Ex. lower of historical cost and market for inventory and temporary investments
* **Consistency**: Accounting principles and policies should be applied consistently from period to period so that readers can compare performance from one year to another
* **Materiality**: Something is material if a misstatement/omission would influence the judgment or a reasonable person
  + Must always be disclosed (this may be diff from materiality test for securities leg)
  + What is material may differ from contract to contract (not all assets/liabilities will be on a balance sheet.)

|  |  |  |
| --- | --- | --- |
| **Types of Financial Statements** | | |
| **Statement** | **Description** | **When?** |
| **Balance Sheet** | **Financial position reporting on assets, liabilities, and ownership equity**  Formula: Assets = Equity + Liabilities   * But, includes net income through retained earnings * Retained earnings = opening retained earnings + net income/loss – dividends   **Assets**   * Liquid ones are usually first * Ex. Cash and cash equivalents, short term investments, accounts receivable, inventory, prepaid investments, land etc.   **Liabilities and Equity**   * Liabilities 🡪 accounts payable, wages payable, dividends payable, taxes payable, etc * Equity 🡪 share capital, retained earnings | At a specific date |
| **Income Statement (Statement of Earnings)** | **Measures the success of operations**  Formula: Income = (revenues – expenses) + (gains – losses)   * Revenues 🡪 sales, services, fees, rental revenue * Expenses 🡪 costs of goods sold, selling expenses, general admin expenses * Gains 🡪 increase in equity – sale of equipment, land, investments * Losses 🡪 decrease in equity – loss on sale of equip, land, investments   Revenue/expenses, profit/loss report, company income, expenses, profits | For a period of time |
| **Cash Flow Statement** | **Measures and highlights cash inflows and outflows**  Cash and cash equivalent flow activities: operating, investing and financing activities | For a period of time |
| **Notes** | Info added to explain line items in the FS and explain the company’s financial condition (ex. debt, going concern criteria, accounts etc) | -- |

**Types of Statements**

* **Internal Statements** produced Weekly/Monthly/Quarterly/Yearly
* **Reports/Work**
  + Compilation: Raw data into a format with no analysis
  + Review: External auditors inquiring into data, but not as extreme as an audit (halfway house)
  + Audit: In depth review based on risk and materiality
    - Ex. maybe look ONLY at trans over $2M
* **Auditors Report**
  + To ensure the financial statements are not materially misstated
  + Auditor’s Report
  + Types of Opinion
    - Qualified Opinion: place where there is only a little info
    - Adverse/denial opinion: when FS are materially misstated

**Retained Earnings = net income (revenues - expenses) + retained earnings – dividends**

Double Entry Bookkeeping

* Every entry involves recording debits and credits of equal aggregate value
* Accounting equation must always stay in balance after each transaction

T-Accounts

* The “T” account: For every debit (left side), there must be a credit (right side)
* Assets – debit to increase, credit to decrease
* Labilities – debit to decrease, credit to increase
* Equity – debit to decrease, credit to increase

# Accounting and Financial Analysis

### Financial Statements

As a lawyer, when looking at financial statements you must:

* Read the notes in the balance sheet
  + On what basis did they end up with that number?
  + How did they define each term?
* Examine company’s capital structure
* Look for key trends and risks
  + Company moving through cash quickly? Too much debt?
  + Read the MD&A disclosure
* Look for potential liabilities/contingencies
* Always read balance sheet with diligence in mind

**Best Buy Balance Sheet**

Initial High-level Observations

* Timing
  + Balance sheet reflects a specific point in time (choice of year end is selected by the company)
    - For retail stores, having a floating year end on a weekend is common so inventory counts are less disruptive
* Consolidation
  + Balance sheet reflects the entire enterprise – parents and subs (so for the Best Buy example, this is the entirety of the enterprise, Canada and US)
    - Subs are gen based on 50% ownership threshold
    - Non-wholly subs result in no-controlling interests on the balance sheet
    - Minority interests don’t qualify as subsidiary
* Absence of contra accounts in certain cases
  + Contra accounts reduce the value of specific balance sheet items
    - Ex. allowances for doubtful accounts reduces accounts receivable; accumulated depreciation reduces fixtures and equipment
  + Certain balance sheet accounts are instead presented on a net basis

**Current Assets** – Notes to Financial Statements

* **Cash is most liquid**
  + Restricted cash can sometimes be excluded from cash and working capital
  + Cash is less than 3 months
* **Receivables**
  + Receivables may be for sales on account to customers, customer credit sales, instalment sales
  + Must be presented net of an allowance for doubtful accounts
  + Decreased from 1.28B to 1.162B
    - Whether this is positive or negative will depend on whether this is a due to a decrease in sales or an increase in collections
    - Watch out for write-offs or bad debts, which could also be drivers for a decrease
* **Merchandise inventories** – represent the merchandise on the shelves and in warehouse
  + Must be presented at the lower of cost and market value
  + Decrease here in Best Buy from 5.17B to 5.05B
    - Generally they are good (show sales)
* **Property and Equipment** – Originally recorded at historical cost – must be presented net of accumulated depreciation

**Liabilities**

* Contingencies – Future litigation etc – will be quantified by analysts
* Commitments

**Equity**

* Capital Stock
* Additional paid-in capital – Only if Best Buy is selling Stock
* Retained Earnings
* Non-controlling interest

**Off-Balance Sheet Accounting**

* Why all the fuss?
  + Can change dramatically the valuation of a company and fail to disclose certain liabilities
  + Point is to manipulate the balance sheet
* Things include:
  + Operating Leases – changes to treatment of certain operating leases currently being debated
  + Guarantees of debt – typically in notes
  + Contingencies – disclosed in notes
  + Special Purpose Vehicles – though can be abused

Pro-Forma Balance Sheet

* Financials adjusted for the anticipated results of a transaction
  + Fictitious to show what something MIGHT look like – build in assumptions

EPS & EBITDA

* **Earnings Per Share** (EPS) = evaluates profitability measuring the income available for each share of common stock
  + Disclosed on the face of the income statement
  + Basic EPS formula: **Net income available for common shares / weighted average number of common shares outstanding**
    - Ex. if net income was 720k (no preferred SHH) over the 100 shares of common stock
  + Basic EPS doesn’t recognize potentially dilutive securities in the capital structure
  + Fully Dilutive securities = convertible into common shares
    - Income statement shows worst case scenario converting all securities
    - Would be represented as “Fully dilute earnings per share”
* **Earnings Before Interest Taxes Depreciation Amortization** (EBITDA) = gauge of core continuum income of a company often used to compare core business of a company
  + A pro-forma figure creating that is NonGAAP/IFRS Figure

# Financial Ratios

A **Financial Ratio** is a ratio derived from financial information that compares key variables in a business. The purpose of a ratio is to alert a company, creditor and other parties that, once the financial ratio is reached, business practices may need to be changed.

Although GAAP and IFRS may have their own way of defining certain variables in financial ratios, each company (or even each financial statement) may have different definitions. The result could be a completely different picture of what people thought.

**As a result, when you are reading financial ratios, you MUST understand what the variable actually stands for (ie does Total Debt include litigation liabilities?)**

There are 3 primary categories of ratios:

* Purchase agreements (working capital adjustments)
* Leverage Ratios (financial covenant patterns)
* Liquidity Ratios (financial covenant patterns)

The big issues in Financial Ratios are:

* No universal formulas, no prescribed rules 🡪 it can be whatever you want it to be
* What question are you trying to answer?
* Needs to be negotiated
* Generally trying to assess risk

## Issues in Working Capital Adjustments: Purchase Agreements

When a purchase agreement is signed, it is not necessarily closed. Therefore, between the signed agreement and closing, there almost always is a working capital adjustment to account for the fluctuation of the assets and liabilities that arise within this period. **Working Capital** is the difference a company’s Current Assets (cash + cash equivalents) minus Current Liabilities.

Post-closing, usually the purchaser wants a broad definition of assets so as to include as many things contemplated in the purchase agreement to transfer to the purchaser (ex. all accounts receivable). On the other side, the seller wants assets narrowly defined (ex. accounts receivable for the next two months). Given that there is broad discretion on the drafter to define each term (ex. what constitutes accounts receivable, inventory value etc.), it is imperative that when reviewing purchase agreements, the reader understands what exactly each term means.

**Working Capital**

Current net Accounts Receivable + Inventory Value + Value of Prepaid Expenses & Deposits

Less

Excluded Assets + Current Accounts Payable and Accrued Liabilities

For example, one term in a **Post-Closing Purchase Price Adjustment** could be that within2-10 days before closing, both parties must do an inventory count, value that inventory count, and take that amount and reduce the purchase price by that amount so long as it is under $35k.

* Adjusted Net Working Capital was defined as the sum of all accounts receivable, prepaid expenses, and adjusted inventory
* They exclude the aggregate value of assets under 35k because for the size of deal they may be small assets

## Issues in Financial Covenant Patterns: Leverage Ratios

Leverage Ratios generally are there to assess different risks to a particular company. There are 5 main types of leverage ratios:

* Interest Coverage Ratio
* Fixed Charge Coverage Ratio
* Debt Coverage Ratio
* Debt-Asset Ratio
* Debt-Equity Ratio
* Debt-to-Cash Flow Ratio

Leverage Ratios primarily look at 2 types of risks

* **Repayment Risk**: The ability of the company to repay its short and long-term debt (focus on cash)
  + Generally measured by coverage ratios
* **Recovery Risk:** Degree to which assets exist to satisfy the debt upon a failure to repay (focus on assets)
  + Ie on liquidation, does a company have enough total assets to repay the debt?
  + Generally measured by debt ratios

### Coverage Ratios: *Repayment* Risk

There are 3 main Leverage Ratios that look to whether the company service the debt:

* Interest Coverage
* Fixed Charge Coverage
* Debt Coverage

#### 1. Interest Coverage Ratio

An **interest coverage ratio** looks at the difference between cash earned and money to meet current interest payments. It is sometimes seen as EBITDA / Interest Expense, but it depends on what you are trying to answer on a financial statement.

**TYPICAL FORMULA** 🡪 EBITDA OR Operating Free Cash Flow Before Tax

Interest Expense Total Cash Interest Payments

Some examples:

* “EBITDA means the Net Income of the Debtor determined in accordance with GAAP for the last four completed Financial Quarters:
  + **Plus**, Interest Expense, Income Tax Expense, Depreciation and Amortization Expense,
  + **Plus**, any other non-cash items reducing such Net Income.
  + **Minus**,
    - (i) all extraordinary, non- recurring and unusual items;
    - (ii) gains or losses on sales of Assets;
    - (iii) losses from write-downs; and
    - (iv) any other non-cash items increasing such Net Income (other than any non-cash items that were accrued in the ordinary course of business).
* “EBITDA means the aggregate earnings of the Borrower before interest, income and franchise taxes, amortization and depreciation, excluding extraordinary items, each as determined in accordance with GAAP consistently applied.”

There are a number of EBITDA definition issues:

* Capitalized operating costs not considered
* Non-operational revenues not excluded
* Required capital expenditures not considered
* What about unusual gains and losses?
* Income from affiliates should be excluded

#### 2. Fixed Charge Coverage Ratio

A **Fixed Charge Coverage Ratio** looks at the difference between cash earned and money to meet current fixed/contractual obligations.

* **Fixed Charge** = any cash payments (paid or payable during the relevant period) that the company has a contractual obligation to make.
  + Ex.payment of debt obligations, lease payments, mandatory dividend payments, etc.

**TYPICAL FORMULA** 🡪 Operating Free Cash Flow Before Tax

Fixed Charges (v broad)

For example, a sample ratio may be to “maintain a ratio of EMITDA to Fixed Charges for one financial quarter not less than 1:1” where “Fixed Charges” are defined as the aggregate of interest paid in cash during the period + principal payments

#### 3. Debt Coverage Ratio

A **Debt Coverage Ratio** looks at how long it will take to fully repay the total debt from internally generated cash flow.

* Essentially, it is a measure of long-term repayment risk
* Typically, to manage the debt effectively, companies need to look at debt maturity schedules to see when debt obligations are due

**TYPICAL FORMULA** 🡪 Total Debt

Operating FCF Before Tax

For example, a sample ratio may be to “maintain during each Financial Quarter a ratio of Total Debt to EBITDA for the four Financial Quarters of not more than 6.0:1”

### Debt Ratios: *Recovery* Risk

**Recovery Risk** is the ability of all assets to cover to fully repay all current and outstanding debt.

There are 2 main debt ratios:

* Debt-Asset Ratio
* Debt-Equity Ratio

#### 1. Debt-Asset Ratio

A **Debt-Asset Ratio** looks at the ability of all assets on liquidation to cover to fully repay total debt. The debt-asset ratio ONLY considers assets that have a liquidation value. Total debt should include legal claims, off-balance sheet liabilities etc. Alternatively, the definition of “debt” could restrict the definition to particular types of debt that is more relevant to the answer the ratio is attempting to provide.

**TYPICAL FORMULA** 🡪 Total Debt

Liquidated Value of Assets

For example, a sample ratio may be to “maintain a ratio of Total Debt to Total Tangible Assets of not greater than 0.75:1 …”

* “Total Tangible Assets means the aggregate book value of all assets and … MINUS the aggregate book value of all goodwill and other assets classified as ‘intangible assets’”
  + The aim is to exclude the realizable value not capable of being in the debt-asset ratio
* Total Tangible Assets here needs to be realizable assets capable of being liquidated
  + Ex. Restricted cash, inventory valuations, capitalized costs etc.

#### 2. Debt-Equity Ratio

A **Debt-Equity Ratio** looks at the extent to which a company is financially leveraged. In general, the definition of “Total Debt” should not be limited to a specific type of debt as it should show all debt relating to that entity relative to its equity.

* Larger the ratio (2:1, 6:1 etc) = the great the risk to creditors
* Total Debt = all debt
* Total Equity = Capital stock + contributed surplus + retained earnings

**TYPICAL FORMULA** 🡪 Total Debt

Total Equity

## Issues in Financial Covenant Patterns: Liquidity Ratios

### Liquidity Ratios: Assessing Short-Term Solvency

There are 4 main Liquidity Ratios:

* Current Ratio
* Quick Ratio (Acid Test)
* Cash Ratio
* Defensive Interval

#### 1. Current Ratio

A **current ratio** generally shows the relation between current assets and current liabilities at a given time.

* Higher Liquid Asset 🡪 Current Assets must become cash in one year
* Short-Term liabilities 🡪 Current Liabilities must be paid in one year
* Usually the assets and liabilities are very specifically defined so as to give an accurate snapshot of the current ratio

**TYPICAL FORMULA** 🡪 Current Assets

Current Liabilities

|  |  |
| --- | --- |
| **Common Current Assets** | **Common Current Liabilities** |
| * Restricted cash or marketable securities * Inventory valuations and obsolescence * Exclusion of prepaid expenses * Exclusion of deferred tax assets | * Related party payables (ex. supply contracts) * Future income tax liabilities * Current portion of long-term debt * Purchase and other contractual commitments |

For example, a sample ratio may be that “At any time, the ratio of Current Assets to Current Liabilities shall be greater than or equal to 1.10:1.0” where:

* “Current Assets (and Current Liabilities) means all items which would be classified as current assets (or current liabilities) on a consolidated balance sheet of the Borrower”

#### 2. Quick Ratio

A **Quick Ratio** generally shows the same thing as a Current Ratio (current assets minus current liabilities), but excludes from assets current inventory. This is because inventory is not something you can liquidate quickly, and the point here is to show to a lender the ability to repay a debt obligation

**TYPICAL FORMULA** 🡪 Current Assets – Inventories

Current Liabilities

#### 3. Cash Ratio

A **Cash Ratio** shows the same thing as a Current and Quick Ratio but it is with cash. The idea is to show the ability of a company to repay its short term debt. It is useful to creditors when deciding how much debt, if any, they would be willing to extend to the asking party.

* Similar issues with defining “current liabilities” “cash”

**TYPICAL FORMULA** 🡪 Cash

Current Liabilities

#### 4. Defensive Interval

A **Defensive Interval** is the number of days of operating expenses that could be paid with only the currently available quick assets. The idea is to show how long a business can continue to pay its bills.

* “Cash” 🡪 Cash, STIs, marketable securities etc
* “Accounts Receivable” 🡪 related party receivables
* “Total Cash Operating Expenses” 🡪 only ordinarily recurring expenses that are paid for in cash

**TYPICAL FORMULA** 🡪 Cash Items + Accounts Receivable

Total Cash Operating Expenses

# Asset Valuation

## Introduction

Why Business and Asset for Valuation?

* Highly used in litigation, tax, accounting, and M&A.
* We primarily care about:
  + **Professional valuation bodies** – in Canada, US and internationally that govern the valuation profession
  + **Non valuation bodies with interest in valuation** – accounting bodies, tax authorities, securities commissions and government sanctioned boards provide guidelines on valuation

There are a number of key value principles that guide the valuation process:

1. **Inadmissibility of hindsight** 🡪 what information is considered hindsight?
2. **Value at a point in time** 🡪 Value at what time? Each day/week/month it fluctuates
3. **Value is Prospective** 🡪 Historical information is only useful if it can be used as a guide for projecting future results
4. **Value ≠ price** 🡪 price is not necessarily the same as value
5. ↑ **higher tangible asset backing =** ↑ **higher value** 🡪 Evaluating the underlying tangible asset base is important
6. **Controlling Interest vs Minority Interest** 🡪 minority SHs don’t necessarily enjoy the same benefits as controlling SHs
7. **Liquidity** 🡪 liquidity and valuation
8. **Corroboration of Value** 🡪 valuation is an art, so there are reasonability tests to ensure their values are within a reasonable range
9. **Value terms and their use in practice** 🡪 FMV, fair value, market value, value to the owner, intrinsic value, etc.

## Valuation Methodologies

There are 3 primary approaches to asset-valuation:

* Income based approach
* Asset based approach
* Market approach

### Income-Based Approach

The **Income-Based Approach** is values assets primarily based on looking at income, expenses, the normalized cash-flow and how that can generate future income.

**FORMULA** 🡪 **Value = [Income x Multiplier] + Redundant Assets**

Where:

* **Value** = value of core operations
* **Income** = accounting income, cash flow, EBITDA, and revenue, among other things.
* **Multiplier** = measure the effect of aggregate spending over time, and is the factor by which gains in total output are greater than the change in spending that caused it.
  + A function of risk (↑Risk 🡪 ↓Chance in profit 🡪 ↓Multiplier).
  + Multipliers are derived from market statistics, empirical data, academic models, and professional judgment
  + Most multipliers will be in the range of 4-6
* **Redundant Assets** = the assets not necessary for business purposes (fancy cars, condo in Hawaii etc.)

### Asset-Based Approach

An **Asset-Based Approach** assesses the value of a company based on the FMV of the assets less the liabilities

It is used for a number of key categories:

* Holding companies
* Operating companies w/o commercial goodwill
* Non-viable companies (ex. small to medium sized contractors, construction company)
* Goodwill is much less of a consideration (hard to build cache with construction/home renovation etc.)

**FORMULA** 🡪 **Value = FMV of Assets – FMV Liabilities**

### Market-Based Approach

A **Market-Based Approach** is the current FMV that a company would be valued at. Ideally this is the preferred valuation technique, but it assumes a prudent seller AND buyer at all times in a given market.

Here, the value of the company is based off of public company trading multiples and transaction multiples

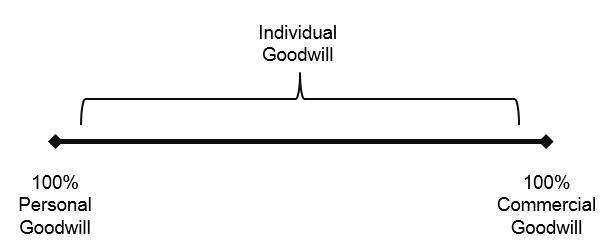
* Advantages: Theoretically superior (if proper “comps” identified), easy to apply, easily understood
* Disadvantages: Lack of detailed transaction data, no two companies are exactly alike, subjectivity is still a factor (professional judgment still impt)

## Goodwill

**Goodwill** is an intangible asset, often the most valued asset. It includes a number of the intangibles derived in business, like brand, trademarks, customer relationships, client lists, attractive location, IP etc. In short, goodwill is the value left over after removing the net tangible assets from all the business operations.

**FORMULA** 🡪 **Goodwill = Value of total business operations - Value of net tangible assets**

Goodwill can either be commercial or personal goodwill:

* **Commercial** **goodwill** 🡪 attaches to a business
  + Relatively high multiple
* **Personal** **goodwill** 🡪 attaches to a person
  + Relatively low multiple
* That said, goodwill can be converted from personal to commercial if:
  + Identify & mentor successors
  + Formalize & document processes
  + Share knowledge & transfer relationships
  + Emphasize corporate branding
  + Plan well ahead!

People can sell their individual goodwill but generally they are restricted in certain circumstances:

* Management contract
* Non-compete clauses
* Earn-out provisions

## Normalizing Income

**Normalized** earnings are earnings adjusted to remove the effects of seasonality, revenue and expenses that are unusual or one-time influences. Normalized earnings help business owners, financial analysts and other stakeholders understand a company's true earnings from its normal operations so as to better predict future performance.

The process of normalizing income includes:

* Income splitting w/ family members
* Addressing Personal expenses
  + Any personal expenses (e.g. university tuition for kids) gets added back on to the cash value (as if it had never been expended)
* Income/Expenses re redundant assets

## Factors Impacting the Multiplier

**Macroeconomic Specific Factors**

* Economic growth (GDP, etc.)
* Interest rates
* Availability of capital (debt & equity)
* Foreign exchange fluctuations

**Industry-Specific Factors**

* Barriers to entry
* Cyclicality
* Stage of life cycle
* Industry consolidation/“roll-up”
* Shifting consumer habits
* Technological change
* Government policies

**Company Specific Factors**

* Management depth 🡪 Transition plans – is there only one person who can run the company?
* Customer and/or supplier dependence
* Product & geographic diversification
* History of operating profits?
* Nature of value proposition
* Extent of tangible asset backing (“TAB”)
* Scalable or at capacity?
* Documentation of key procedures
* Sophistication of MIS
* Condition of plant and equipment

# Financial Disclosure in M&A

Public Companies

* **Annual Reports (AIF)** – HAS to be complete
* **MD&A** – Contains some information that won’t be in the FS
* **Notes to the Financial Statements**
* **Auditors Report**
* Canadian Securities Administrators (CSA)
  + **NI 51-102 – Continuous Disclosure Obligation**
    - Form 51-102F1 MD&A – a balance of forward looking information and past info
    - Form 51-102F2 AIF
    - Form 51-102F3 Material Change Report
    - Form 51-102F4 Business Acquisition Report
    - Form 51-102F5 Information Circular
      * Discloses compensation – philosophy, directors, governance related
  + **NI 52-110 – Audit Committees**
    - Form 52-110F2 Information Required in AIF
  + **NI 51-201 – Disclosure Standards**
    - Written in plain English, short, and gets to the materiality issues

**Continuous Disclosure**

Continuous Disclosure is comprised of two main categories

* Periodic 🡪 disclosure and filing of periodic financial and other information
* Timely 🡪 timely disclosure and filing of other corporate information (material changes)

The Principal instruments are **NI 51-102 Continuous Disclosure Obligations**, sand **NP 51-201 Disclosure Standards**.

The animating principle in continuous disclosure is equal access by all investors to accurate and timely information that may affect their investment decisions

### Periodic Disclosure

Financial Statements

* AIF
  + Contains income statements, statement of retained earnings
  + MUST BE AUDITED (quarterly) independently
    - Audited financials must then be approved by the board
  + Filing
    - Non-venture 🡪 90 days after the end of most recently completed financial year
    - Venture 🡪 120 days after end of most recent financial year
* Interim unaudited financial statements
  + Contains income statements, statement of retained earnings
  + Must be reviewd by the board, but can be delegated to the audit committee
  + Filing
    - Non-venture 🡪 45 days after the end of interim period
    - Venture 🡪 60 days after the end of interim period
* **NI 52-109 – Certificate after the end of interim period**
  + CEO and CFO must certify on a quarterly basis
    - Annual and interim financial statements
    - Fair rep of the financial condition of the reporting issuer for the relevant period
    - Enhanced written disclosure procedures
    - Due diligence defence – “reasonable investigation”
* **MI 52-110 – Audit Committee**
  + Committee
    - Must have charter
    - Oversee external auditor and resolve/monitor disputes between auditor and management
    - Ensure auditor independence
  + Members – must be 1) independent, and 2) financially literate (low bar)
* **51-102F1 – MD&A**
  + Discussion “through the eyes of management” of factors that have affected the reporting issuer’s results historically and prospective analysis of factors likely to impact future results
  + Focus is on material information
  + Filed with annual and interim financial statements
  + BOARD APPROVAL
    - Annual MD&A must be approved by board
    - Interim MD&A board approval may be delegated to audit committee

### Timely Disclosure

To be listed on the TSX, there is required timely disclosure of all material information (material change AND material fact). This information can get out to the public in a few different ways:

* Material Change Report
* Proxies
* Information Circulars
* Statement of Executive Compensation
* Compensation Disclosure and Analysis (CD&A)

**1. Material Change**: all material changes must be promptly disclosed by way of a material change report no later than 10 days after the change occurs in Form 51-102F3.

* **Material change**: a change in the business, operations or capital of the issuer that would reasonably be expected to have a significant effect on the market price or value of any of the securities of the issuer or a decision to implement such a change (**s.1(1) *Securities Act* (Ontario)**)
* What is material varies between companies according to their size, the nature of their operations and other factors
* **S. 4.3 of NP 51-201** discusses material changes in Financial Results as:
  + A significant increase or decrease in near-term earnings prospects
  + Unexpected changes in the financial results for any periods
  + Shifts in financial circumstances, such as cash flow reductions, major asset write-offs or write-downs
  + Changes in the value or composition of the company’s assets
  + Any material change in the company’s accounting policy

**2. Proxy Solicitation:** Proxy Solicitation is the sending of a notice of meeting and form of proxy to all securityholders for use at meeting. The reporting issuer must file this on SEDAR

**3. Information Circular:** includes key information to be voted on at a security holder meeting

* Directors
* Shareholders owning 10%
* Description of the types of securities
* Auditor appointment
* Management contracts if performed by others than D/Os
* Special matters

**4. Statement of Executive Compensation** – Compensation of the top 5 paid people in the company (CEO, CFO, and the next highest 3)

* The idea to keep executive compensation in check

**5. Compensation Disclosure and Analysis (CD&A)**

### Additional Filing Requirements

Any news releases, securityholder info, key material contracts

* These must be filed concurrently with the AIF or within 120 days of the financial year end of the reporting issuer

### Civil Liability – on the Secondary Market

If a company doesn’t properly disclosure, investors may not be properly apprised of all material facts of the company prior to investing and as a result may go to litigation.

Under **s.138.3 of** the **Securities Act (Ontario)** Investors can sue the reporting issuer, directors, senior officers, “influential persons” and experts if:

* Public disclosure contains a **misrepresentation** + the investor acquires or disposes of securities between the time when the document was released and when the misrepresentation was corrected
  + Misrepresentation is an un-true statement of material fact, or
  + An omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in the light of the circumstances in which it was made
  + Investors are deemed to have relied on this
* **Strict liability** for “core” documents (prospectuses, take-over bid circulars, issuer bid circulars, directors’ circulars, rights offering circulars, MD&A, AIFs, information circulars, annual financial statements and (for officers) material change reports)

Causes of action:

* **138.3(1):** documents
* **138.3(2):** public oral statements
* **138.3(3):** failure to make timely disclosure

#### Defenses to Civil Liability

* State of mind (for non-core documents and oral statements)
* Knowledge
* Due diligence – reasonable investigation
* Reliance on expert
* Republication
* Inadvertent release
* Whistleblowing

### Emerging Trends

**Corporate Governance Best Practices**

Each Company should have a formal Corporate Governance Best Practices that that is reviewed by corp gov disclosure committees

* Should include:
  + How to decide what info is material, policy on reviewing analyst reports, how to release earnings announcements and conduct related analyst calls and meetings
  + How to conduct meetings with investors and the media
  + What to say or not to say at industry conferences
  + How to use electronic media and the corporate web site
  + Policies on the use of forecasts and other forward-looking info
  + How to deal with unintentional selective disclosures
  + How to respond to market rumours
* Even news releases go through these corp gov disclosure committees

**NEW OBLIGATIONS – NI 58-101**

* Board diversity – comply or explain
  + Number/target of women on the board and in exec positions
  + Policies re rep of women on the board
  + Boards consideration of the rep of women in director ID and selection process
* Board Renewal Terms – comply or explain
  + D term limits or other mechanisms of board renewal
  + Succession planning

# Accounting Contracts and Financial Experts

The aim of financial professionals in court is to be a professional on finances in support of **one party calculating damages**. They have a variety of applications, from personal injury damage claims, matrimonial disputes, business losses etc.

Experts are either 1 of 2 roles:

* **Expert witness** 🡪 An independent economist/evaluator that can be questioned under oath
  + Must be independent from parties
  + Word product permitted into evidence
* **Consultant** 🡪 Dependent or independent economist/evaluator that CANNOT be questioned under oath
  + Word product NOT introduced into evidence

## Engagement Process

On engagement, an expert does the following:

* **ID any Conflict of interests** 🡪 must be independent
* **Qualifications/experience** 🡪 cannot properly advise without the requisite expertise
* **Merits of the case** 🡪 Is the damages claim going to be more than the cost of hiring an exper?
* **Deliverables** 🡪 What is the expert producing – Expert report? Graph?
* **Timelines and resources**
* **Discuss Fees**, and sign an **engagement letter**

Experts usually draft either a Chief (Expert) report or a Responsive (Limited Critique Report).

## Loss quantification

When calculating business losses, the preparer is only striving towards a reasonable basis for the compensation rather than absolute precision. Usually ranges are used, essentially a comparison of ‘but for’ (unaffected) results to actual (affected) results.

There are 3 common approaches to loss quantification:

1. **Before and After**
   * Use historical experience as the benchmark to predict the future loss suffered because the loss is avery unique experience
   * Must have a history of stable operations (to predict from)
   * Typically you look at 5 years before and 2-3 years after (business cycles are generally about 5 years)
2. **Comparable Yardstick**
   * Comparing event to similar loss events or comparable businesses
   * Ex. if you lose a commercial fishing license. Since salmon is a commodity, this is what it is used for, we would have been able to sell this many of lbs of salmon etc.
3. **Projection** (modelling) (Last resort if the above two aren’t appropriate)
   * Unreliable as use many assumptions

* A combination of approaches can be used
  + Both past and future losses can be quantified. More certainty with past loss as “actual” results are known.
  + Often, if you arrive at similar numbers using both approaches 🡪 number is more likely to be reliable
  + Future losses require projection of both “but for” and “actual” results

### Business Losses

To calculate business losses: **Loss = Lost revenue MINUS variable costs saved**

* This allows a business to claim the lost revenue, but they you also save the cost to generate that revenue (ie the Contribution Margin)
* **Variable cost**: costs that depend on other factors (ex. utility cost depends on how much you use per month)
  + This typically fluctuates with your output (revenue)
  + Complication as variable costs are often “step” variable as the size of the loss and/or the loss period increases.
    - Loss calculations are generally pre-tax (they are assumed taxed in the same manner as the foregone income).

### Personal Injury Losses

To calculate personal injury losses: **Loss = Without Accident income – With Accident income**

The expert is permitted to make some assumptions that are within the expert’s area of expertise, but the more factual they can be the stronger the expert’s report is. Moreover, the court is the ultimate trier of fact.

# Mergers and Acquisitions

## Introduction

|  |  |
| --- | --- |
| **Buyer Goals** | **Seller Goals** |
| 1. Investigate business  2. Minimize risk  3. Plan for integration   * How do you get yourself set up for integration?   4. Optimize consideration | 1. Certainty of closing  2. Maximize consideration (get the best price)  3. Preserve consideration   * Subjects/damages/conditions – keep the value or factor these into the purchase prices |

Sources of Law

* Corporate 🡪 BCBCA
* Securities 🡪 BC Securities Act, National Instruments
* Common Law
* Equity 🡪 equitable remedies (injunction), non-comp, non-solicitation, specific performance
* Other
  + Secured Transactions (e.g. Personal Property Security Act)
  + Real Estate (Land Title Act)
  + Tax Law (Income Tax Act)
  + Other (Environmental, Intellectual Property, Labour and Employment, Competition, Regulatory Matters, etc.)

|  |  |
| --- | --- |
| **Private M&A** | **Public M&A** |
| 1. Generally **share/asset purchase** **agreement** w/ parties signing | 1. Generally **arrangement**, **amalgamation** or support agreement   * Requires shareholder vote |
| 2. No hostile transactions | 2. Hostile transactions are possible |
| 3. Typically no fiduciary out | 3. Fiduciary out   * Even after you sign an agg, “if we get another offer and a better one, we can pursue another offer” |
| 4. Signing and closing can be simultaneous | 4. Staggered signing and closing due to req for SH approval |
| 5. More reps/warranties, more extensive diligence | 5. Fewer reps/warranties, less extensive diligence |
| 6. Indemnification by seller(s) | 6. No indemnification (premised on the disclosure regime) |
| 7. Subject to certain securities laws, but **mainly driven by corporate law** | 7. Subject to applicable securities law requirements on disclosure, etc. |
|  | Occurs when the public company is the target, whether the purchaser is a public or private |

|  |
| --- |
| **Process for M&A Transaction**   1. Sign Preliminary Agreements 2. Due Diligence 3. Negotiate and Sign Definitive Acquisition Agreement (and any Ancillary Agreements) 4. Satisfy Closing Conditions 5. Closing |

## Step 1: Preliminary Agreements

### Confidentiality Agreement

Parties will enter into a **confidentiality agreement** to protect sensitive information and transaction details from disclosure (ex. patents, finance, business trajectory etc.), and prevent improper use of information. They do this because certain terms can have unexpected consequences for a buyer. Certain things in the CA prevent these from happening (ex. standstills, non-solicitation prevent this.) For example, a standstill, if implemented, may be 12 months, may be 18 months – this is up to negotiation

With the CA comes an understanding of mutuality: if the Buyer discloses sensitive information to Seller, consider whether to make the agreement mutual versus one-way – if share for share 🡪 seller is interested in the buyer as well and should diligence the buyer.

### Term Sheets / Letters of Intent

**OPTIONAL STEP**

|  |  |
| --- | --- |
| **Advantages** | **Disadvantages** |
| * Clarification of business deal and helps to create a roadmap and expectations for signing and closing * Helps expose any “deal breakers” early in the discussions * May be helpful to Buyer when seeking financing * May help create a “moral obligation” to abide by its terms | * Almost always non-binding * If not drafted appropriately, risk of unintended consequences or being construed as creating an obligation to negotiate in good faith (consider recent *Bhasin* decision) * Can be an extensive and lengthy negotiation; takes time away from negotiating the definitive agreements, particularly when time is of the essence |

## Step 2: Due Diligence

**Due Diligence** is the step where a company engages professional advisors (legal, financial, tax, accounting, environmental, etc.) and receive access to an online data room prepared by Sellers to investigate the business

* **Purpose** 
  + Identifying key risks 🡪 Understanding assets and liabilities of the target and validating valuation
    - Ex. Is there material litigation against the Target? Is the Target subject to a large environmental contingency? Is a key distribution contract scheduled to expire in the near-term?
  + Identifying structuring and execution considerations
    - Ex. Are there third party consent requirements under key contracts?
* **Key Considerations** 
  + Due diligence pulls reps/warranties into the acquisition agreement, when reviewing disclosure schedules
    - Look to SEDAR – AIF, MD&A, financial statements
  + Due diligence is an ongoing fluid process
  + Public M&A due diligence is typically much less extensive than private M&A (can rely on public disclosure)

## Step 3: Negotiation of Agreement

Here, a back and forth of a share purchase agreement occurs, key issues are discusessed with the Buyer & their counsel and review a number of things in the Acquisition Agreement

* Definitions, Acquisition Structure / Mechanics (including assets vs. shares), Purchase Price and Adjustments, Closing Arrangements, Representations and Warranties
* Covenants, Closing Conditions, Indemnification (as applicable in private deals), Termination Rights, Miscellaneous

They also discuss the Acquisition Structure. There are 3 basic Structures:

* 1. Share purchase
* 2. Asset purchase
* 3. Business combination (amalgamation, arrangement, merger, etc.)
  + **Always used in public M&A**
  + **Rarely used in private M&A** but useful if there is a large number of shareholders and 100% control is sought

**Considerations that drive structure:**

* What is being bought/sold
* Ownership structure (public/private, number of shareholders etc.)
* Third party consents (anti-assignment clauses vs. change of control issues)
  + Share sales 🡪 consent with change of control/consent
  + Asset sale 🡪 consent with assignment of contracts
* Liability issues
* Tax considerations
* Combination of the three basic structures
* Disadvantage to the Asset Sale: you need to get the money out by way of dividends to shareholders. However, despite tax credits double taxation still occurs when you issue dividends
  + Could do share buyback or a shareholder loan, but there are issues there as well

|  |  |
| --- | --- |
| **Share Sale Advantages and Disadvantages** | |
| **Buyer** | **Seller** |
| **Advantages**  1. Simplicity  2. Certainty that it is acquiring the whole business  3. Fewer consent requirements 4. More focused diligence  **Disadvantages**  1. Buyer can’t pick and choose from the assets  2. Buyer will be bound by all company agreements  3. Buyer assumes all liabilities (even unknown) | **Advantages**  1. Simplicity  2. Generally provides a more tax advantageous result for the Seller  3. Clean exit; liabilities go with the company  **Disadvantages**  1. If only a portion of the business is being sold, can become more complex  2. Could result in lower valuations |

|  |  |
| --- | --- |
| **Asset Sale Advantages and Disadvantages** | |
| **Buyer** | **Seller** |
| **Advantages**  1. Get to choose assets  2. Avoids unknown liabilities and potentially known liabilities  3. May have tax benefits through step-up in asset tax basis  4. Avoids minority shareholder issues  **Disadvantages**  1. Complexity  2. May be difficult to get third party consents for assignments  3. May trigger transfer tax | **Advantages**  1. More specificity in what you purchase retain certain parts of the business  2. Could result in higher valuations if high-value assets are not combined with low-value assets  **Disadvantages**  1. Seller left with corporate shell and potentially “orphaned” assets  2. Diverse set of assets and jurisdictions makes asset transfer complex and may require more third party consents  3. Generally less tax advantageous 4. May trigger transfer tax |

### Purchase Price

* **Forms** 🡪 Cash, Shares, Debt, Earn-Out, Mixed
* **Other Adjustments** 🡪 escrows, holdbacks, deposits

#### Purchase Price Adjustments

Purchase Price Adjustments occur post-closing to adjust the purchase price to account for inventory. The purpose is to confirm that Target’s financial condition more or less meets Buyer’s expectations.

* Buyer is preparing valuation based on financial statements from the Seller
* Absent adjustments, profits/losses of Target between signing and closing are for the account and risk of Buyer
  + Buyer needs to ensure there are tight covenants that prevent value leakage
* Adjustment is based on changes in a specified metric (of a certain target amount, as of a specified date, etc.)
  + Common metrics include shareholders’ equity, working capital, net debt, other adjusted net worth figures

**Typical Process**

* Reference metric specified at/before signing
* One party prepares closing financials and prepares its calculation of reference metric
* Other party given access to any necessary information and may challenge the calculation (within a specified period)
* Dispute resolution by an independent accounting firm
* Incremental payment by Buyer or Seller to the other (plus interest in some cases) if above or below the target

There is sometimes a need for for a purchase price adjustment escrow with some counterparties where there are:

* Multiple Sellers
* Troubled Sellers
* Private Equity Sellers

#### Earn-Outs

An **Earn-Out** is a post-closing adjustment to purchase price based on performance of the target company. It is often used when the parties can’t agree on a purchase price. It may have to do with a short operating history, material contingencies, unusual or fluctuating performance, etc.

**Key Issues**

* Which metric to use? Revenue? Net income? EBITDA? Other?
* One-way or two-way? – typically an upward price increase only
* Timing
* Who has the right to calculate the metric after closing and how are disputes resolved?
  + Practice issues: access to information, availability of personnel and auditors
* How to prevent gamesmanship in the metric?

### Representations and Warranties

**Representations** and **warranties** are statements of facts, subject to exceptions, that create a picture of the relevant parties or subject matter

* Breach of rep 🡪 rescission, unless fraud
* Breach of warranty 🡪 repudiation and damages

Purpose of reps and warranties are generally 3-fold:

* Due diligence
* Conditions to closing
* Basis for indemnification or allocation of risk

**Exceptions to representations and warranties:**

* Disclosure schedules – usually contain exceptions to the representations and warranties
  + If contained in the schedules 🡪 at the Buyer’s risk unless Seller agrees to give a specific indemnity
  + Must be read in conjunction with diligence findings
* Data room – Very seller-friendly for data room to constitute an exception
* Public filings – Typical in public M&A deals; Buyer relies on securities laws related to disclosure

**Types of Reps/warranties:**

* Legal formalities
  + Corporate organization; authority and approvals; capitalization; enforceability; title to shares/assets
  + Often considered “fundamental” representations and warranties
* Business condition – Material contracts; customers; suppliers; intellectual property; real and tangible property; sufficiency of assets
* Financial condition *–* Accuracy of financial statements; tax matters; internal controls
* Liabilities and risks – No undisclosed liabilities, litigation; compliance with laws etc.
* Industry-specific – Oil and gas reserves, mining reserves, bank regulatory, insurance regulatory, etc.

#### Key Issues

* **Who will provide the representations and warranties?** 
  + Target? Seller? Both?
  + Joint and several? Several and not joint? Pro rata exposure?
  + Buyer representations and warranties if there is share consideration
* **Use of qualifiers: materiality, MAE, knowledge** 
  + May be appropriate in certain circumstances but not all – whose risk should they be?
* **Role of specialists** 
  + For highly specific reps, may need to consult with specialists in the subject matter
  + Tax, employment, pensions, environmental, intellectual property, regulatory, real estate, etc.

## Step 4: Closing Conditions

### Pre-Closing Covenants

Covenants are agreements to take or refrain from certain actions (affirmative/negative covenants) A few covenants include:

* Interim operations covenant – want to ensure people aren’t wasting away the money from the sale
  + Governs operation of the business between signing and closing and restricts certain actions:
    - Changes in capitalization
    - Dividends
    - Acquisitions and divestitures
    - Incurrence of debt
    - Amendment or termination of material contracts
    - Changes in employee arrangements
    - Commencement or settlement of legal proceedings
    - Other actions outside the ordinary course of business
* Regulatory Approvals Covenants – to make all filings and take appropriate actions to obtain approvals
  + “hell or high” water provision
* Best Efforts Covenant – covenant to take actions necessary to satisfy closing conditions and consummate the transaction
  + Best efforts? Reasonable efforts? Commercially reasonable efforts?
* Access and Inspection Covenant – helpful for purposes of integration planning

### Post-Closing Covenants

A few post-closing covenants include:

* Non-Compete – Prohibits Seller from engaging in a competing business post-closing
  + Scope and duration are heavily negotiated and must be “reasonable” to be enforceable
  + Duration is typically 2-5 years
    - \*\*Employment lawyers say don’t ask for more than 1 year
  + It’s so grey – you can’t be overly broad or else it is going to be unenforceable. Less is more!
* Employee Non-Solicitation – protects Buyer from Seller soliciting target employees post-closing
  + More frequently an issue when acquiring business from a strategic Seller versus a financial Seller
* Non-Disparagement
* Access to information
* Tax Cooperation in the future
* Employee matters

### Public M&A – Deal Protection Covenants

* **Covenants on Recommendation** 
  + Target agrees to recommend that its shareholders approve the deal  “Force the vote” provisions require a vote even in the face of a superior offer
* **No-Shop** 
  + Target agrees not to solicit competing offers or enter into an agreement with respect to a competing offer
  + Subject to a fiduciary out allowing the Target to change its recommendation (usually limited to circumstances in which it receives a superior offer)
  + Buyer has right to match the terms of the superior offer
* **Go-Shop**
  + In certain deals, the target is permitted to solicit competing offers during a go-shop period
  + You’d want a break fee if there is an interloper – payment could be reimbursement of lawyers fees hours etc, or something more significant such as 5-6B
* **Termination Fee** 
  + Termination fee often payable by target upon termination of deal based on change in recommendation

### Closing Conditions

* **Key Issues** 
  + Tension between closing certainty for Seller and protection for Buyer
    - Seller will insist on minimal conditions; Buyer will want to preserve flexibility
  + Consider the possibility of a simultaneous signing and closing
* **Typical Conditions**
  + Regulatory approvals
  + Competition Act Approval
  + In a regulated industry, there may be other approvals
* Third party/contractual approvals
* Corporate approvals (shareholder/board)

**Closing Conditions**

* Financing conditions
  + Becoming increasingly rare but still prevalent
  + Even if financing is required and is not a condition, consider financing cooperation covenants and reverse termination fees
* Absence of an MAE (Material Adverse Effects)
  + Very high legal standard; difficult to refuse to close on the basis of an MAE
* “Bring-down” of representations and warranties
  + Still need to be true as of closing date
* Compliance with covenants
* Other
  + Delivery of closing deliverables (e.g. ancillary agreements, certificates, etc.)
    - Sometimes a coupel, sometimes 100
    - Certs, resolutions, licenses, leases, assignment agreements
  + Legal opinions – becoming increasingly rare

### Indemnification

* Applicable only in private company deals; in public deals, representations and warranties typically don’t survive closing
* Indemnities provide Buyer with remedy for:
  + Breaches of representations and warranties and covenants
  + Specific known liabilities that the Seller has agreed to continue to bear (e.g. pending litigation)
* Survival of representations and warranties
  + Buyer may only make indemnification claims during the survival period
  + At least one full audit cycle is ideal – 12-18 months is fairly typical
  + Some fundamental (e.g., title, capitalization) and “long-tail” (e.g., environmental, tax) representations and warranties may survive longer
* Limitations
  + Deductible or threshold – often 1-2% of purchase price
  + De minimis exclusions
  + Caps (if seller) – heavily negotiated and are trending down; could be 10-50% of purchase price
* Read-out of materiality/MAE qualifiers
* Recourse for indemnity claims
  + Need for a parent guarantee or escrow?
* Anti-sandbagging provision
  + No rights for Buyer to seek indemnification for breaches known at closing
  + Forces a difficult choice on Buyer to walk away or accept the problem
  + Relationship to representation bring-down closing condition
* May be forced to close because disclosed breaches do not constitute an MAE, but no ability to seek post-closing indemnification
* Updates to disclosure schedules

### Termination Rights

* Termination Provisions
  + Mutual agreement
  + Drop-dead date
  + Closing prohibited by law or final injunction
  + Material breach of agreement
  + Other negotiated termination rights
* Other Termination Issues
  + Termination fee/reverse termination fee
  + Survival of certain provisions (particularly confidentiality)

### Miscellaneous

* Governing law
* Dispute resolution
  + Litigation versus arbitration
  + Jurisdiction
* Notices
* Amendments
* Assignments
* Expense reimbursement
* Specific performance

## Step 5: Closing

* Execution and delivery of closing deliverables
  + Officer certificates
  + Legal opinions
    - Becoming increasingly rare in M&A transactions but depends on facts and circumstances
  + Ancillary agreements
    - Shareholders’ agreement
    - Employment agreements
    - Management equity agreements
    - Transition services agreements
    - License agreements
    - Financing documents
* Payment of purchase price
* Transfer of shares/assets
* Typically, all deemed to happen “simultaneously