

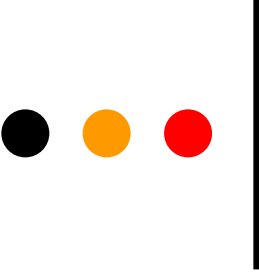


Mergers, Acquisitions and Other Contracts in the United States

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Workshop Study Outline

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Mergers, Acquisitions and Other Contracts in the United States

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- Business, tax, commercial and insurance law firm
- Located in New York City
- Clients are large and small domestic and international corporations and businesses
- “Big firm” standards, small firm costs



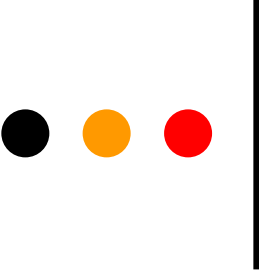
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- Corporate and Tax Matters:
 - Acquisitions, divestitures and reorganizations
 - Securities transactions – raising capital
 - Intellectual property development, protection and licensing
 - Joint ventures – production and distribution arrangements
 - Commercial real estate transactions
 - Asset-based lending
 - Domestic and international tax
 - International trade issues and problems



Lazare Potter Giacobas & Kranjac LLP

- Commercial arbitrations and litigations
 - Federal and State trial and appellate courts
 - Domestic and international arbitration forums, including ICC
- Insurance Law
 - Represent insurance companies



Workshop Objectives

- Understanding United States Contracts Generally
- Understanding United States Merger and Acquisition Contracts



Contracts Generally

- Contracts made in the U.S. have a characteristic structure
- The business deal is only a part of the contract
- Today, we will help you understand that structure



Parts of a Typical Contract

- Preamble, Recitals and Transition Provisions
- Definitions
- Business Terms
- Representations and Warranties
- Covenants
- Conditions to Closing
- Remedies
- Miscellaneous Provisions
- Signature Page
- Exhibits and Schedules



Preamble, Recitals & Transition

- Preamble:
 - Caption
 - Parties
 - Date
- Recitals explain background
- Transition: “The parties agree as follows:”



Definitions

- Isolate a term or concept so it is given the same meaning each time it is used
- Remove ambiguity
- Contain or clarify scope
- Important from an enforcement perspective



Business Terms

- o Business terms include:

- Performance:

- Subject matter
 - Mutual promises and obligations
 - Time and place of performance
 - Standard
 - Acceptance and rejection

- Payment



Representations and Warranties

- A representation is a statement of fact made at a particular point in time upon which the other party is expected to rely
- A warranty is a statement that a represented fact is true. It creates an indemnification obligation if that fact is false



Covenants

- On-going promises by a party to take or not to take certain actions
- Could be:
 - pre-closing
 - post-closing
- Affirmative
- Negative
- Events of Default



Conditions to Closing

- “I promise to pay you \$1m”
- “I promise to pay you \$1m *if* the cargo reaches New York”
- A condition is an event which must occur before performance becomes due



Remedial Provisions

- Remedies are often expressly provided
- Remedial provisions have 3 elements:
 - Triggering events that give rise to a remedy
 - Catalog of available remedies
 - Costs



Typical Remedies

- Termination:
 - More useful if exercised before performance is due.
- Acceleration:
 - Making debt due and payable immediately rather than at stated maturity. Example: loan contracts
- Indemnification:
 - Frequently used in M&A contracts, discussed below
- Liquidated damages
- Equitable remedies
- Coercive remedies



Miscellaneous Provisions

- Interpretation
 - Importance of Preamble and Recitals
 - Third-party rights
 - Entire agreement
 - Severability
 - Notices
 - Waivers
 - Amendments
 - Counterparts



Miscellaneous Provisions

CONTINUED

- Last minute and miscellaneous bargains
 - Indemnification (if not already included)
 - Assignment and delegation
 - Further assurances
- Enforcement
 - Choice of law
 - Dispute resolution forum
 - Jury trial



Signature Page, Exhibits and Schedules

- Signatures are often affixed on a separate page
- The contract is intended to be a complete document
- Miscellaneous section often provides that Exhibits and Schedules are part of the agreement



Merger and Acquisition Contracts

- Private merger and acquisition (“M&A”) transactions are a good example of the contract structure we discussed
- We will now discuss certain pertinent parts of an M&A contract



M&A Methods

- 3 basic ways to sell or buy a business:
 - A. By merger
 - B. By selling or buying voting stock
 - C. By selling or buying assets



Merger - Many Variations

- For Example:

- Target (“T”) into Acquiror (“A”)
- T into Subsidiary (“S”), for stock of Parent (“P”) (triangular merger)
- S into T, for stock of P (reverse triangular)
- For cash, stock, property, third party securities
- Structuring is heavily driven by tax law



Merger – When Used

- Acquisition of public companies – the target has too many shareholders for stock purchase to be practical, or there is a dissenting minority
- Parent-sub subsidiary
- Sometimes preceded by a stock purchase



Stock Purchase

- Often used by small businesses when there are no pressing reasons to choose another form
- The risk of assuming unintended liabilities
- Often more tax advantageous to seller rather than buyer



Asset Purchase

- Frequently used when:
 - Business is not separately incorporated
 - Buyer wants to avoid certain assets or contracts
 - Undesired or unknown liabilities
 - Book value of assets is much lower than fair market value – opportunity for buyer to step-up tax basis



Representations & Warranties

- Buyers want them because:
 - Disclosure
 - Set stage to walk out
 - Groundwork for indemnification
- Sellers try to limit content and scope



Seller's Tool-Kit

- Sellers try to limit scope by adding knowledge and materiality exceptions
- An example of knowledge exception:
 - Buyer's draft: “Seller represents that it is not in default under any of the assigned contracts.”
 - Seller's change: “Seller represents that **to its knowledge, no party has asserted that Seller** is in default under any of the assigned contracts.”



Knowledge – more examples

- Buyer's draft: “Seller represents that there exists no default under the lease.”
- Seller's change: “Seller represents that **to the best of its knowledge**, there exists no default under the lease.”
- Buyer's change: “Seller represents that it **is not in default under the lease, and to the best of Seller's knowledge, the lessor is not in default under the lease.**”



Materiality

- Addition of materiality criteria is another example of how Sellers typically limit scope.
- Example:
 - Buyer's draft: “Target has good and marketable title to, or valid leasehold interest in, all of the Acquired Assets, free and clear of any Liens or restrictions on transfer.”
 - Seller's change: “Target has good and marketable title to, or a valid leasehold interest in, all **material assets it uses regularly in the conduct of its business.**”



Covenants

- Pre-closing:
 - Preserving the value of business
 - Confidentiality and “no shop”
 - Steps to obtain pre-closing approvals
- Post-closing:
 - Non-competition
 - Use of intellectual property
 - Seller’s access to business for certain purposes
 - Further assurances



Covenants

CONTINUED

- If third parties are involved, then often qualified by a “best efforts” promise

- Example:

Covenant:

“Seller shall apply promptly for a tax ruling || and will use Seller’s best efforts || to obtain it as soon as possible.”

Comment:

Absolute, no qualification as it is within Seller’s control || or “reasonable best efforts,” since this is not in Seller’s control || Buyer may add that Seller shall diligently prosecute any application filed



Interplay

Example for covenant and condition:

- Buyer in an asset deal has 2 principal worries:
 - Seller might take cash out before closing, and
 - Results of operations for most recent quarter may be below projections.
- Regarding cash: Buyer may want a covenant, the compliance with which is also a condition
- Regarding results: Buyer will create a condition



Indemnification

- Important in private M&A agreements
- Covers breaches of warranties and covenants
- Usually only for the benefit of buyer
- But Seller may be indemnified against post-closing operating liabilities
- Basic purpose is to make Buyer whole
- Buyer's basic fear:
 - Merger or share purchase: undisclosed or understated liabilities
 - Asset deals: the existence and quality of assets



Indemnification Issues

- Survival period – “*cut-off*”
- Damages + legal and other expenses
- Seller will request “*basket*” or a *threshold*
 - Buyer may argue that materiality qualifications should be ignored
- Seller will request a maximum amount (“*cap*”), for example, the purchase price
 - Buyer may insist on escrow of part of the purchase price or a “*hold-back*”
- Whether exclusive remedy – often, yes; but not in case of fraud, misrepresentation, violation of law
- Joint and several liability



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