A GPS for Business Deals: Planning a Route Through Complex Business Transactions

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Over the past several years, mergers and acquisitions and financing activity decreased sharply as a result of the economic recession and the tightening of credit markets. However, as 2010 progressed, we saw a substantial increase in deal activity, and it now appears that we are on our way to returning to pre-recession levels. Indeed, in the fourth quarter of 2010, mergers and acquisitions and financing activity was downright robust, with companies and their advisors rushing to get year-end deals done.

As business transaction activity levels continue to increase, more investors are funding new investments and companies are again exploring strategic transactions. Capital is becoming more accessible and companies are able to undertake significant business initiatives that were previously unavailable to them. In reflecting on the year-end rush that closed out 2010, it seems clear that, regardless of the type of transaction, our clients were as focused as ever on accomplishing two principal (and ever-present) objectives: (1) getting the deal they wanted, and (2) managing the costs associated with the transaction.

These two objectives seem extremely straightforward and sensible. Wouldn't all parties to a deal want these things? Nonetheless, achieving these goals in spite of the many the twists and turns of a transaction is not as easy as it might seem. The question, then, is: What practical steps can you take during the transaction process to help accomplish these goals?

To get the "right" deal (the deal you want), and do so in as cost-effective a manner as possible, it's helpful to keep a couple of key points in mind throughout the transaction.

1. Know what you want to achieve.

As negotiations with counterparties get underway, be sure that you've taken the time to think about what the transaction means for your business. The implications of the transaction will depend on the deal itself and what you're trying to accomplish with it.

For example, if you're a business owner raising capital, you'll need to consider what you're willing to give up in exchange for the money you're new investors will put in. How much of a stake in the company are you willing to part with? Do you want to maintain control, or are you alright answering to a board of directors appointed by others? What type of dividends will be paid to new investors before you get your share of profits?

Similarly, if you're making an acquisition, beyond negotiating the price, you'll need to think about how the addition of the new division or assets will be accomplished. What are the important assets that make you want to do the deal? Are there key employees that need to come along too? What level of liability are you willing to assume in connection with taking on the new business your company is acquiring?

Understanding these and other important considerations at the outset will allow you to structure the transaction in the way that makes the most sense and avoid having to change your position later, both of which will help save time, money and energy as the transaction progresses. Additionally, understanding the "big picture" pieces of the transaction will allow you to get the most out of your advisors, which brings us to the second key point:

2. Make sure your advisors know what you want.

In order for your financial advisors, attorneys, accountants, consultants and others to help you get you the deal that you want for your company, they have to know what's important to you. Once you've thought through the big picture issues, it's very important that you establish a healthy dialogue with your advisors about what your expectations are for the transaction and what you want to get out of it. As you discuss your objectives with your advisors, they may be able to spot issues that you might have otherwise missed. Your advisors can also help you to come up with the best framework for negotiating and achieving the objectives that you identify.

Involving your financial, legal and operational advisors in the process early and keeping the lines of communication open will create the best working relationship for achieving your goals. It will also allow you and your advisors to avoid working on unimportant tasks and alleviate redundancies in the business transaction process. The resulting efficiency will save you time and money.

After you've established the foundational goals and have made sure that the deal team has a thorough understanding of these goals, you can move on to the business of negotiating and structuring the deal.

3. Set deal-breakers and tackle the tough issues with other parties early.

As you and your advisors formulate negotiation strategy based on the goals that you have set, it's important that the deal team identifies its "must have" list. This list of things that you must have when all is said and done should reflect the goals you have set out to accomplish through the transaction.

Once you've determined what your deal breakers are, you should work to reach agreement with the other side on these critical points as early as possible in the negotiation process. As with the other phases of the transaction, your advisors should play an important role. If at all possible, try to ensure that your must-have points are incorporated into the Letter of Intent or Term Sheet that sets out the basic terms of the deal.

Establishing deal breakers and reaching agreement with the other side early in the process has many benefits. Most importantly, this approach will allow you and your advisors to flesh-out any difficult negotiation points and issues that might scuttle the deal <u>before</u> you have too much invested to walk away. Parties that don't identify deal breakers until everyone is well underway in the transaction process often need to make concessions on those points because they have invested too much or have lost leverage as the negotiations have progressed. Put another way, it's easier to walk away from a deal earlier in the process if the opposing party won't meet your demands. The ability to walk away gives you leverage to get exactly what you want. That leverage diminishes as the deal progresses.

Additionally, working out the tough issues early makes structuring the transaction and drafting the transaction documents much easier and more efficient. If these issues aren't addressed early in the process, the resolution of unresolved points and the negotiation and drafting efforts related to that resolution tend to be complex and costly for the interested parties. Incorporating your deal-breaker points into the LOI or Term Sheet will give all parties a road map that will serve as a basis for the more complex transaction documents. This helps to minimize cycles of re-negotiation and re-drafting on issues that have already been resolved and, in so doing, can lead to significant cost savings.

4. Maintain focus, stay organized and understand and manage critical projects.

If you've been able to successfully identify your goals, communicate them to your advisors and establish and negotiate the deal-breaker points with the other side, then you're well on your way to getting what you want out of the transaction. Getting there in a cost-effective manner, though, has only just begun.

As the transaction progresses, it's important for you and your team to keep the goals that you have established in mind. Don't lose sight of what you initially set out to accomplish. Keeping everyone focused on the essentials of the transaction is the best way to keep costs down.

By this phase of the transaction, the attorneys on both sides will be underway with drafting the transaction documents. The documents will be based on the LOI or Term Sheet that includes your must-have deal points. Make sure that all members of your deal team – both your advisors and your employees – know their role. Even more importantly, make sure that they know what their role means to achieving the overall objectives for the transaction. Keeping these parties from going "off the reservation" will reduce inefficiencies and eliminate efforts that aren't worthwhile, thereby reducing the cost of the transaction.

Another thing that can help to reduce costs is organization. As the documents come together, it's important to stay organized. Be sure you understand what remains to be accomplished and who has responsibility for each task. Even more importantly, understand the substance of the task and how it relates to the rest of the transaction.

For example, it's very important for all parties to understand how the due diligence process relates to the representations and warranties in the purchase agreement and, ultimately, the disclosure schedules to that agreement. These three areas are among the most time consuming for both the business principals and their advisors, and working efficiently through them can result in substantial cost savings. Making sure that everyone knows how risk is being addressed and allocated through these three mechanisms will allow all parties to be more proficient and effective in their approach to each task associated with them. It will also make it easier for you to coordinate each of these multifaceted projects amongst your advisors and other deal team members.

A corollary to keeping the team focused is managing information flow. Be sure that everyone on the team knows who should communicate with whom and what information should be conveyed. Generally speaking, your team members should deal with their counterparts on the other side of the transaction (lawyers talk to lawyers, CFO's talk to CFO's, etc.) but important decisions should be made only by you and your core team after you receive guidance from your advisors. If possible, avoid making on-the-spot decisions without input from your team. Often, you may not see the whole picture. By soliciting advice before committing to a position, you can avoid having to go back to the other side hat-in-hand to renegotiate because you inadvertently ok'd something that doesn't work. This is particularly true as the parties work through to finalize the transaction documents, which are often complex.

5. Don't lose sight of the importance of getting the details right.

As parties to a transaction push to get to closing, if you're not careful, critical pieces can get lost in the shuffle. Bringing all of the documentation together, making sure the representations, warranties and disclosure schedules are right, and getting all of the parties to agree upon and sign the final documents can be an arduous and time consuming task. Often, by the time the parties are nearing closing, some deal fatigue has set in. In these cases, the parties may be tempted to just take whatever terms they've settled on so far and "cave-in" on the rest just to get the transaction completed. While in some cases, time constraints and other business considerations may require some adjustment of terms, you should avoid making concessions at this stage unless you fully understand the ramifications for your overall goals.

The role of your advisors in this part of the process cannot be overstated. Typically, business and legal advisors have more experience with the transaction process and are less likely to be fatigued. Additionally, your advisors will have worked through all of the details with you throughout the course of the transaction and by doing so will have a thorough understanding of the ramifications of changing the details. As you near the finish line, consult with them regularly and rely on them to help you get the deal done while still achieving your goals.

If you need assistance with a business transaction or other legal matters, please contact one of our business transactions attorneys at (410) 727-6600 or by e-mail at:

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