TEXAS LAWYER
May 13, 2013
An ALM Publication

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A Checklist for the Early Stages of an M&A Transaction

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When a merger-and-acquisition deal commences, in-house counsel of private and public companies face daunting tasks. They often have to coordinate work streams involving outside counsel and company personnel, in addition to juggling responsibility for spotting legal issues and managing communications. Here are some significant steps in-house counsel should take as they become initially engaged in an M&A transaction.

• *Execute a nondisclosure agreement.* When parties first engage in merger talks, they should execute a confidentiality or nondisclosure agreement.

Public companies' in-house counsel should pay special attention to whether it is appropriate to include a standstill provision in the agreement. These provisions prevent the would-be acquirer from taking enumerated unsolicited actions with respect to the would-be target, such as buying the target's securities or engaging in a proxy contest.

One form of standstill provision is called a "don't ask, don't waive." Under this formulation, not only does the would-be acquirer agree not to take the listed actions, but it also agrees not to ask the would-be target to waive the protections.

However, counsel for the target should approach such provisions with care. Based on recent Delaware court pronouncements, the target should consider whether a "don't ask, don't waive" standstill provision may present fiduciary complications after signing a definitive agreement by suppressing competing bids during the no-shop period. The target's board should weigh in on whether to include such a provision.

In addition, if a buyer is successful in avoiding the inclusion of an explicit standstill provision, the buyer also should resist inclusion of the word "negotiated" or "between" in the definition of the possible transaction in the confidentiality agreement. The Delaware Chancery Court recently indicated that judges could interpret such words in that context as limiting use of information exchanged pursuant to the agreement to evaluation of a consensual deal. Such a limit on use of information can create a backdoor standstill restriction, by effectively foreclosing any unsolicited action by the buyer.

• *Gauge initial interest of the board of directors and provide regular updates.* Generally, management should consult with the board to gauge the directors' initial reaction to the proposed transaction. If the transaction appears to be viable, executives should schedule a special board meeting to discuss whether

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to proceed. Once the board decides to pursue the transaction, management regularly should inform the board of material developments throughout the negotiation process.

• *Engage financial advisers.* After the potential target's board has decided to pursue a possible transaction, it should consider whether to engage a financial adviser or investment banker to assist with the process. A financial adviser can serve as a liaison for negotiating purposes and can assist the board in evaluating the economic terms of the transaction.

However, recent Delaware cases have highlighted the problems associated with financial advisers' conflicts of interest. The company should solicit information from financial-adviser candidates regarding conflicts, such as any relationship with potential transaction counterparties, so that the board can assess the financial adviser's independence.

Once the board selects a financial adviser, it will require the company to enter into an engagement letter. Target companies should pay special attention to the nature and timing of the success fee payable to the financial adviser and the length of the tail period (during which the financial advisor may be entitled to a fee if the target completes a transaction after the financial adviser's engagement concludes).

• *Evaluate potential conflicts.* The board should evaluate whether the transaction poses any potential conflicts involving members of the board or management. Potential conflicts can arise in a variety of situations during the course of the transaction; for example, members of the target's management team may accept positions with the acquiring company during negotiations.

If potential conflicts arise with respect to board members, in-house counsel should encourage the board to consider whether it's appropriate to form a special board committee of disinterested directors to negotiate the transaction and whether that committee should engage separate financial and legal advisers to assist in the process.

Given the increase in the frequency of litigation challenging M&A transactions, particularly involving public companies, it is particularly important to make a proper evaluation of potential conflicts early in, and repeatedly during, the negotiation process.

• *Maintain confidentiality within the company.* To avoid premature disclosure of the potential transaction, companies should form an internal working group or restrict the number of individuals within and outside the company who know about transaction.

Premature disclosure of a potential transaction could have adverse consequences with third-party vendors, destabilize the transaction, affect the trading price of the parties' stock if it is publicly traded and potentially lead to employee-retention issues.

• *Organize and obtain due-diligence information.* One of the initial steps in a transaction is distribution of a lengthy due-diligence request list that will likely cover accounting, financial, tax and legal due-diligence items. In-house counsel will be responsible for collecting and organizing information and documents from various company departments without alerting individuals of the possibility of a transaction.

It has become increasingly common to respond to due-diligence requests by placing documents into virtual data rooms. This approach lets the company restrict access to certain groups and monitor who reviews particular pieces of information.

• *Evaluate potential antitrust issues.* Depending on the size of the transaction, the buyer and seller may need to make filings pursuant to the Hart-Scott-Rodino regulations. If a filing is required, in-house counsel needs to assess whether regulators are likely to scrutinize the transaction. If a transaction will involve a heightened level of review, companies should consider engaging antitrust counsel early in the process.

• *Special concerns for public companies.* Public companies may consider imposing a blackout on insiders' transactions while executives negotiate the deal. In-house counsel will need to consider the impact of closing the trading window for all employees or just for the internal working group that has knowledge of the transaction.

After the company publicly announces a transaction, a number of entities will scrutinize trading in the company's securities. Stock exchanges, the Financial Industry Regulatory Authority, and the Securities and Exchange Commission all may take a close look. Although federal securities laws generally do not require disclosure of preliminary M&A negotiations, a company should be prepared to respond to rumors that could have an impact on the company's stock price.

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