

Board Business: *M&A transaction issues*

COVID-19 has led to a period of volatility and uncertainty in global and domestic markets. Achieving deal certainty in M&A transactions is now more challenging. The impact of this uncertainty will likely be felt in relation to both existing and future M&A transactions.

In this edition of our series “**Responding to COVID-19 – Board Business**” and to assist Boards in navigating the M&A process in this unprecedented environment, we look at some immediate challenges for Boards and deal makers as the disruptive effects continue to intensify across all sectors of the economy.

We focus on the following 3 key areas for Boards who are in the midst of:

- Contemplating a transaction
- Mid-negotiations
- Post-signing with a completion date in the future

We also identify a number of lessons we can learn from the **global financial crisis in 2008** in terms of transaction planning and risk mitigation.

Before we examine these areas, we have also addressed some **practical questions** relating to transactions. These are issues which now arise due to the new requirements around physical distancing and remote working. While generally the remit of the advisors, they are points which remain of interest to the Board as they will ultimately ensure a smooth completion if addressed as early as possible.



You will find a full range of timely materials for businesses in our dedicated **COVID-19 HUB** on our website.

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Practical / administrative

There are a number of practical processes which are followed at various stages of a transaction which we have never had to question or test before.

Coronavirus has impacted the basic logistics of doing a deal as countries close borders and the majority of deal teams will now be working remotely. These deal processes, while administrative in nature, are critical in ensuring that completion occurs validly and in a timely manner. We have addressed some of the most common queries we are receiving from Boards below.

Q1: How do we execute transaction documents remotely?

Simple contracts and agreements which don't need the formal company seal may be executed using e-signature. For documents requiring the company seal, the Board can approve the granting of a power of attorney to an individual to execute documents on its behalf, which removes the requirement for the affixing of a company seal. The power of attorney itself does not need to be executed under seal by the company but the relevant deed will need to be witnessed.

Q2: Is it possible for the chairman of our completion Board meeting to sign the relevant minutes electronically?

Yes, there is no legal requirement that this signature be in wet ink.

Q3: Can we still carry out completion searches on a target if, for example, the Judgments Office has closed?

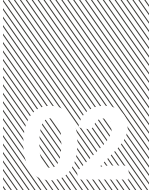
At the time of writing, the Central Office is open for judgment, petition and proceedings searches. The Companies Registration Office is available online also.

Q4: How do we arrange payment of stamp duty if the Revenue Commissioner's offices close?

The Revenue Commissioners have confirmed that their online services remain available. The filing of stamp duty returns online will therefore remain available.

Q5: Will there be any disruption in funds/ wire transmissions on the day of closing?

No. As long as the banks continue to function, the movement of funds for transactions will continue as normal.



Corporate transactions

Depending on the stage of a transaction, there will now be different challenges and considerations for the Boards of purchasing entities to discuss. These range from a refreshed approach to due diligence to a potential re-opening of discussions around the purchase price.

Where a transaction is reliant on third party debt for financing, the Board will need to ensure at the outset that this remains available and consider the inclusion of a financing condition in the transaction documentation. Although the inclusion of such a condition is typically successfully resisted by sellers, we may see a change to this approach as certainty of and access to debt funding will come into sharper focus.

We have approached these questions from the perspective of a buyer Board, but have highlighted certain instances where a seller should take particular care also.

Contemplating a transaction:

How should we approach the due diligence exercise?

Alongside your usual due diligence exercise, key contracts should be reviewed to ensure that the obligations under those contracts are still capable of being met in the current circumstances. Termination rights along with force majeure provisions should also be reviewed in case the current crisis triggers any right of the counterparty to exit a valuable contract prematurely. The ability to suspend material contracts without penalty will also be a key area of focus on the supply side.

Buyers will be in a much better position to look for indemnities or particular warranty coverage if they are able to identify and articulate specific potential costs that a target may face based on thorough diligence that is properly focused on COVID-19 impacts.

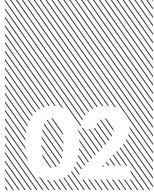
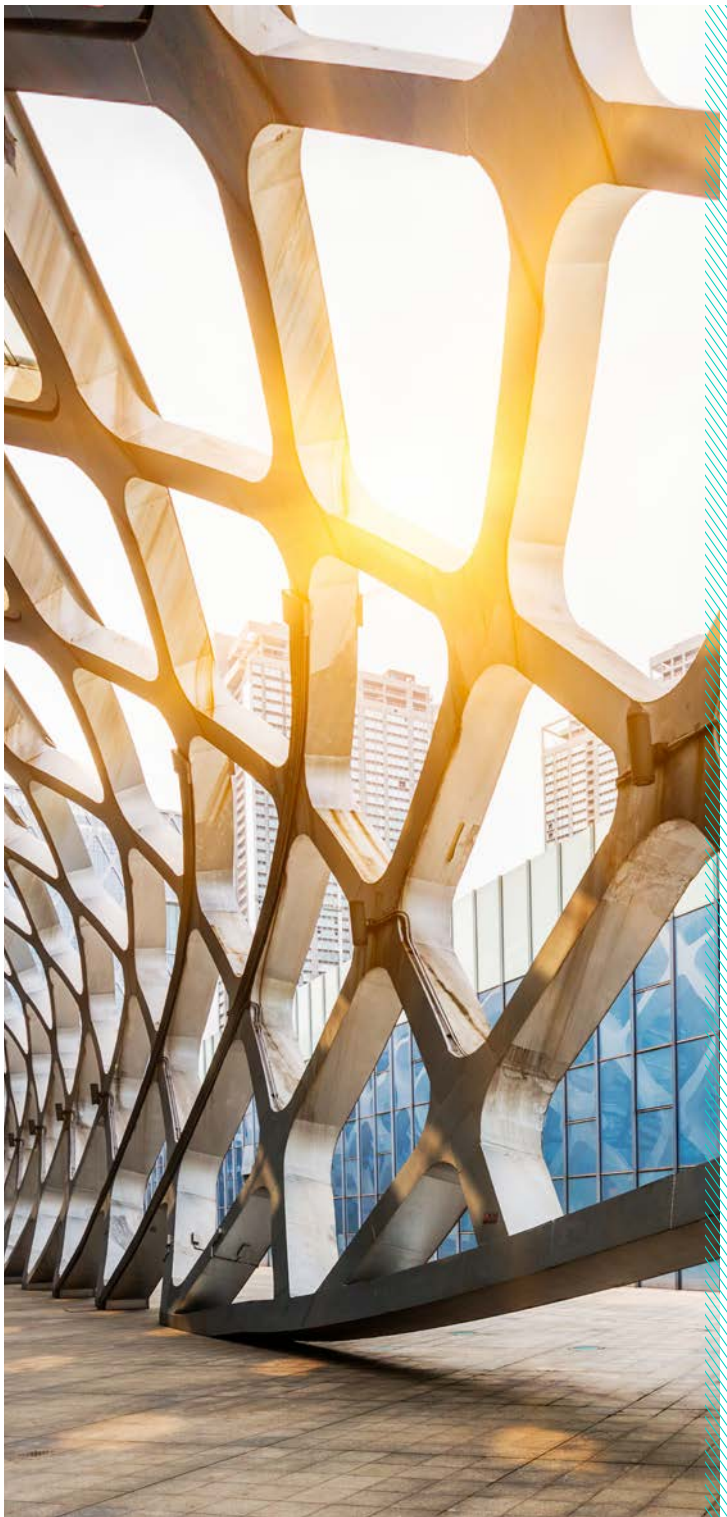
How has the target dealt with its employees during the COVID-19 crisis?

In the case of employees and GDPR, the activity of the target should be examined to ensure that any short term layoffs have been carried out legally. Where sensitive employee information has been handled, enquiries should be made to confirm that it has been done in a way that is GDPR compliant.

If the relevant business is high risk in the context of COVID-19 (for example, a large factory where the risk of cross infection would be higher), consider whether additional specialists (public health professionals, for example) should be asked to carry out their own specific checks or risk assessments so as to ensure that the buyers are fully informed of any potential issues.

Are there additional agreements which are now particularly material?

Where the target is a party to facility agreements containing covenants and/or a requirement to repeat warranties on a regular basis, confirmation should be sought by a buyer to ensure that these have not already been breached. This is obviously of particular importance where it is intended to maintain such facilities post transaction. If not it is likely to be relevant in the context of any new debt financing which is to be put in place to replace existing facilities. Boards should also consider "stress testing" the target in the context of any applicable covenants and examining the implications of a breach.



Corporate transactions

What type of COVID-19 specific issues should we be looking for?

Boards and their advisors should ascertain whether the target has complied with all applicable regulatory requirements relevant to COVID-19 so far. Many companies are implementing a business continuity plan, and if it exists for the target, this should be reviewed. Details should be sought of any statutory emergency funds, such as the SBCI COVID-19 Working Capital Scheme, which have been availed of. It may also be advisable to explore any further assistance put in place by the government which could be availed of post-completion.

Insurance position of the target – what should we focus on?

All insurance policies of the target should be reviewed in the context of the current crisis – does any business interruption provision cover losses due to mandatory closures or as a result of an inability to honour contractual obligations for example? Policies should also be reviewed for any provisions which require the policyholder to mitigate loss. If such provisions are present, enquiries should be made as to whether this has yet occurred.

Mid Negotiation:

Can I now insist on a Material Adverse Change (MAC) clause and will it be enforceable?

The ability of a buyer to use a MAC clause will depend on the wording of the clause and the specific facts (as it is ultimately a question of fact as to whether it has occurred). Historically

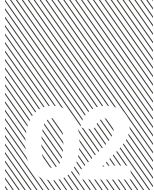
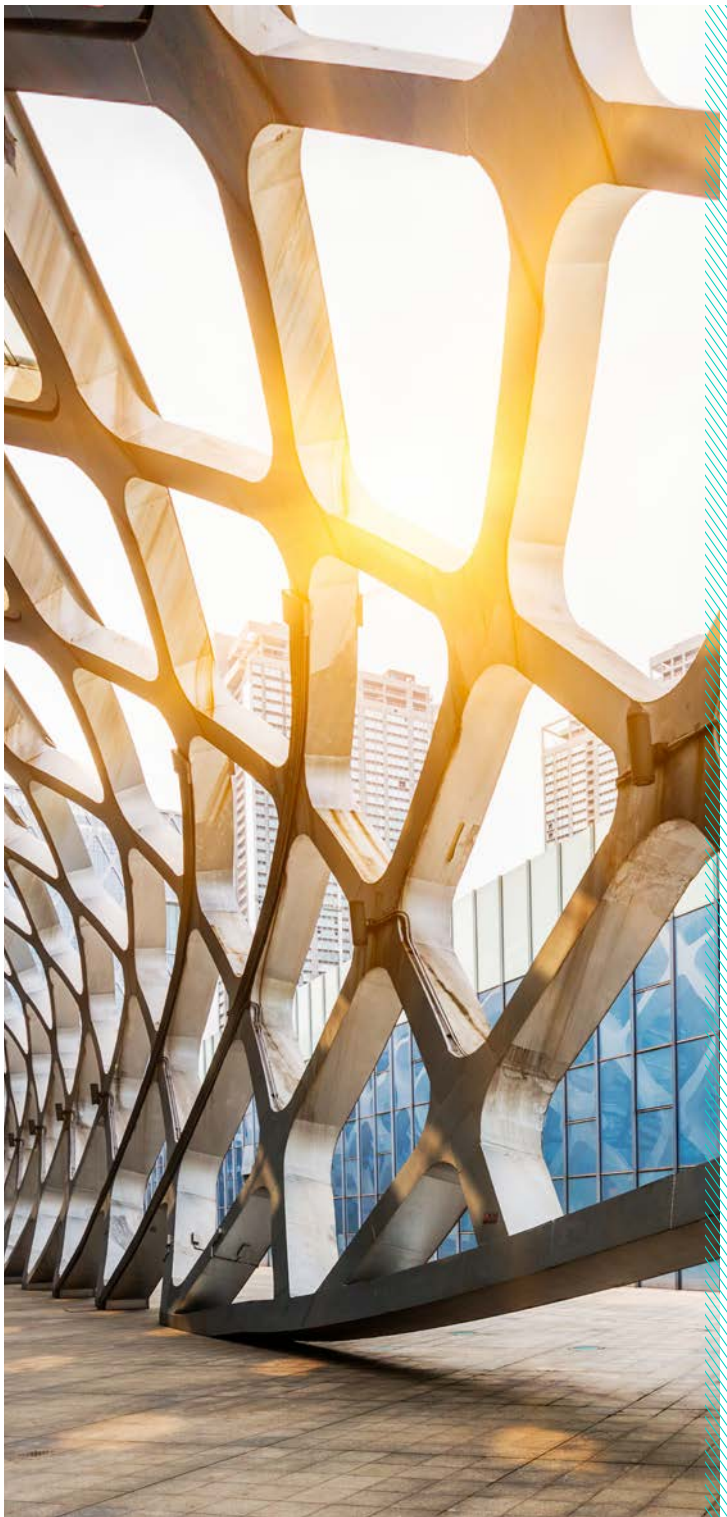
MAC clauses have proved difficult to both negotiate and to rely on in practice. Reliance on a pre-crisis MAC that makes no reference to pandemics or epidemics may be challenging. In respect of transactions not yet signed, we would advise both buyers and sellers to negotiate explicit language to address COVID-19 risk-allocation in the context of any MAC provision and this is something we have seen in practice in response to past crises.

Actions between signing and completion – what should the seller do?

Where negotiations are ongoing in relation to interim operating covenants, Boards of selling entities in particular should revisit these to ensure that they will be in a position to carry out all specified actions during the relevant period. For example lending covenants may well be breached during this period. Sellers should also bear in mind that this interim period may now be considerably longer than initially projected. This is particularly the case where regulatory consents are required in order to complete, given the likely delay in obtaining such consents as covered below.

Warranties and Indemnities – how should we review these in light of COVID-19?

Any relevant COVID-19 specific warranties should be sought by the buyer. Particular care should be taken in relation to financial warranties and any financial projections which have been warranted by the seller. To ensure that any additional areas of risk are identified and appropriately dealt with by way of warranties or specific indemnities, a focussed due diligence is particularly critical at this time.



Corporate transactions

Where either the buyer or the seller is arranging to obtain warranty and indemnity insurance, consideration should be given to whether losses arising from a known risk, such as COVID-19, would be covered by this insurance. As COVID-19 is now a known risk, we expect that insurers will likely specifically exclude any virus related losses from policies in respect of transactions which have not yet signed.

In the context of warranty and indemnity insurance we can also expect to see underwriters looking more closely at the following as part of the due diligence:

- Current business continuity plans
- Insurance policies and ability of the target to recover for COVID-19 business losses
- Ability to terminate or suspend material contracts without penalty
- Supply chain disruption and alternative sources of supply
- Key counterparties and their jurisdictions of operation
- Regulatory or HR compliance implications as a result of remote working

Should we, as buyer, revisit our pricing mechanism in the circumstances?

Obviously from a sellers' perspective the aim will be to maintain the agreed pricing mechanism. From a buyer's perspective, where commercially possible, pricing mechanisms would ideally be reviewed in light of the current crisis. Where a locked box or fixed pricing mechanism was previously agreed, for example, it may be necessary to re-open this and look at alternative methods, such as incorporating an earn out

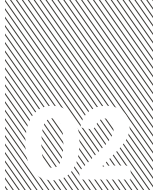
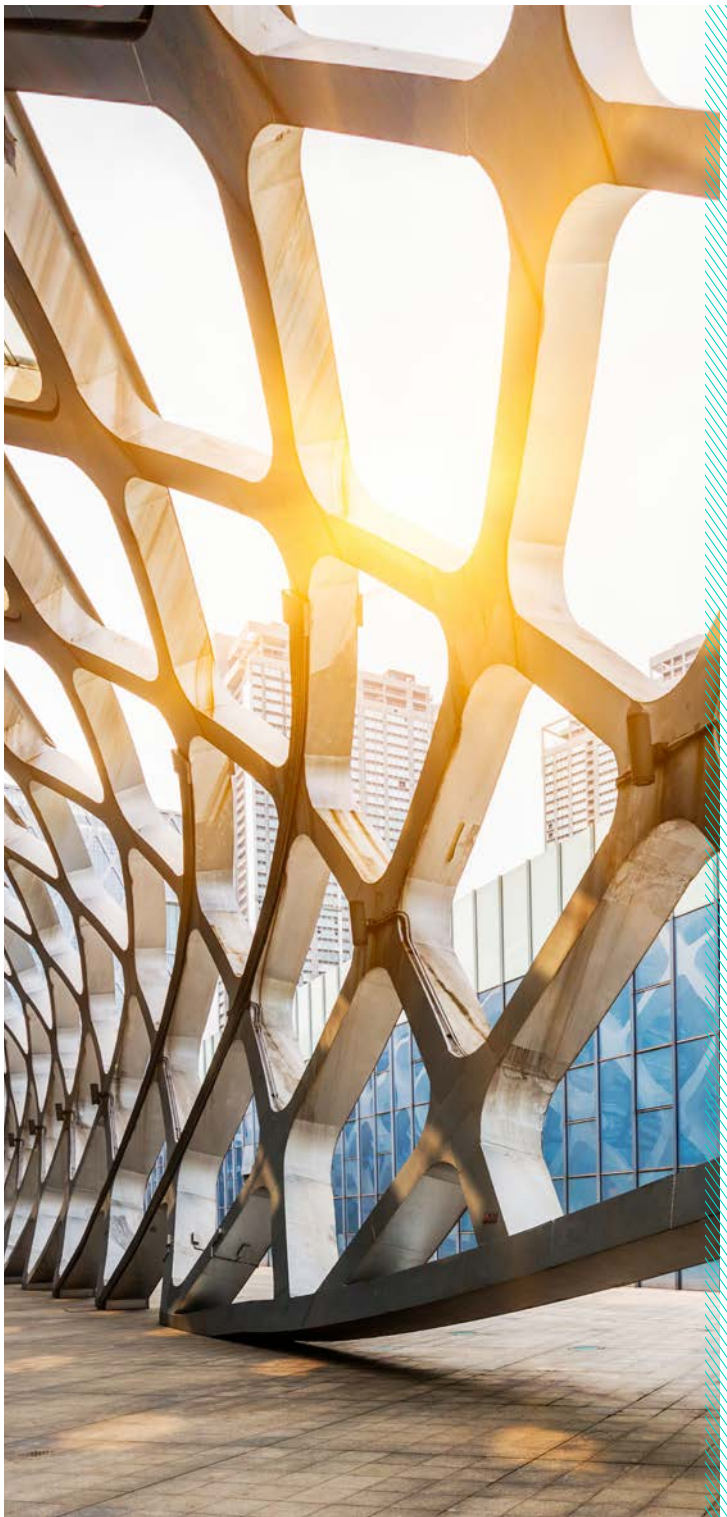
provision into the transaction documents. Cash bids are likely to trump offers that involve buyer equity in light of current market volatility.

Transactions which have signed but not completed:

Examine any regulatory consents which are required to complete. Are there likely to be delays in obtaining these?

Regulatory approvals, be it merger control or central bank approval, can delay even the best-laid plans between signing and completion. Compliance requirements will continue to apply irrespective of COVID-19 however the process for obtaining such approvals is likely to be significantly delayed.

During the financial crisis in 2008 regulators worked at pace to approve transactions as deal volume was lower. However COVID-19 is different. With office closures and remote working, there is an extra strain on already short staffed agencies. For example, the Irish Competition and Consumer Protection Commission (CCPC) has issued a press release encouraging notifying parties, where possible, to delay filing planned merger notifications until further notice. Where this is not possible, the CCPC has asked that notification forms and all supporting documents be submitted electronically due to the reduced presence of staff on their premises. Further challenges may arise if there is full lock down and government agencies close for a period of time.



Corporate transactions

Is the proposed long-stop date still realistic?

Any period between signing and completion is likely to be more protracted than originally contemplated. As a result, it is likely that the existing long-stop date may need to be revisited and agreement reached between the parties as to a realistic long stop date given the current circumstances.

A buyer should also consider long-stop provisions in debt agreements alongside the acquisition agreement and ensure that the long-stop date in the acquisition is not pushed out past the date in debt agreements.

Are there any shareholder approval issues now arising?

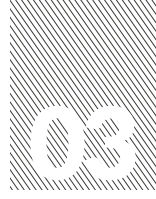
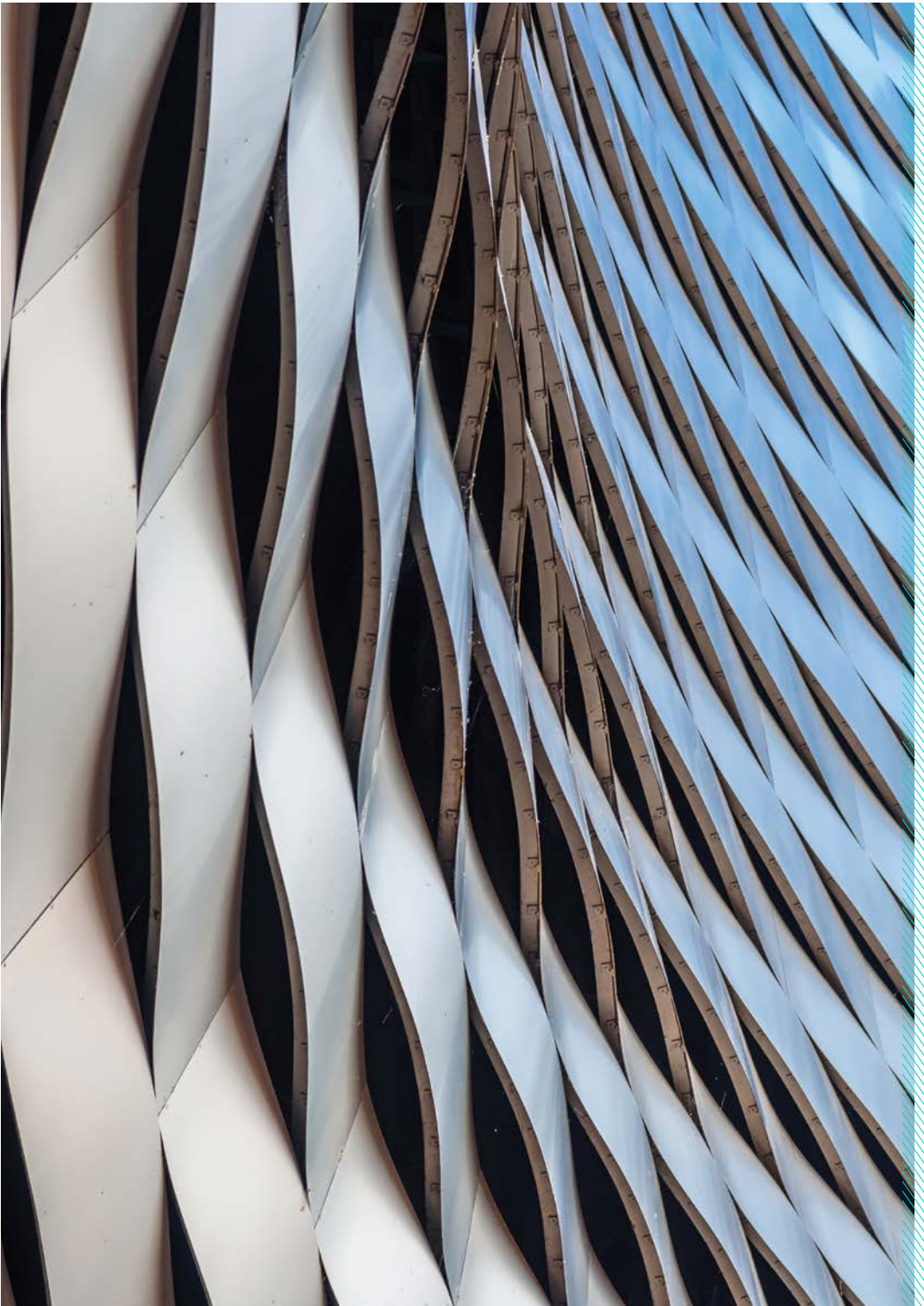
Deals that require shareholder approval, whether on the seller or buyer side, may also face delays on a purely practical level as gathering such approvals in a world of remote working, lockdowns and self-isolation can create difficulties. On the basis that shareholder approvals are typically included as conditions to completion in the transaction documentation the likely delays in obtaining any such approvals will impact on the discussion regarding long stop dates.

Is there any scope to revisit the purchase price?

For already announced deals, buyers and sellers may have to live with pre-coronavirus terms. For new deals, at least in the short term, we can expect that COVID-19 will likely result in a move away from typical purchase price adjustment mechanics. What constitutes “normalised” working capital, which is typically prescribed in the transaction documentation, may need to change. Sellers will likely need to undertake radical measures to maintain acceptable liquidity at target company level and may look for specific mechanics in purchase price adjustment to avoid being unduly impacted during the crisis. On the flip side, buyers will want to ensure the target has sufficient levels of working capital and liquidity once it takes control.

Have the interim operating covenants been breached?

Interim covenants in respect of the operation of the target's business between signing and completion, for example compliance with debt covenants or no restructuring may well have been breached or need to be adjusted to ensure the target's continued solvency. As these covenants can be waived with the buyer's consent, from a seller's perspective it is important to engage early with the buyer in relation to any potential breaches rather than waiting for the breach to occur and providing the buyer with a potential termination right.



Looking ahead - lessons from the global financial crisis

The outlook for M&A activity is understandably uncertain. However markets have faced similar crises in the past – the global financial crisis in 2008 was, albeit quite different, also severe.

We can learn from the remedial measures deployed after the financial crisis to improve our planning and risk mitigation in current circumstances.

For example, following the global financial crisis, we saw an increase in clients establishing strategic partnerships or an increase in buying or selling a stake rather than the entire company. COVID-19 could have a similar impact, with buyers and sellers reassessing the way in which they approach M&A.

The COVID-19 pandemic will hopefully be a short-lived emergency. Future planning in uncertain times is critical. The following considerations could assist with your transaction planning:

- Revisit any transactions completed during the financial crisis. Is there anything you would have done differently then? If so, should the Board consider this in the context of the current transaction?
- Consider entering into strategic partnerships which may diversify your business in a positive way.
- Consider JVs or strategic partnerships which limit your financial exposure in the short term but with an ability to formalise commitments at a later date when there is greater stability (put and call options for example).
- Is there an opportunity to purchase or sell a stake in a business rather than the entire business?
- Consider structuring transactions around preference or convertible shares to allow the parties to find an agreement on valuation.

Please do not hesitate to contact A&L Goodbody if you wish to discuss any of the matters raised in this publication.

In our next edition we will continue to look at the impact of COVID-19 on company Boards as the disruptive effect of the pandemic intensifies.

If there are any issues relating to the impact of COVID-19 which you would like to see dealt with in future editions, please contact any member of the [Corporate and M&A team](#).



You will find a full range of timely materials for businesses in our dedicated [COVID-19 HUB](#) on our website.



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