



MERGERS AND ACQUISITIONS

Buying and Selling Businesses in the Current Market

by **Gerry Halpenny**

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Increased mergers and acquisition activity in Ireland means there are lots of deals to be done. But to get the best results, you need the best advice, as Gerry Halpenny explains

Ireland's mergers and acquisitions (M&A) market is recovering, once again there are deals being done. Prospective buyers are active in the market and sellers who held off selling following the crash are now more realistic in their expectations.

LK Shields Solicitors have seen recent activity in the pharma/medical, retail, recruitment, telecoms, energy, internet, financial and food/food services sectors. While distressed asset sales are still common, and the majority of acquisitions remain funded by larger corporates with their own resources, bank and other finance is again readily accessible to fund deals.

It is important to be aware of some of the characteristics that drive the shape of deals done in the Irish market.

Mind The Gap

In many jurisdictions, legal or regulatory requirements mean that there will always be a gap between the signing and closing of an acquisition agreement. In Ireland, most deals sign and complete at the same time. The need for a gap arises generally where there is a third party approval (such as a regulator or key business contact of the target) required that cannot be sought until an agreement has been signed. Any internal or discretionary condition in favour of the purchaser should be resisted by the seller, because it effectively changes a purchase agreement into an option in favour of the purchaser.

During the gap period, restrictions may be placed on the activities of the target, which protect the purchaser's interests but which may damage the interests of the target should the deal collapse. Usually, the seller will be required to repeat at completion any warranties about the business given on signing, so warranting a state of affairs at a future date, something that is never very palatable. So sellers should resist a gap unless absolutely unavoidable.

Consideration Adjustments

Years ago, it was pretty simple. The seller and purchaser agreed a price, a purchase agreement was signed and the deal completed. Usually there was a net assets warranty in the agreement, together with warranties on the target accounts and operations since the date of those accounts. Nowadays, it's a bit more complicated.

Purchase price adjustments are now almost inevitable, calculated by reference to accounts prepared as at closing.

Adjustments may be by reference to net cash/debt, normalised working capital and net assets. Deals are often done on a "cash-free, debt-free" basis, adjusting for any cash or debt in the business, but there can be disputes about what those terms mean, such as whether finance leases constitute debt.

If the price has been calculated as a multiple of profits, the completion accounts may be used to verify those profits. Any variance from the expected profit levels can produce a significant price adjustment because of the multiplier, so it is important for the seller to be confident in the financials of the target and for the purchaser to be able to conduct a full review of the figures.

'Earn-outs', where part of the purchase price is paid in the future by reference to future performance of the target, have become popular again. An earn-out allows a purchaser to hedge its bets somewhat, deferring payment of part of the consideration until it knows how the target is trading. The earn-out also provides an incentive for the sellers to maximise profits and increase the amount of consideration they receive. As the purchaser will be in control of the target after closing, the seller will need some protections in the purchase agreement regarding the future operations of the business.

Escrow Arrangements

Escrows involve depositing part of the consideration in a secure account pending determination of specified issues, usually the amount of any consideration adjustment or warranty or indemnity liabilities. Escrows almost always benefit the purchaser, ensuring that funds are available to meet any anticipated payment obligation of the seller.

Escrows are unusual in Ireland, usually seen only where likely liabilities of the seller have been identified, or where the seller's creditworthiness after closing is in doubt. In the USA, where escrows are more common, usually between 10% and 20% of the consideration goes into escrow, but the escrow is often the only recourse for most claims.

In Ireland, the cap on liability is invariably higher, between 50% and 100% of the consideration. The seller should always resist the concept of escrow unless there is a specific reason for it.

Negotiating a good deal requires knowledge of what sellers and purchasers will be willing to accept. The relative bargaining position of the parties will dictate much, but receiving commercial and pragmatic business advice is vital as transaction documents become ever-more complex; the good adviser will not waste time negotiating provisions that may never have any practical application.

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