MERGERS & ACQUISITIONS 1: OVERVIEW AND TRANSACTION TYPES: DEAL POINTS

October 2024

I. Executive Summary

Mergers & Acquisitions (M&A), the transactional process by which a business is bought and sold, is a topic about which many business executives and even their professional advisers know less than they would like, but do not always feel comfortable asking questions about that might betray ignorance. No other area in corporate law and finance is as shrouded in murky terminology by its practitioners and treated as specialized knowledge for which they alone can supply the answers. Most practice guides to M&A are either too dense to be accessible to non-specialists, or too superficial to convey practical and usable information. We are revising, expanding and updating our 2022 series of advisories on M&A in a specific effort to bridge the gap and offer to business executives and their professional advisers an M&A guide both accessible and of practical use when embarking on an M&A transaction in their own business. In doing so, we will follow the format of our other practice guides like "Raising Capital through Private Placements: Deal Points" (available at **Kurtin PLLC Raising Capital**). This advisory, the first in the M&A series, will give a general overview to the topic and survey of transaction types. All advisories in the series will be available on our website at **Kurtin PLLC Mergers & Acquisitions** and **Kurtin PLLC Whitepapers and Advisories**.

Following the discussion in each advisory in the series are "Deal Points" on considerations in the purchase or sale of a business when we handle these types of transactions for our clients: what to do, and *what at all costs not to do*. Future editions in the series will drill down on issues like tax considerations driving M&A transactions and transaction structures; preliminary documentation like letters of intent (LOIs), memoranda of understanding (MOUs) and Term Sheets; due diligence; transaction documents; securities law considerations, especially when public reporting companies are parties to the M&A transaction; antitrust (competition) law issues; financing the M&A transaction; foreign investment review and technology export rules; employment and equity-based compensation; Cross-border M&A (where Acquirer and Target are domiciled in different countries) and industry-specific regulatory regimes. A progressively cumulative glossary of defined technical terms used will appear at the end of each advisory in the series.

II. M&A Overview

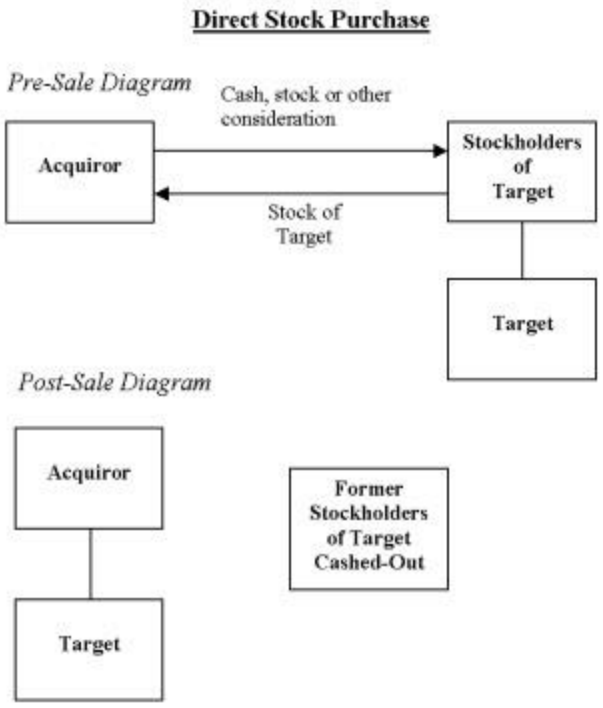
M&A is a catch-all term used collectively to refer to a variety of transactions by which a business entity or person (Acquirer or Buyer) acquires all or the majority of the stock or assets of another business (Seller or Target). Negotiated, as opposed to unsolicited or hostile, M&A transactions are essentially contractual agreements, falling into one of three basic forms: a Stock Purchase, by which a business is acquired by buying its equity securities; an Asset Purchase, by which a business is acquired by buying its assets (whether tangible, like manufacturing machinery, or intangible, like intellectual property); or a Merger, a process by which one business merges into another, and the combined merged business carries on the business of its predecessors. The principal transaction documents for each form are generally called, respectively, a Stock Purchase Agreement, an Asset Purchase Agreement, and a Merger Agreement or Agreement and Plan of Merger. Each type of document routinely contains certain elements. Among these are a description of the basic transaction contemplated by the agreement; the Acquisition Consideration or Merger Consideration (the purchase price), in what form it is to be paid (cash, stock, assumption of debt or some combination), and how it may be adjusted to take account of the occurrence or non-occurrence of certain contingencies; "conditions to closing," the failure of which to be satisfied relieves the beneficiary party from its obligation to close the transaction after the deal is signed; representations and warranties by Target and Acquirer that a certain state of affairs exists as of the date of the agreement's signing, and in some cases, as of closing; affirmative and negative covenants, promises by Target and Acquirer to either do something or refrain from doing something or to preserve a represented state of affairs until closing; termination provisions, which provide for when a transaction can be called off after signing but before closing; and others, such as choice of governing law and dispute resolution provisions.

III. Typical M&A Transaction Structures

M&A transaction structures fall into three basic categories: (a) a Stock Purchase, in which the Acquirer acquires all or most of the Target's stock; (b) an Asset Purchase, in which the Acquirer acquires all or significant portion of Target's assets out of the Target's ordinary course of business (for example, not merely buying all of Target's existing inventory that it sells in the normal course of business, but the means of creating or obtaining further inventory); and (c) a Merger, which is a means of combining two businesses by a merger procedure set forth in a state's corporate law statute, in which one of the companies is the "Surviving Entity" and the other is merged into it and ceases to independently exist.

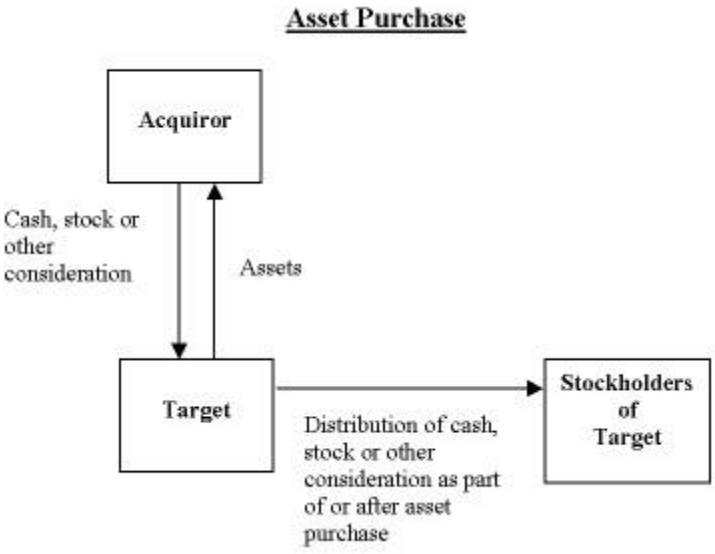
As one would think, the Surviving Entity is normally the Acquirer, but not always, as will be discussed below.

a. Stock Purchase. A Stock Purchase is ostensibly the simplest M&A transaction type. It can be accomplished as simply as by Acquirer's executing a Stock Purchase Agreement with Target's shareholders. The Target is not a party to the transaction but becomes Acquirer's subsidiary. In a Stock Purchase, the by buying Target's stock, Acquirer automatically succeeds to all of Target's assets and liabilities.



b. Asset Purchase. In an Asset Purchase, the transaction is usually directly between Acquirer and Target. Target does not become a subsidiary of Acquirer; it continues to be owned by its current shareholders, who do not directly receive the Acquisition Consideration. All other things being equal, the Asset Purchase is the preferred structure for an Acquirer, because it can pick and

choose among Target's assets rather than take (and pay for) assets and assume liabilities it may not want, as it does in a Stock Acquisition.

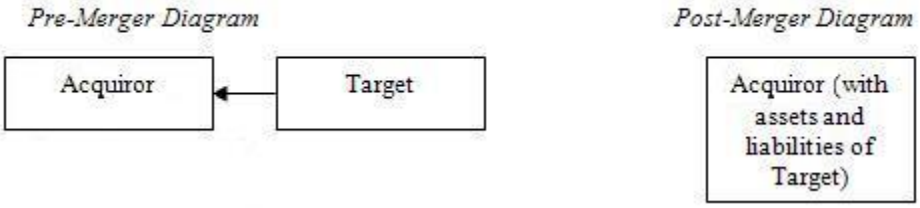


c. Merger. Mergers are a transaction form created and governed by state corporation statutes such as the Delaware General Corporation Law (DGCL). The use of a statutory merger provides both ease and established legal certainty. When the certificate of merger is filed with the Secretary of State of the state of incorporation, one company merges into the other, the first company's legal existence ends, and title to its assets and liabilities transfer automatically to the Surviving Entity.

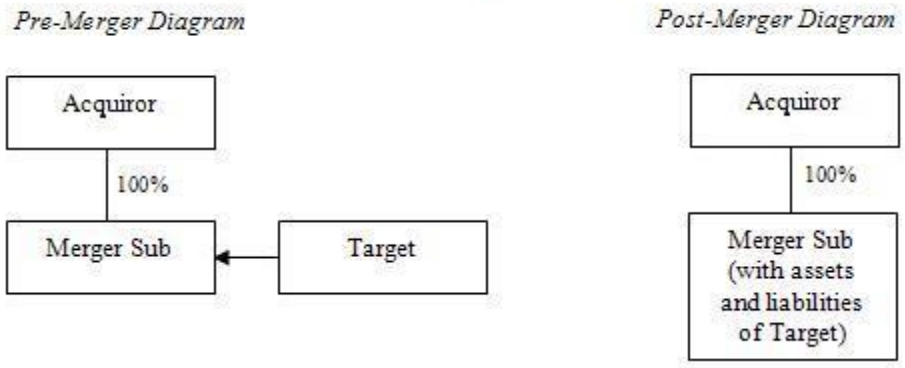
In a Direct Merger, Target merges directly into the Acquirer, which is the Surviving Entity. In a Reverse Merger, Acquirer merges into Target and it is Acquirer that ceases legally to exist, while the Target is the Surviving Entity. In a Forward Triangular Merger, Acquirer forms a subsidiary (Merger Sub) (or uses a pre-existing subsidiary) to serve as a vehicle for the merger, Target merges into Merger Sub, and Merger Sub is the Surviving Entity and subsidiary of Acquirer. In a Reverse Triangular Merger, Merger Sub merges into Target, and Target is the Surviving Entity, becoming a subsidiary of Acquirer. The Reverse Triangular Merger format can allow Acquirer to remain separate from, and structurally unaffected by, the core transaction, while allowing Target to become an intact operating subsidiary of Acquirer. The Reverse Triangular Merger structure also often allows Acquirer to take control of Target without triggering anti-assignment

provisions in third-party contracts to which Target may be bound. The need to obtain third-party consents and the assignment clauses of agreement to which Target is a party can be a significant factor in driving transaction structuring. Some third-party agreements can represent so much of Target's enterprise value that a failure to obtain the third-party consent to assignment could derail the transaction.

Direct Merger



Forward Triangular Merger



IV. Deal Points

Deal Point No. 1: Don't sneer at the LOI, MOU or Term Sheet. Don't sneer at the Letter of Intent (LOI), Memorandum of Understanding (MOU) or Term Sheet, even if most or all their terms are not binding on the parties. As often as not they embody the *de facto* or binding structure of the deal, and advantages casually given away by treating the LOI, MOU or Term Sheet as a low-level document not requiring serious attention may never come back. Also, even if most of the LOI, MOU or Term Sheet are not binding, there can be serious value in making some terms binding, such as a confidentiality provision, a "break-up fee" (a fee to be paid by one party to the other for pulling out of the deal), or others.

Deal Point No. 2: The business case should drive the deal and deal structure, not vice-versa. This sounds like a bromide. Think again. Overcomplicated deal structures and deal documents are a stock in trade of many Acquirers and, sad to say, many Acquirers' law firms and investment banks. A few years ago, we were called in to help on the buy side with a piece of a not terribly large or complicated deal, one which had a few, but only a few, wrinkles because some industry-specific government regulation and multiple pieces of real property subject to assignment restrictions had to be addressed. The client's lead law firm, a large but not especially elite regional firm, had drafted the equivalent of a Stock Purchase Agreement (the Target was a Limited Liability Company, or LLC, so what was being purchased were technically "membership interests," not stock) that was 75 pages long and so grossly byzantine that I had trouble reading it. It was apparent that Target, and Target's local attorneys, could not make head or tail of the document, and that the deal, which Target wanted to do at least as much as

Acquirer did, was stalled for weeks on end for that reason alone. The transaction was finally dragged over the finish line, but it was painful to see, and of course more expensive than it should have been. The deal could have been done on far simpler and shorter papers.

Deal Point No. 3: Like MOU's, LOI's and Term Sheets, Due Diligence should not be an afterthought. Nobody loves doing due diligence. What's even less lovable than due diligence is a nasty surprise after a deal is signed up that doesn't provide an excuse from closing or so obviously breach a representation, warranty or covenant as to justify termination or at least a significant purchase price adjustment. Of course, due diligence should be scaled to the size of the deal, but that doesn't mean it should be blown off, unless the Acquirer has made an affirmative decision that it wants to complete the acquisition come hell or high water, whatever warts post-closing tearing-off of band aids may reveal. There may be a business case for that, but it should be because of affirmative decision-making. More Deal Points in the next M&A edition!

Owen D. Kurtin

About Us

Kurtin PLLC is a New York City-based law firm founded in 2008 and celebrating its 16th anniversary this year. Our practice focuses on corporate, finance, commercial and regulatory representation for both mature and early stage companies, investment funds, investors and lenders in the Biotechnology & Life Sciences, Communications & Media, Information Technologies & Internet, Satellites & Space, and Venture Capital & Private Equity sectors. Among our key values, none rank higher than creative and individualized solutions to business issues, absolute client discretion and unsurpassed responsiveness. Since our founding in 2008, we have represented clients in over 40 countries on six continents and across the United States on transactional and dispute resolution matters.

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Mergers & Acquisitions: Deal Points
Cumulative Glossary
Appendix 1

1. **Acquirer (or Acquirer, Buyer or Purchaser):** the purchaser, or "buy side" party in an M&A transaction, whether an Asset Purchase or a Stock Purchase, which acquires all or the majority of the stock or assets of another business. In a Merger, the parties are not technically purchaser or seller, but when one party is clearly the dominant party in the transaction and is often the Surviving Entity (though not always, as in the case of a Reverse Merger), that party can be thought of as the Acquirer.

2. **Acquisition Consideration:** the purchase price paid by Acquiror to Target in an M&A transaction, whether in cash, stock, assumed debt or a combination thereof.

3. **Asset Purchase:** a transaction by which one party to an M&A transaction purchases all or the majority of the assets of another party. Distinguished from a sale by Target in the ordinary course of business, as in selling a part of its inventory, or surplus equipment not needed for continuing its business operations.

4. **Asset Purchase Agreement:** a contractual agreement serving as the principal document by which an Asset purchase is effected.

5. **Cross-border M&A:** M&A transactions in which Acquiror is domiciled in one country, and Target in another country. For purposes of this M&A: Deal Points series, one of those countries in which either Acquiror or Target is domiciled is the United States.

6. **DGCL:** the Delaware General Corporation Law, serving as a paradigm corporation statute in the U.S., and frequently the basis of incorporation by U.S. companies, wherever physically based, that intend to do business across the U.S. as well as inbound subsidiaries of non-U.S. companies wishing to have operations in the U.S.

7. **Due Diligence:** the scope of the parties' disclosures to each other before the M&A transaction closes, generally buttressed by deal protections in the form of warranties, representations, covenants and linked rights of indemnification, termination, conditions to closing and others.

8. **LLC:** a limited liability company organized under a state's LLC statute, generally offering the limited liability protection for shareholders of corporations with the "pass-through" taxation of partnerships (i.e., not taxed at the LLC level, but taxable income or loss is "passed through" to the owners, called "members," equivalent to a corporation's shareholders). Also usually featuring less burdensome management and governance costs and formalities than equivalent corporations.

9. **M&A:** generally used abbreviation for "Mergers & Acquisitions," a catch-all term sweeping up Stock Purchases, Asset Purchases and Mergers, all involving the legal or *de facto* acquisition of all or a majority of one business's stock or assets by another business.

10. **Merger (or Statutory Merger):** a process set forth in the company law statutes of the individual states by which two companies merge with each other, leaving one company or its subsidiary as the Surviving Entity, while the other company merges into that company or its subsidiary and ceases to exist as a separate legal entity.

    a. **Direct Merger:** A Merger structure in which Target merges directly into Acquirer, which is the Surviving Entity, while Target ceases to exist.

    b. **Reverse Merger:** A Merger structure in which Acquirer merges into Target, which is the Surviving Entity, while Acquirer ceases to exist.

    c. **Forward Triangular Merger:** A Merger structure in which Acquirer forms a subsidiary (**Merger Sub**) (or uses a pre-existing subsidiary), Target merges into Merger Sub, Merger Sub is the Surviving Entity and a subsidiary of Acquirer, while Target ceases to exist.

    d. **Reverse Triangular Merger:** A Merger structure in which Merger Sub merges into Target, Target is the Surviving Entity and becomes a subsidiary of Acquirer, while Merger Sub ceases to exist.

11. **Merger Agreement (or Agreement and Plan of Merger):** a contractual agreement serving as the principal document by which a Merger is effected.

12. **Merger Consideration:** the Acquisition Consideration in a Merger.

13. **Preliminary Document: (MOU, or Memorandum of Understanding; LOI, or Letter of Intent; or Term Sheet. Also, NDA, or Non-Disclosure Agreement, which may be part of an MOU, LOI or Term Sheet or a standalone Preliminary Document):** forms of preliminary documentation used to set a framework for an M&A transaction and confidentiality before executing documents like an Asset Purchase Agreement or Stock Purchase Agreement. Some terms in preliminary documentation may be binding on the parties for a certain period, for example confidentiality or exclusivity, while others are usually not binding.

14. **Stock Purchase:** a transaction by which one party purchases all or the majority of the stock of another party. Distinguished from a minority investment by one party in the other, such as a typical venture capital investment, which is not an M&A transaction.

15. **Stock Purchase Agreement:** a contractual agreement serving as the principal document by which a Stock Purchase is effected.

16. **Surviving Entity:** the company that continues its corporate existence and operations following a merger.

17. **Target (or Seller):** the seller, or "sell side" party in an M&A transaction, whether an Asset Purchase or a Stock Purchase, which sells all or the majority of its stock or assets to another business, the Acquirer. In a Merger, the parties are not technically purchaser or seller, but when one party is clearly the less dominant party in the transaction and is often the merged party (though not always, as in the case of a Reverse Merger or Reverse Triangular Merger, that party can be thought of as the Target.