

**15.617, Spring 2004**  
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**Lecture 9: 3/3/04**

Guest: Terry Mahoney, Partner, Leboeuf Lamb Greene & McRae

Page 23: work our way through purchase agreement.

Stock Purchase Agreement prepared by Kirkland and Ellis.

- 1.) Buyer's counsel prepares agreement (Seller responds)
  - 2.) Negotiation. Ask –
    - Why did buyer pick specific language?
    - How does the seller respond?
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- In agreement, Article 2: has the price. How do we figure out price
    - value of assets
    - growth potential (needs to generate earnings)
    - multiple of cash flows (earnings)
  - The buyer wants to put as many conditions as it can.
  - Seller wants no conditions.
  - If you breach a covenant you get sued.
  - Reps (representation) ties into the conditions to close.
  - Page 37: "We're in conditions to closing."
  - Look at 3:1.A
  - Reps are true on the day you sign and close (w/o taking into account disclosure on pg. 56)
  - Page 56: Look at Representation: "The last Rep made by the seller says that the above will be true on the closing date, unless I tell you otherwise in writing."
  - The buyer is saying I came up with a price based on the information you gave me → this is true → if not it's a different game.
  - It's given the buyer a chance to regenerate. If we come to closing, and the company blows up, then Rep isn't true.
  - These conditions have no material adverse effect.
  - These covenants try to tackle this.
  - Buyer knows that things change.
  - Avoid "cock-tail" with the bankers.
  - It is difficult for both the buyer and seller. It is based on the fate of your opponents (do they have a good history?)
  - Obligation of good faith: it covers cocktail with bankers. Did the people operate in and above the Board's manners?

## Covenants:

### \* Seller is alert here!

- Buyer wants seller to take good care of the assets. Why would seller cross this out?
- Once the seller signs, that's it.
- Seller must continue to conduct its business in the ordinary course.
- Any time you have 2 provisions dealing with the same stuff it is bad because court will want to give it more "power." Since they will say what was covered in "E" was covered in "A."
- Why is "material" so important?
  - Without material, if Xerox says "no" buyer could say I don't want to close because you didn't get every single 3<sup>rd</sup> parties' consent.
- Page 46, Figure 5.7
- Be in accordance with GAAP.
- Tell us everything you know. Don't hold back secrets.
- Buyer vies this as a risk-allocation provision. IF something "crops up" it is your (seller) problem.
- For example: Should B assume warranty obligations → B says NO, but warranty expense is an ongoing expense, and you should have a reserve of it.

### How do you determine the proper multiple?

- Market multiple ( you get all of the junk with it)
- Page 56, Section 5-23.
- Everything you tell us should be true.
- If this was a honesty clause, and not a risk clause, then you can't burn anything.
- IF business went south → WHY?
  - B/c of market?
  - Other competition?
  - Pricing pressures?
  - Is it the seller's job to teach buyer about the market?
- Everyone should do their homework.
- Page 62: Indemnification Clause: If you breach a covenant or Rep, I, the Buyer get to sue the Seller. Without this clause you can still sue people. It allows you to recover your attorney's fees.
- There is a risk business people take to buy an asset, because someone else will buy it. That's why if you state 80M, you'll take 40M.
- If people think that something went wrong, they will sue.
- How do you defend "80M"? Perhaps historical basis or relative?
- Legal fees: 1-2% of purchase price → driven by practice (powerful!)