



M&A Building Blocks

Introduction to the Deal



Buying and selling is a basic human activity that has been going on for thousands of years. Mergers and acquisitions – M&A – involves buying and selling at a highly sophisticated and complex level because it concerns not just the sale of a product, but of a whole business including the means of producing products and services and the infrastructure that goes with it.

The most essential element of any M&A transaction is agreement on the price to be paid. But there are many other issues which must be agreed upon before a deal can be struck or a transaction completed. While each deal is unique, there is a recognizable sequence of events or process that most deals follow, at least to some extent. Key threshold issues and process points are discussed below.

Key Issues/Process Points

While the relative importance of the following matters will vary from deal to deal, all of them usually play at least some role in bringing a deal to conclusion.

1 Due Diligence

Purchasers will want to kick the tires before finalizing a price. While the outlines of a deal can sometimes advance quite far before due diligence is complete, at minimum “confirmatory due diligence” will be necessary at some point before money changes hands. Some of the principal issues associated with due diligence include:

- **Confidentiality or non-disclosure agreements:** Potential purchasers are usually required to agree to keep confidential any information disclosed to them. These agreements may include “standstill” provisions prohibiting the purchaser from buying securities of the seller, and/or provisions preventing the poaching of employees.
- **Contracts:** Is the seller bound by contracts which, from a legal or business perspective, require consent before the business can be sold? Or which will have an adverse impact on the business after the sale?
- **Title:** Especially with real estate and IP assets, does the seller have good ownership to its assets? Are there assets subject to security arrangements or mortgages with lenders?
- **Employees:** Can the key employees be retained by the buyer? Do they have the right to leave and be paid large settlements? Are there constraints on combining the target’s work force with the buyer’s? Privacy laws may affect the disclosure available.
- **Environmental:** Are Phase 1 or 2 reports appropriate given the nature of the assets to be acquired?
- **Litigation/Potential Liabilities:** Does the seller have outstanding litigation which could lead to liability? Are there other potential liabilities for, by way of example, warranties, product liability, regulatory breaches, negligence, or accounting or financial misstatement?

2 Approvals

Transactions routinely require approvals, such as:

- **Competition Act:** Pre-merger filings and approvals are required for transactions meeting certain size thresholds.
- **Investment Canada Act:** Acquisitions by non-Canadians of Canadian businesses above a certain size, involving cultural industries, or raising issues of national security, require approval.
- **Regulatory:** Many industries have licensing, permitting or other regulatory regimes which require approvals for a change in ownership, including companies in the financial sector, seniors housing, natural resources, communications and broadcasting, and transportation.

3 Financing

Depending on the nature of the seller’s assets and the buyer’s financial resources, financing can be a very significant element to a transaction. For example, if the target’s existing financing arrangements are to be assumed by the purchaser, the purchaser may need to negotiate with the target’s financing parties.

4 Structure

Most deals can be implemented in more than one way, but there may be many reasons, often but not always tax-related, why a particular structure is better than another. Both the buyer and the seller will have views in this regard. For friendly acquisitions involving public companies, the statutory plan of arrangement has become the method of choice to implement a deal because of its flexibility in allowing a transaction to encompass many steps designed to achieve various objectives.



5 Timetable

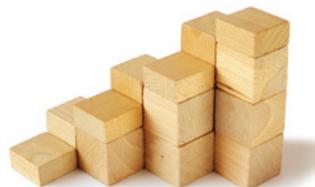
An M&A transaction has a number of recognizable stages. Certain stages may have more or less prominence because of the way a particular deal develops, the relationship of the parties, the financial position of the seller or any number of external factors. From a seller's perspective, the key stages might include:

- **Retaining advisors and consultants:** Legal, financial, environmental, engineering/structural and/or valuation experts may be required.
- **Offering the target for sale:** This could include steps such as drafting and circulating a confidential information memorandum, soliciting bids, creating a data room to allow prospective purchasers to carry out due diligence, exploratory approaches to prospective purchasers, and/or pre-transaction structuring to sever certain assets or implement tax planning.
- **Negotiating the deal:** This often occurs in one or more stages, as certain basic terms might be fixed at the time of accepting a particular bid, then fleshed out in a letter of intent or term sheet, and then finally agreed upon in great detail in a definitive purchase agreement.
- **Announcement:** A critical point in time for any deal is when it is announced. The parties learn what the market thinks of their deal and receive preliminary indications as to whether their shareholders are likely to approve. Employee expectations, too, must be managed.
- **Shareholder approval:** The requisite target shareholder approval (and sometimes other security holder approvals) must be obtained either by way of the purchaser making a take-over bid which shareholders may accept or reject, or the target holding a shareholder meeting at which shareholders vote upon the transaction. Sometimes significant shareholders are "locked up" in advance through a commitment to tender to a bid or vote in favour of a transaction. Depending on applicable stock exchange rules, if the purchaser is issuing shares as part of the purchase consideration, the purchaser may also need its shareholders to approve the deal. In all cases, a disclosure document, either a proxy circular for a shareholder meeting, or a take-over bid circular and directors' circular, must be prepared and sent to the relevant shareholders.
- **Regulatory approvals:** Regulatory approval applications are usually commenced following the announcement while the applicable shareholder approval process is underway although the regulatory approvals themselves may take much longer. Sometimes tax rulings are necessary and they, too, have a long time horizon.
- **Third party consents/financing:** Also at the same time, third party consents and financing arrangements, if necessary, are secured.
- **Closing:** Once everything is in place, the transaction closes and the purchase price can be paid.

As noted at the outset, M&A transactions can be complex and the timeline for a transaction is typically measured in months. A time frame of a year or more is not atypical from the time a seller begins to undertake a sale process until the time it is complete.

Conclusion

The above only scratches the surface of the M&A process. In coming issues, we will explore specific deal points in more depth.



AUTHOR

Paul Mingay

T 416.367.6006

F 416.367.6749

pmingay@blg.com

KEY CONTACT

Frank Callaghan

National Group Head,
Corporate and Capital Markets

T 416.367.6014

F 416.367.6749

fcallaghan@blg.com

Calgary

Centennial Place, East Tower

1900, 520 – 3rd Ave S W, Calgary, AB, Canada T2P 0R3

T 403.232.9500 | F 403.266.1395

Montréal

1000 De La Gauchetière St W, Suite 900

Montréal, QC, Canada H3B 5H4

T 514.879.1212 | F 514.954.1905

Ottawa

World Exchange Plaza, 100 Queen St, Suite 1300

Ottawa, ON, Canada K1P 1J9

T 613.237.5160 | F 613.230.8842 (Legal)

F 613.787.3558 (IP) | ipinfo@blg.com (IP)

Toronto

Bay Adelaide Centre, East Tower

22 Adelaide Street West, Suite 3400, Toronto, ON, Canada, M5H 4E3

T 416.367.6000 | F 416.367.6749

Vancouver

1200 Waterfront Centre, 200 Burrard St, P.O. Box 48600

Vancouver, BC, Canada V7X 1T2

T 604.687.5744 | F 604.687.1415

blg.com/ma



BLG
Borden Ladner Gervais