

CHAPTER 1

Organizing the Acquisition Review

COMMUNICATING WITH THE CLIENT

The lawyer who is engaged to represent the purchaser in an acquisition may need to educate the client about a variety of matters, including the options available to the client in regard to the scope of acquisition review, and will need to reach an understanding with the client on these and other issues.

One important goal of the purchaser is to complete the transaction efficiently and promptly. At the same time the purchaser expects its lawyer to protect it from risk. As one lawyer has observed,

Lawyers usually bring to each transaction . . . a penchant for detail, the ability to scrutinize, and an eagerness to investigate that is not present in other professionals. These are the characteristics that cause lawyers to be called nitpickers, deal busters, and a variety of other names. These characteristics, also, are the reason lawyers are hired.¹

The acquisition review is a potential obstacle to a quick and painless closing. The purchaser hopes (but, one expects, is never entirely confident) that its attorney will concentrate only on matters of material risk of loss. The seller naturally fears that the purchaser may learn something that will cause the purchaser to lose interest in the deal or to seek to renegotiate the price. Even if the seller is fully candid, there will be issues requiring extensive work by the purchaser's counsel to uncover and analyze the pertinent facts.

As early as possible in the transaction, counsel should meet with the client and agree upon the scope of the acquisition review and the basis of the lawyer's fees for those services.

ALLOCATION OF RESPONSIBILITIES AND COORDINATION OF EFFORTS

In some transactions, outside counsel may be asked to be the "captain of the team"--to gather and deploy all of the persons needed to make the investigation. In other transactions, an executive of the client may manage the process. It depends on the relative knowledge, experience, personality, and availability of the executive and the lawyer, and on the other resources available to the client. As the person principally responsible for the acquisition agreement and for determining the satisfaction of conditions to closing, however, the lawyer should endeavor to be aware of all findings of the investigation.

In whatever way the responsibilities for the acquisition review are allocated, the following principles are relevant:

- a. There should be a clear understanding by all participants of the responsibilities of each participant.
- b. The course and results of the review should be assessed periodically as

the transaction proceeds. It may be easier to make adjustments in mid-review than to reopen the inquiry.

c. The results of the review should be gathered in a form that can be readily digested. Sometimes this can be done by a single checklist, with the findings incorporated in the document. In other cases, the result may be a series of memoranda gathered in a loose-leaf binder. It is not necessary, however, to make a written summary of everything that may be learned in the review.

d. There should be some mechanism for sharing among all participants the information gathered during the review, particularly if there are various teams operating semiindependently. In particular, the lawyer should insist on seeing everything that could be deemed to be a written representation and on being told of any significant conversations. Often documents may pass from executives of the target to executives of the purchaser, apart from the formal disclosure process.

In situations in which the client wishes to have parts of the acquisition review performed by its staff lawyers, by its executives and staff, and by third parties, including benefit consultants, environmental auditors, etc., outside counsel should ask for a clear understanding of what he or she is not responsible for. For example, the lawyer may say to the client (given the name Beyer Corporation in this example):

We understand that you wish us to take overall responsibility for the review of the business and affairs of Target Company; to brief each of the persons or groups that will participate in this effort on the critical aspects of the transaction; to consolidate the findings and evaluations of the various investigators; to draft the purchase agreement in light of the findings and conclusions; and to disseminate the findings and conclusions in accordance with your instructions.

We will organize the investigation of the legal aspects of Target Company, in particular the following:

- a. its corporate documents,
- b. its contracts,
- c. its real estate records,
- d. its governmental authorizations and approvals, and
- e. its litigation.

We will work with Andrea Hamilton, Vice President-Law, and her staff and such representatives of your financial and marketing departments as may be designated to participate in this transaction.

We will make a preliminary evaluation of any patent or other intellectual property rights held by Target, and of any such rights held by others that may be implicated by Target's activities. Depending on our findings, we may recommend that you retain special counsel to advise you on these matters.

We understand that you have engaged Friends of the Environment, Inc., to

review Target's permits and its pollution and hazardous waste situation. We will meet with them to ensure that they appreciate the legal significance of these aspects of Target's affairs.

We understand that members of Beyer's comptroller's office and of its finance staff, together with representatives of Beyer's independent certified public accountants, will review Target's tax returns, will advise Beyer regarding the tax implications of the proposed transaction, and will prepare any desired ruling requests.

We understand that the finance/audit team, together with professionals from ERISA Associates, Inc., and a lawyer from Ms. Hamilton's staff, will review Target's employee benefit plans. We will be glad to advise the tax and employee benefits teams on any legal matters that they may raise with us, and we will refer to them any information that comes to our attention that is pertinent to their inquiries. But apart from such incidental consultations, we will leave the review of these aspects of Target's business to such other groups.

Enclosed is a draft of a work program for the Beyer team that assigns to various persons and groups responsibility for the tasks we anticipate will be necessary to complete the acquisition review and that sets tentative targets for their completion. We understand that Beyer's executives responsible for this transaction will consult with all interested parties and prepare and distribute a definitive work program.

We suggest that a meeting be held of the Beyer employees involved in the transaction, the other Beyer advisors and ourselves, to attempt to locate where the value and the risks are, and to settle how we will proceed.

WRITTEN OR ORAL COMMUNICATIONS

There are advantages to writing a letter to make suggestions on how to proceed or to confirm understandings that have been reached. Letters tend to be more precise and complete and to be taken more seriously than statements in meetings or telephone conversations.

Where the acquisition transaction is the first matter for the client in respect to which the lawyer is engaged, the lawyer generally will conclude that it is preferable to confirm in writing the agreement with the client concerning the scope of the acquisition review. On the other hand, counsel who has regularly represented the client in acquisitions may be confident that there is a true understanding of the allocation of responsibilities and the risks associated with any limitations upon the review. Counsel in those situations may conclude that sending a letter would be counterproductive because it would imply that counsel is not confident of the reliability of the client's prior conduct. In addition, a lawyer may anticipate that the scope of counsel's role in the acquisition review will change during the course of the engagement and that it would be awkward to send a letter memorializing each such change.

The Hypothetical Work Program for an Acquisition Review shown at the end of this chapter is a useful device both for the organization of the

acquisition review and as a vehicle that can be used to reflect limitations on the lawyer's responsibility.

THE DOCUMENT REQUEST

It has become commonplace, at least among large corporations and metropolitan law firms, for the purchaser's counsel to begin the acquisition review process by sending a "document request" to his or her counterpart representing the seller. The forms used for these requests inevitably become longer and more detailed over time, and although it is appropriate for the purchaser's counsel to request copies of documents (in addition to review of the seller's disclosure contemplated by the acquisition agreement), issuing an overblown document request referencing items clearly inapposite to the transaction may create an initial friction between counsel. Appendix A to this Manual contains a sample Document Request Form typical of the requests issued by large firms with significant acquisitions practices. No attempt has been made to create a document request that is entirely congruent with the inquiries identified in the Manual, because all of the substantive inquiries discussed in the following chapters are believed to be substantially more extensive than those that would be required in many transactions. The sample Document Request contained in Appendix A can be a useful checklist for the purchaser's counsel, and, as refined by counsel to reflect the particular needs of the transaction and the issues identified in this Manual, it can be an appropriate guide to organizing and reviewing the relevant facts regarding the target company.

NOTES

1. Campbell, Management of Title Review, Due Diligence and Other Legal Tasks in Large Oil and Gas Transactions, 31 ROCKY MTN. MIN. L. INST. p. 16-9 (1985).

Hypothetical Work Program for an Acquisition Review Responsibilities and Deadlines for the Acquisition Review of Target Company by Beyer Corporation

A copy of any significant document received from Target Company and a copy of any memorandum or other analysis of information learned about Target must be furnished promptly to W. M. Jones, Assistant General Counsel of Beyer Corporation. It is the responsibility of Mr. Jones to see that copies of documents received from Target are distributed to the appropriate executives of Beyer Corporation and to counsel.

Acntnt, Beyer's Independent Certified Public Accountants
BC/HR, Beyer Corporation Human Resources department
BC/Lgl, Beyer Corporation Vice President-Law and staff
BC/Tech, Beyer Corporation Vice President-Technology and staff
Bnfts, ERISA Associates, Inc.

Compt, Beyer Corporation Comptroller
Env, Friends of the Environment, Inc.
InvBnkr, Beyer's Investment Bankers
Lwyr, Outside counsel
Mfctr, Beyer Corporation Vice President-Manufacturing and staff
Sales, Beyer Corporation Vice President-Marketing and staff
Trsr, Beyer Corporation treasury staff

GENERAL

Deadline, Task, Person(s) Responsible
Prepare statement of responsibilities and deadlines; assign staff, BC/Lgl,
Compt, Mfctr, Acntnt, InvBnkr, Lwyr
Retain environmental adviser, BC/Lgl, Mfctr
Bring together and review information on Target Company currently in the
possession of Beyer Corporation, BC/Lgl, Trsr, Sales, InvBnkr
Collect signed copies of confidentiality agreement, BC/Lgl
Confer with Beyer Corporation's lender(s), Trsr, BC/Lgl
Submit to Lwyr proposals for documents and information to be sought from
Target, all hands
Send document and information requests, Lwyr
Arrange with Target for meetings and interviews between Beyer
representatives and Target executives, BC/Lgl
Order copies, certificates, etc., from third parties, Lwyr
Deliver documents and responses by Target,
Assess results periodically; consider modifying review, all hands
Examine Target records on-site, Compt, Env, Lwyr
Consider seeking estoppel letters, confirmations, etc., from third parties
with which Target does business, BC/Lgl, Compt, Lwyr
Gather information obtained into single file, BC/Lgl, Compt, Lwyr

FINANCIAL

Deadline, Task, Person(s) Responsible
Review documents and responses; prepare memoranda on observations,
questions, etc., Trsr, Compt, Acntnt
Prepare pro forma working capital requirements projection; review projected
capital budget, Compt
Review Target casualty and liability insurance policies; confer with
Beyer's broker; confer with Target's broker, Compt, BC/Lgl
Confer with Target's independent CPA, Compt, Trsr, Acntnt
Review Target credit and security agreements; confer with Target's lenders,
Trsr, BC/Lgl

MANUFACTURING

(INCLUDING ENVIRONMENTAL LAW COMPLIANCE)

Deadline, Task, Person(s) Responsible

Review loss runs; review recalls, retrofits, etc.; review product liability experience of peers, Mfctr, BC/Lgl

Review documents and responses; prepare memoranda on observations, questions, etc., Mfctr

Walk through Bislett plant, Mfctr, BC/HR, Env

Walk through Henley plant, Mfctr, BC/HR, Env

Confer about intellectual property assets and risks of Target, Mfctr, Lwyr

Walk through Morgantown plant; interview staff; sample inventory, Mfctr, Env, Sales, Acntnt

Assess need for capital expenditures; prepare projected capital budget, Mfctr, Trsr

Review supply and sale commitments, Mfctr, BC/Lgl

SALES

Deadline, Task, Person(s) Responsible

Review documents and responses; prepare memoranda on observations, questions, etc., Sales

Confer with Vice President-Sales of Target Company, Sales

Confer about antitrust issues relating to Target's pricing policies and distribution methods, Sales, Lwyr

HUMAN RESOURCES

Deadline, Task, Person(s) Responsible

Review union contracts, grievances, claims charges, census, turnover, benefits, etc., BC/HR, Mfctr, Lwyr

Confer with Target's Vice President-Human Resources, BC/HR

Compare Target labor costs (wage rates, benefits, etc.) to Beyer labor costs, BC/HR, Bnfts,

Prepare memo on implications of Target's practices for Beyer's labor relations with existing employees, BC/HR, BC/Lgl

LEGAL

Deadline, Task, Person(s) Responsible

Search database for litigation against peers/competitors, Lwyr

Review documents and responses; prepare memoranda on observations, questions, etc., Lwyr

Confer with Beyer Engineering/R & D re intellectual property issues, Lwyr, BC/Tech

Review lawsuits and other proceedings against and by Target Company, Lwyr, BC/Lgl

Prepare list of required consents, governmental approvals, etc., Lwyr

