Bloomberg BNA

Mergers & Acquisitions Law Report™

MERGER AGREEMENTS

Trends in M&A Provisions: Alternative Dispute Resolutions (ADR) Provisions

BY DANIEL AVERY AND JOHN MARIANO

Introduction

In merger and acquisition (''M&A'') transactions, the definitive purchase agreement (whether asset purchase agreement, stock purchase agreement, or merger agreement) typically contains representations, warranties, and covenants, along with related indemnification obligations, provided by the parties. [1]

The purchase agreement may also stipulate that non-judicial means to dealing with claims under the agreement, such as arbitration or mediation, are to be utilized, whether before seeking redress by the courts or in lieu of judicial proceedings. These alternative dispute resolution (ADR) provisions are an important component of an M&A purchase agreement, and may also tie in to other related provisions within the agreement.

In 2005, 2007, 2009, 2011, and 2013 the American Bar Association (ABA) released its Private Target Mergers and Acquisitions Deal Points Studies (the ''ABA studies''). The ABA studies looked at the M&A agreements of publicly available transactions that occurred in the year prior to each study. In each year, the studies reviewed 150, 143, 106, 100 and 136 private company transactions, respectively. These transactions ranged in size from $17 million to $4.7 billion, across a broad range of industry sectors.

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[1] Note that within this article we use the terms ''seller'' and ''company'' in the context of a stock purchase transaction - - the ''seller'' would be the selling shareholder(s) making the representations and warranties in the M&A purchase agreement, and the ''company'' would be the company being acquired. In an asset purchase transaction, the ''seller'' would be the target company itself but for consistency we are using ''seller'' and ''company'' in a stock purchase setting.

This article examines trends in the use of ADR provisions in private company M&A transactions, as reflected in the past four ABA studies.[2]

ADR Provisions

ADR provisions in M&A purchase agreements tend to raise the following issues for negotiation between buyer and seller:

- Whether, as a threshold matter, the purchase agreement should include ADR in lieu of or prior to judicial recourse;
- Whether, of those agreements including an ADR provision, the ADR is to be by:
  - o Binding arbitration;
  - o Mediation; or
  - o Mediation first, followed by binding arbitration;
- Whether the arbitrator will be specified as the American Arbitration Association, Judicial Arbitration and Mediation Services (JAMS) or another named service provider; and
- How expenses associated with the ADR proceedings are to be allocated between buyer and seller.

These four sets of ADR-related issues are discussed in more detail below.

[2] This article looks at ADR provisions in private company M&A transactions as reflected in the past four ABA studies. This article does not address the provisions in other types of transactions or in public-to-public M&A transactions. The 2005 ABA study did not look at ADR provisions. Accordingly, this article reviews the relevant information in the 2013, 2011, 2009 and 2007 ABA studies.

Related Provisions

ADR provisions within an M&A agreement are related to at least three other provisions which may also show up in the agreement: (i) the ''exclusivity of remedies'' provision, which states that the indemnification structure and procedures in the purchase agreement are the sole remedy for claims (subject to limited exceptions such as fraud);[3] (ii) provisions allowing for specific performance to prevent breaches of covenants (such as non-competition covenants of the seller); and (iii) waivers of jury trials.

Earlier articles in this series looked at trends in exclusivity of remedies provisions and waivers of jury trials.[4]

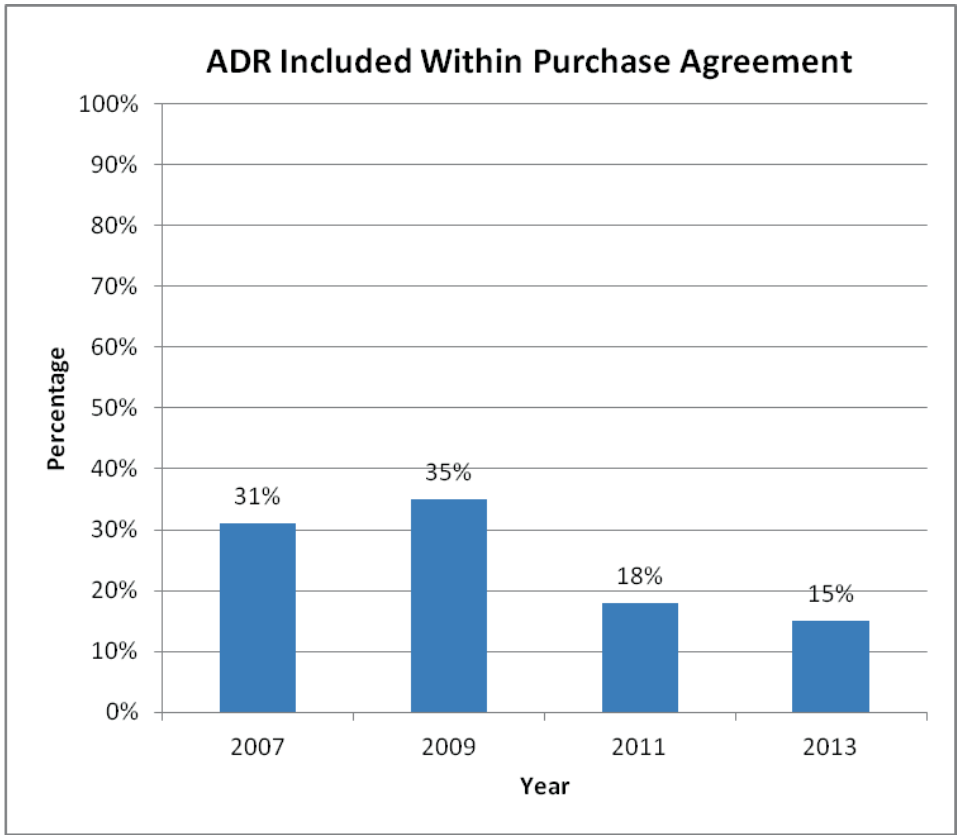
Trends in ADR Provisions

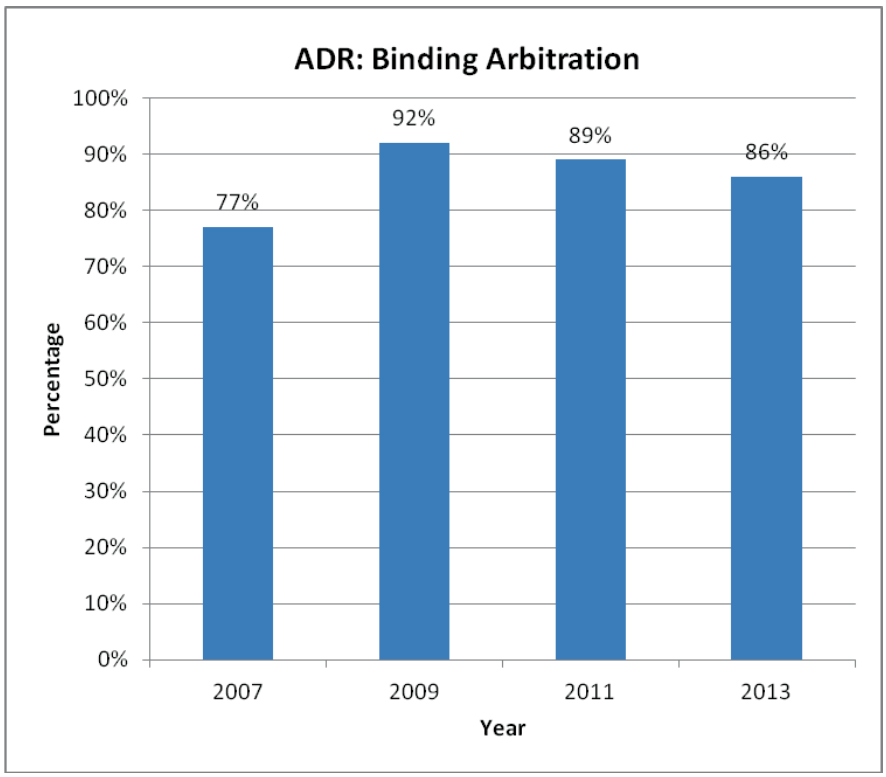
The charts below show the extent to which the four ADR-related concepts described above - - whether ADR provisions are included; what type of ADR is to be required; whether a specific arbitrator is to be identified; and how arbitration expenses are allocated - - are covered in private company M&A purchase agreements, based on the past four ABA studies.

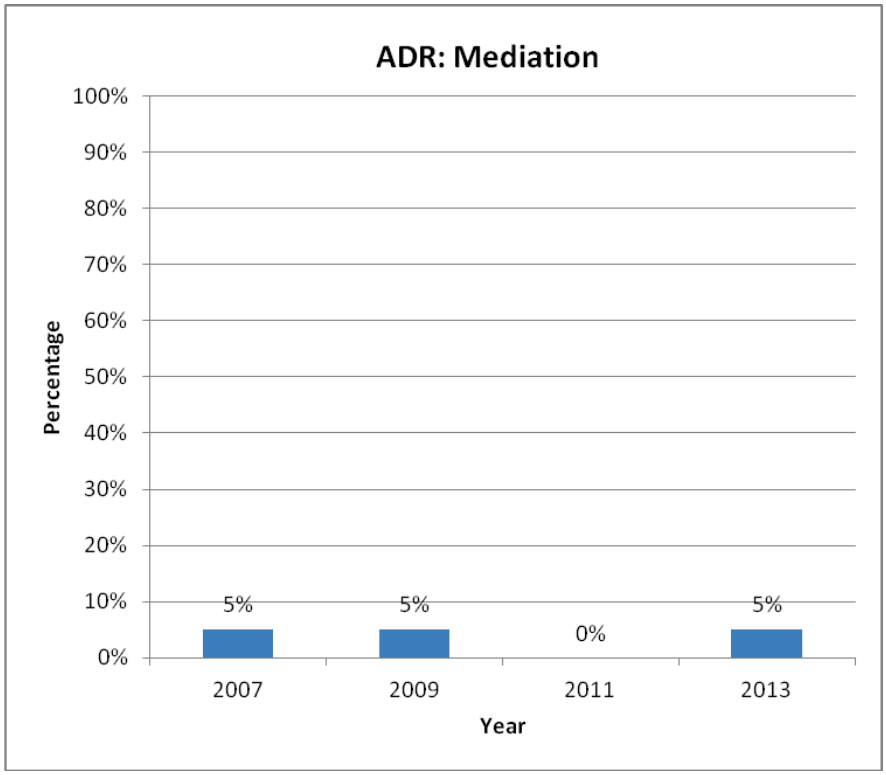
[3] An excellent recent article examined fraud exceptions to the exclusivity of remedies provision and related concepts. *See* West, *That Pesky Little Thing Called Fraud: An Examination of Buyer's Insistence Upon (and Sellers' Too Ready Acceptance of) Undefined ''Fraud Carve-Outs'' in Acquisition Agreements*, The Business Lawyer, Vol. 69, August 2014.

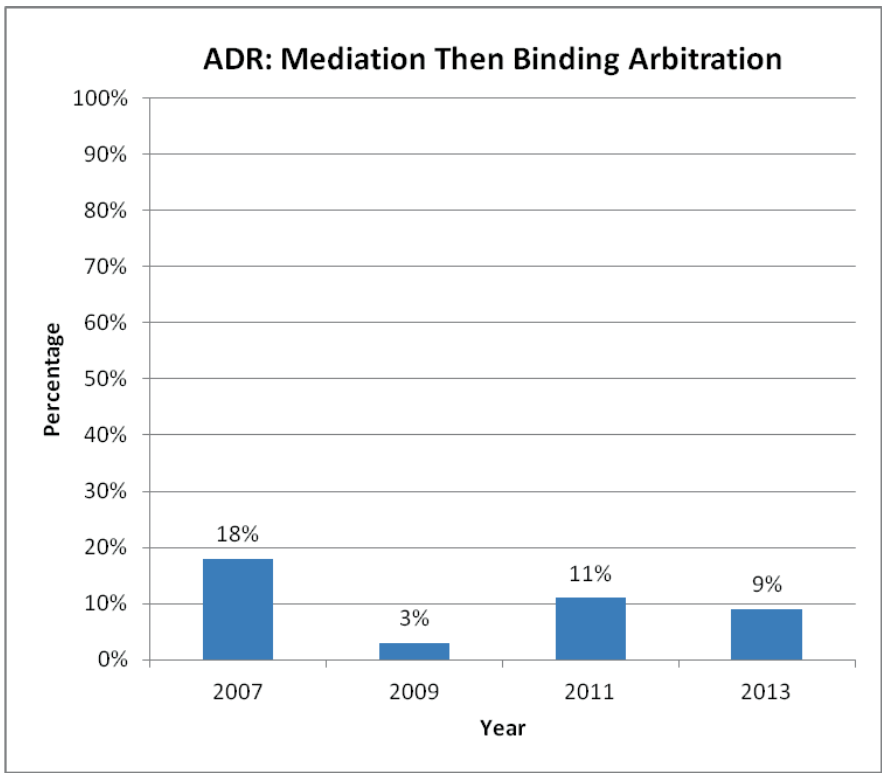
[4] *See* Avery and Perricone, *Trends in M&A Provisions: Indemnification as an Exclusive Remedy*, Bloomberg BNA Mergers & Acquisitions Law Report, Sept. 16, 2013, reprinted at http://www.goulstonstorrs.com/WhatsMarket; and Avery and Brody, *Trends in M&A Provisions: Waiver of Jury Trials*, Bloomberg BNA Mergers & Acquisitions Law Report, January 13, 2014, reprinted at http://www.goulstonstorrs.com/WhatsMarket.

  MALR ISSN 1098-4720

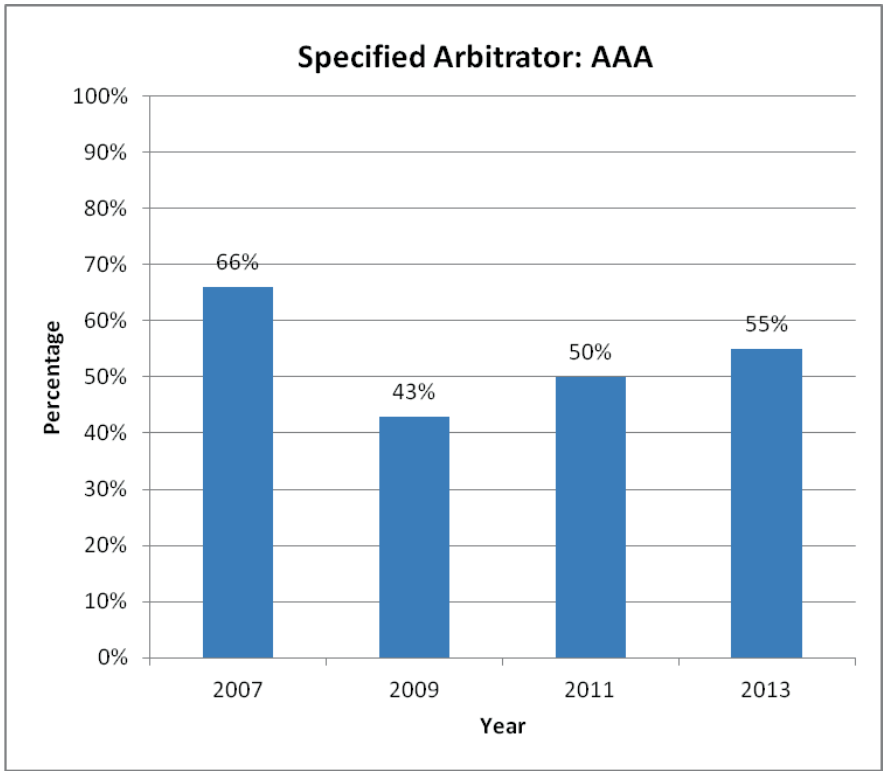

ADR Included Within Purchase Agreement
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
31%
35%
18%
15%
2007
2009
2011
2013
Year

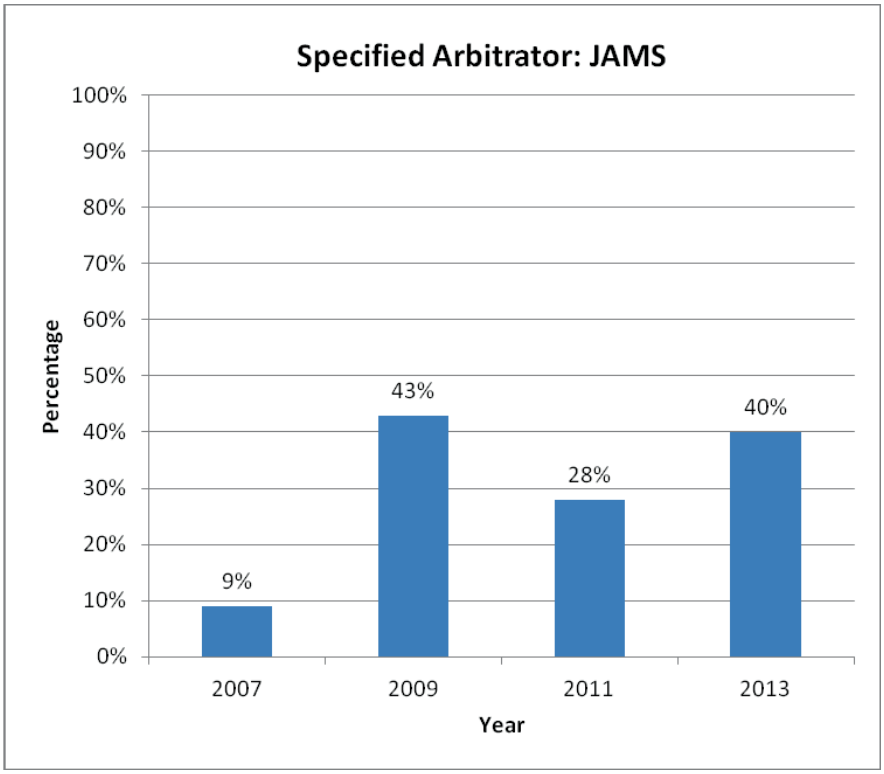

ADR: Binding Arbitration
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
77%
92%
89%
86%
2007
2009
2011
2013
Year

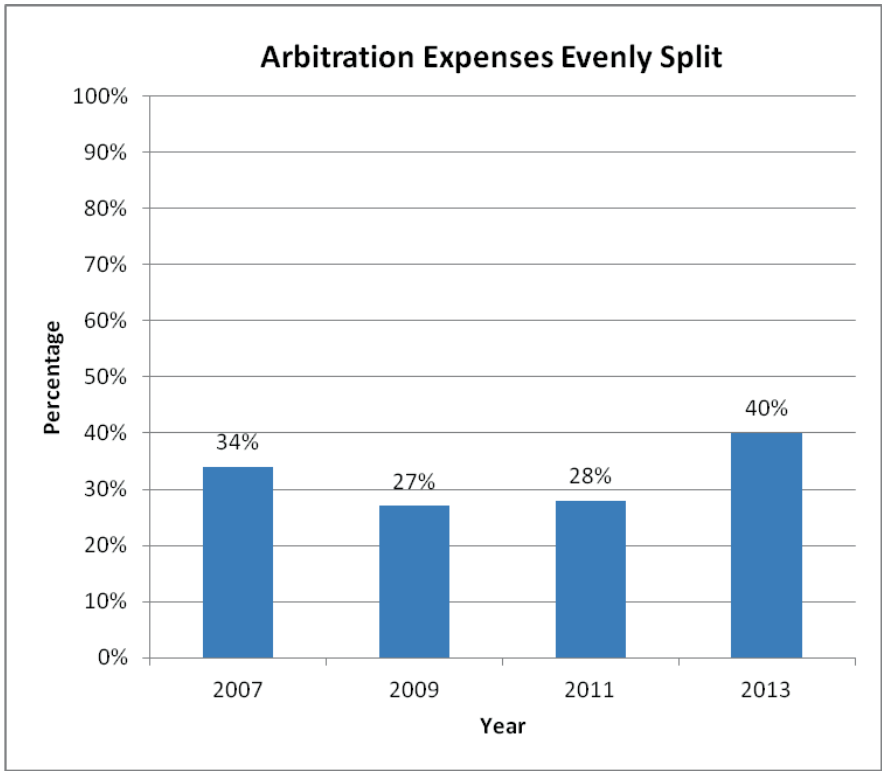


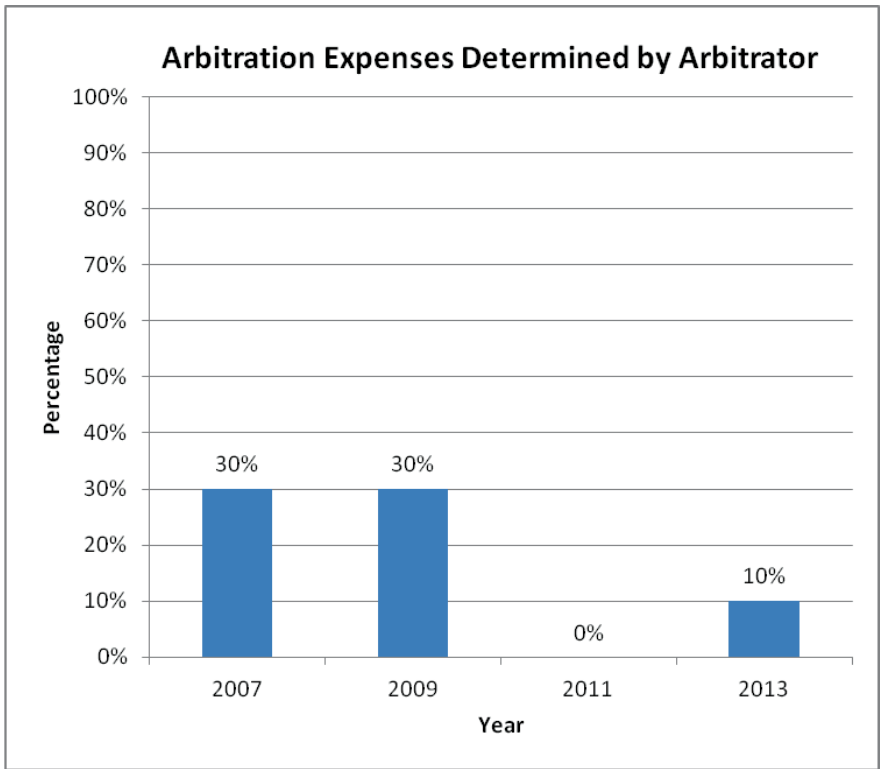


   ISSN 1098-4720

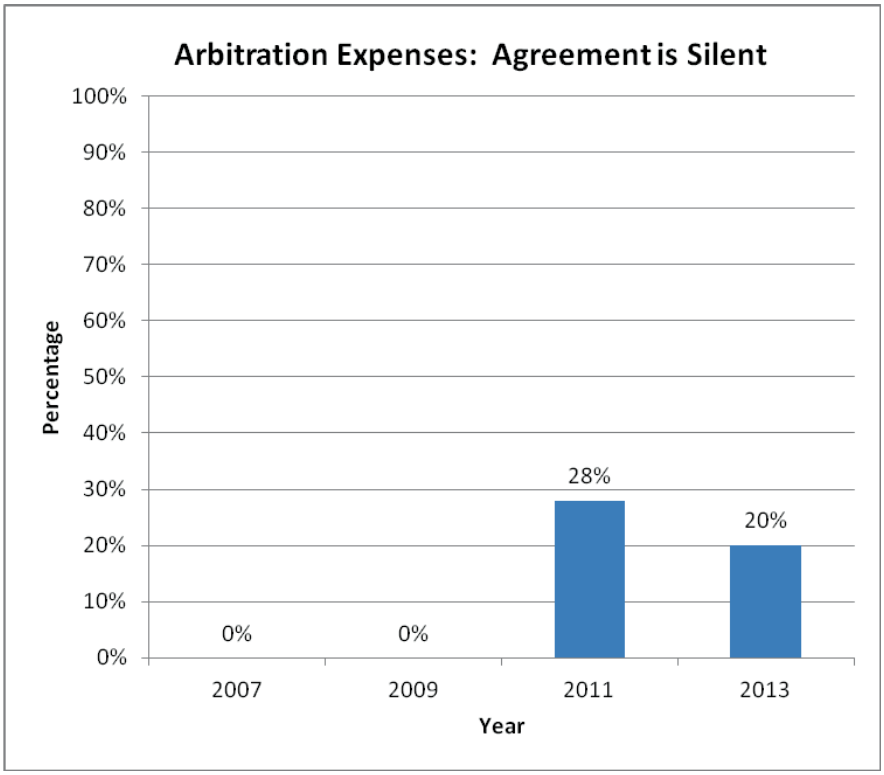

Specified Arbitrator: AAA
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
66%
43%
50%
55%
2007
2009
2011
2013
Year

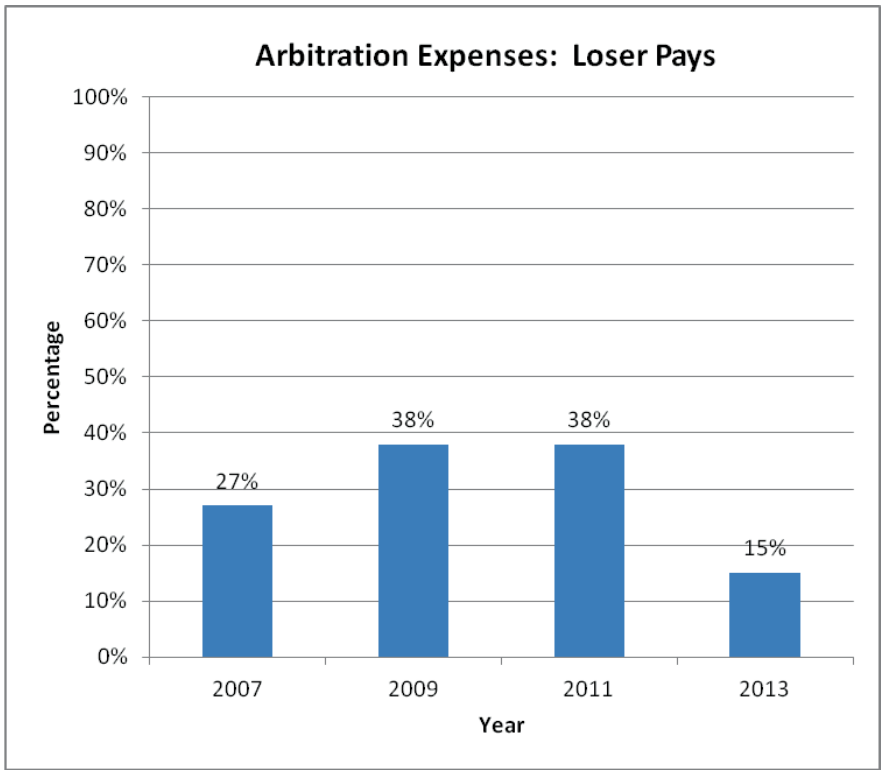

Specified Arbitrator: JAMS
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
9%
43%
28%
40%
2007
2009
2011
2013
Year

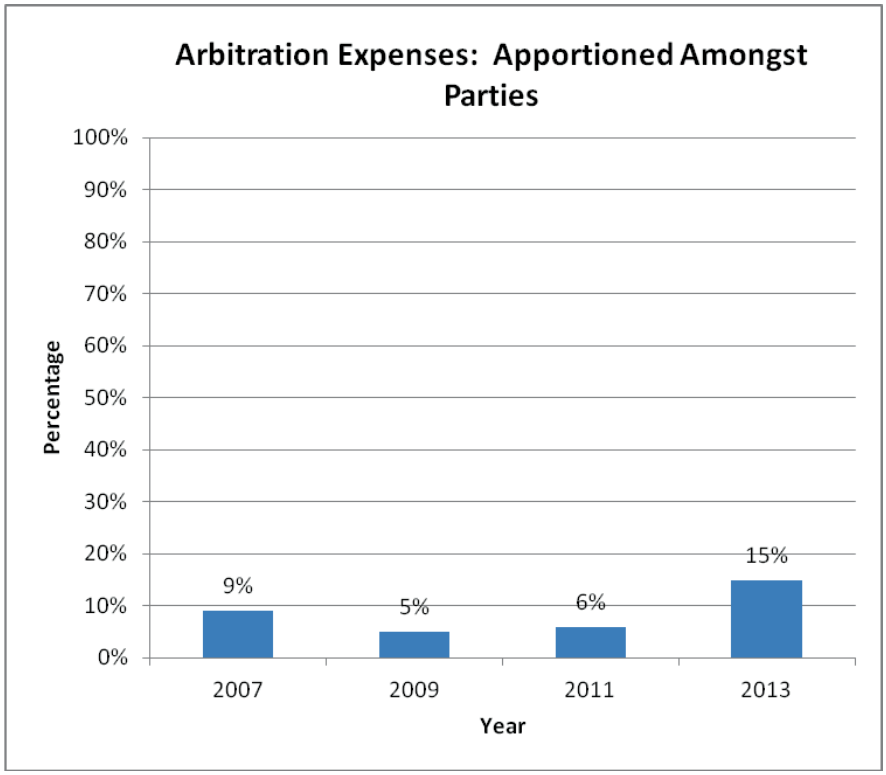




  MALR ISSN 1098-4720


Arbitration Expenses: Agreement is Silent
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
0%
0%
28%
20%
2007
2009
2011
2013
Year


Arbitration Expenses: Loser Pays
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage
27%
38%
38%
15%
2007
2009
2011
2013
Year



Conclusion

ADR provisions are becoming less prevalent in private company M&A transactions, as reflected in the ABA studies, from a high of 35% in the 2009 ABA study (reporting on transactions in 2008) to a low in the 2013 ABA study (reporting on transactions in 2012) of 15%. Of those M&A purchase agreements which include an ADR requirement, binding arbitration—as opposed to mediation or mediation followed by arbitration—is by far the method of choice (selected in more than ¾ of the ADR provisions). When an ADR provision names a specific arbitration body, the American Arbitration Association is the most frequently named (in a majority of cases). Allocation of arbitration expenses continues to be reflected in a variety of ways—whether set by the arbitrator, as a ''loser pays'' system, or allocated amongst the parties.

   ISSN 1098-4720