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Professional Perspective

Alternative Dispute Resolution Provisions

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Market Trends: What You Need to Know

As shown in the American Bar Association's Private Target Mergers and Acquisitions Deal Point Studies:

- Overall, alternative dispute resolution provisions are becoming less common in private company merger and acquisition (M&A) transactions. Inclusion of ADR provisions has declined over the past several years from 35% in the 2009 ABA study to 14% in the 2019 study.
- Of those purchase agreements with an ADR requirement, binding arbitration is still the method of choice (included in 67% of the ADR provisions in the 2019 study). However, the degree of preference has been slowly declining since 2009 when the use of binding arbitration peaked at 92%.
- When an ADR provision names a specific arbitration body, the American Arbitration Association (AAA) or Judicial Arbitration and Mediation Services (JAMS) is the most frequently named.
- Finally, the allocation of arbitration expenses continues to fluctuate over time—whether evenly split, paid by the loser, or allocated amongst the parties.

Introduction

In M&A purchase agreements, the parties may stipulate certain non-judicial means for dealing with claims under the agreement (e.g., arbitration or mediation). These ADR provisions will govern how disputes between the parties are to be handled.

Negotiating Points for ADR Provisions

ADR provisions in M&A purchase agreements tend to raise the following negotiation issues:

- Whether, as a threshold matter, the purchase agreement should include ADR provisions in lieu of, or prior to, judicial recourse
- Which form of ADR the parties are willing to agree:
- Binding arbitration
- Mediation
- Mediation first, followed by binding arbitration
- Whether the arbitrator will be specified as the AAA, JAMS, or another named service provider
- How expenses associated with the ADR proceedings are to be allocated between buyer and seller

Related Provisions

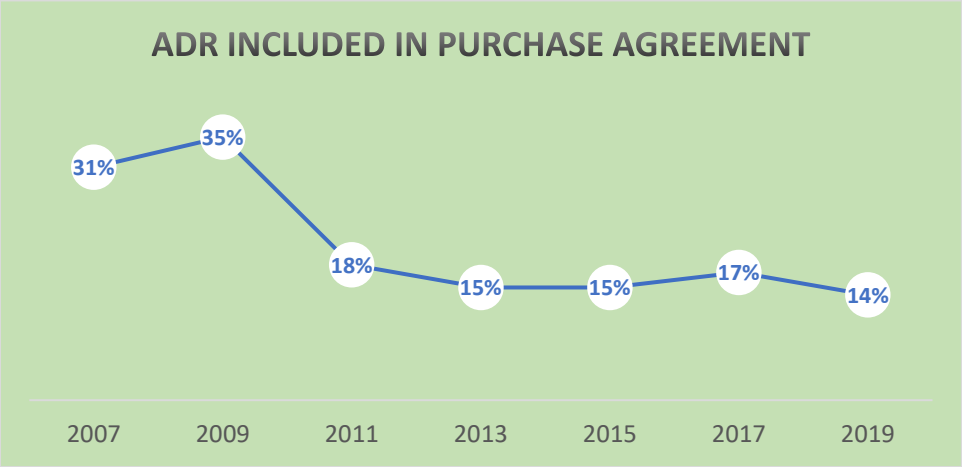
When drafting and negotiating ADR provisions, practitioners must pay careful attention to how the ADR provisions will interact with other provisions in the purchase agreement. This is important because ADR provisions are related to at least three other provisions in an M&A agreement:

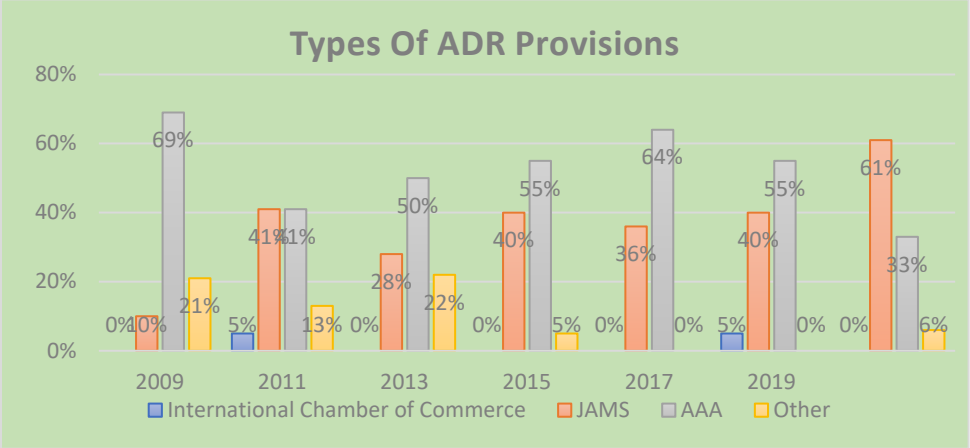
- The "exclusivity of remedies" provision, which states that the indemnification structure and procedures in the purchase agreement are the sole remedy for claims (subject to limited exceptions such as fraud)
- Provisions allowing for specific performance to prevent breaches of covenants (such as non-competition covenants of the seller)
- Waiver of jury trial provisions

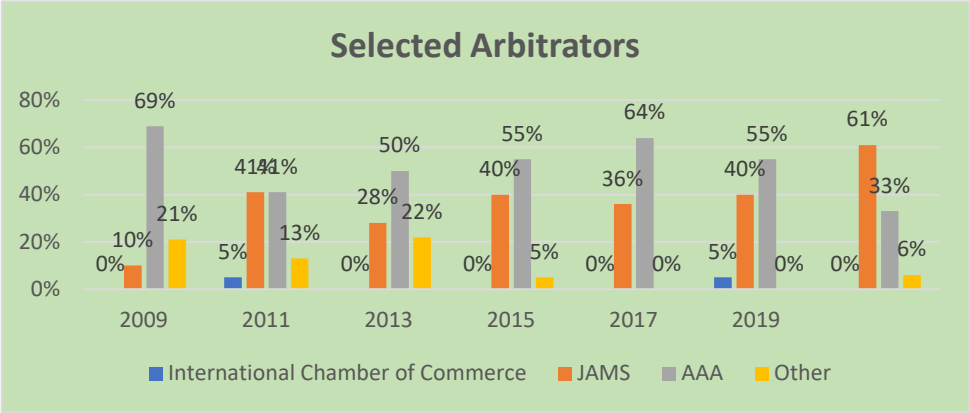
Trends in ADR Provisions

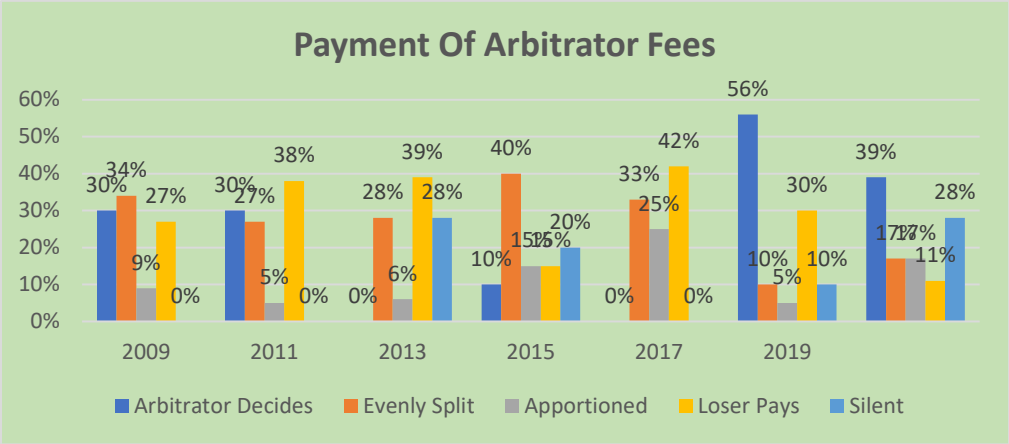
Every other year since 2005 the ABA has released its Private Target Mergers and Acquisitions Deal Point Studies. The ABA studies examine purchase agreements of publicly available transactions involving private companies. These transactions range in size but are generally considered as within the "middle market" for M&A transactions; the median transaction value within the 2019 study was $145 million.

The analysis of data from the most recent seven ABA studies illustrates the extent to which the four ADR-related negotiating concepts described above—whether ADR provisions are included; the form of ADR agreed to; whether a specific arbitrator is identified; and how arbitration expenses are allocated—are covered in private company M&A purchase agreements.









Conclusion

Overall, ADR provisions are becoming less common in private company M&A transactions. As reflected in the ABA studies, their use has declined over the past several years from a high of 35% in the 2009 ABA study to a low of 14% in the 2019 study. Of those purchase agreements with an ADR requirement, binding arbitration is still the method of choice (included in 67% of the ADR provisions in the 2019 study). However, the degree of preference has been slowly declining since 2009 when the use of binding arbitration peaked at 92%. When an ADR provision names a specific arbitration body, the AAA or JAMs is the most frequently named. Finally, the allocation of arbitration expenses continues to fluctuate over time—whether evenly split, paid by the loser, or allocated amongst the parties.