

Akerman's Private Equity Boot Camp Series: Distressed Company Transactions

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An aerial photograph of a winding asphalt road with a yellow center line, cutting through a dense, lush green forest. The road curves from the bottom left towards the top right of the image. The trees are thick and vibrant green, suggesting a healthy, mature forest.
akerman

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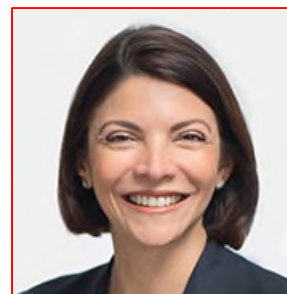


Table of Contents

1. Overview/Sale Process
2. Assumption of Contracts/Bidding Procedures/Stalking Horses
3. Nuts and Bolts of Section 363 Asset Purchase Agreement (APA)

Overview/Sale Process



Distressed Transactions Outside of a Proceeding – *asset values are there but...*

- Seller's Primary Concerns
 - Fair Value
 - Cost of FV Opinion / Benefit?
 - Board Fiduciary Duties
- Buyer's Primary Concerns
 - Fraudulent Transfer Avoidance (4 years)
 - Value of Solvency Opinion
 - Other theories (alter ego, continuing business ent., etc.)

Bankruptcy Overview

- Chapter 11 v. Chapter 7
- Solvency Test?
 - Some economic distress
 - Valid business reason / justification
- Debtor in Possession:
 - Remain in Possession of Assets / Company
 - Operate in Ordinary Course
- Stages of a Chapter 11: Stabilize, Restructure, Exit

Bankruptcy Sales

- 11 U.S.C. § 363(b):
- Sales Outside Ordinary Course of Business Requires Bankruptcy Court Approval
- Must Obtain Highest and Best Price for Assets
- Can Be Some or All of Debtor's Assets
 - Including Include Going Concern Sale or Equity Purchase

Sale Process Overview

- Process Tailored to Particular Sale
 - Sometimes Very Informal, but Always Subject to Higher Offers
- Normally 30 to 90 Days (Could Be Shorter or Longer)
- Initial Process Similar to Traditional Sales:
 - Investment Banker / Broker, Data Room, Teasers, NDAs, CIM
- Auction: In / Out Of Courtroom
 - Selection of Highest & Best Bid, Other Considerations
- Court Approval At (*quick*) Sale Hearing
 - Potential Challenge by Bidders and Parties In Interest

Unique Advantages and Other Terms

- No Subsequent Fraudulent Transfer Risk.
 - Court Order Finds Fair Value for Assets
- Similar Protection for Seller
 - No Need for Fairness / Value Opinion for Board
 - Court will make that finding
- Assets Sold “Free And Clear”
 - Assets With “Hair” On Them Cleansed / Limited Exceptions
- Good Faith Finding Prevents Reversal On Appeal
 - (11 U.S.C. § 363(m))

Unique Advantages and Other Terms

- No Bulk Transfer Liability
- Restrictive Governance Approval Not Required
 - i.e. majority shareholder or other
 - Board + creditors + court
- Less Due Diligence of *Liabilities* Required
 - No Liabilities Assumed Unless Specifically Agreed To
 - Court protection from successor liability

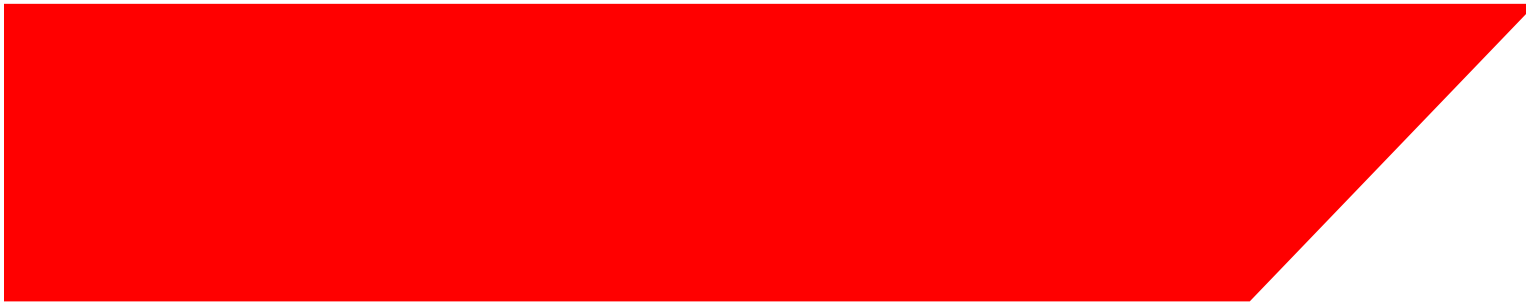
Certain Disadvantages

- Lender Credit Bid Rights (*usually*) Preserved
- Process Not Without Risk
 - e.g., Creditors' Objections, Unpredictability, Other Bidders
- Transparency & Limited Confidentiality
 - Bankruptcy Courts require notice to parties
 - Media Exposure
 - Discovery
- Court Approval Not Guaranteed

Certain Disadvantages (cont'd)

- Transaction Costs
 - Chapter 11 is Expensive
- Short Timeframe to Conduct Due Diligence
 - Distressed debtors' financials, are they accurate?

Assumption of Contracts/Bidding Procedures/Stalking Horses



Assumption / Assignment of Executory Contracts

- Purchaser may choose which contracts to have assigned to it (assume & assign)
- Assumption / Assignment Standards
 - Contract assumed / assigned in its entirety, no severance of contract provisions
 - Purchaser / Assignee must cure all defaults (monetary and non-monetary)
 - Purchaser / Assignee must provide adequate assurance of future performance (monetary and other requirements of contract)
 - Cure amounts noticed to contract counter-parties. If no objections, then cure deemed at amount noticed. If objections, then court determination.

Assumption / Assignment of Executory Contracts (cont'd)

- ◉ Anti-Assignability Provisions largely irrelevant:

Exceptions:

- ◉ Personal Services Contracts
- ◉ Certain IP Licenses
- ◉ Government Contracts

Bidding Procedures

- Bid and Closing Deadlines
- Bidder Deposit of a Percentage of the Purchase Price
- Bidder Must Demonstrate That It Has Financial Ability to Complete the Transaction / No Financing Contingencies
- Minimum Overbid Amount Plus Break-up Fees (2-4%) and Expense Reimbursement Fee
- Markup of APA Not Materially More Burdensome than the Stalking Horse APA
- Can Be Penalized In Bidding Process

Stalking Horses

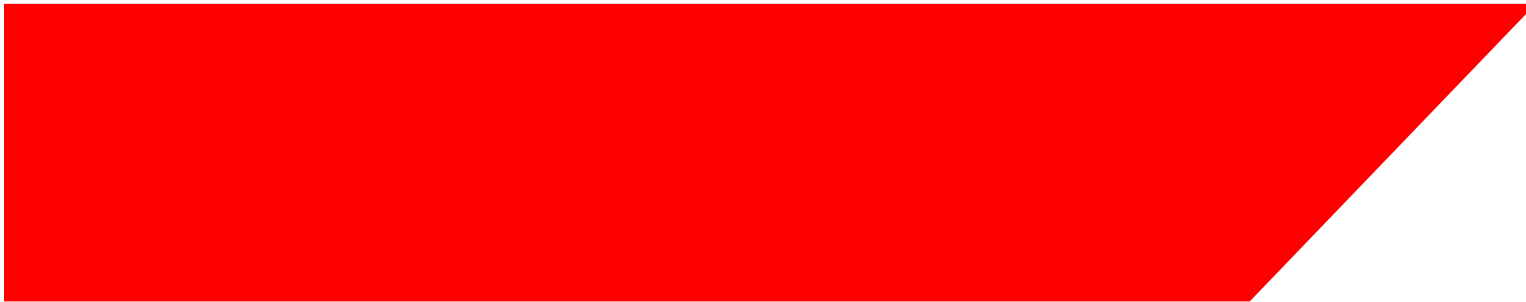
- Advantages
 - More Time and Access to Conduct Due Diligence
 - Head Start on Seeking Regulatory Approvals and R&W Insurance
 - Sets the Threshold Price, Contract Terms and Transaction Structure
 - Competing Creditors Must Bid Against Your APA
 - Receives Certain Bid Protections, Break Up Fees, Expense Reimbursement
 - Negotiates the Bidding Procedures and Process

Stalking Horses (cont'd)

- Creates Strategic Relationships with Debtor and Other Significant Players
- Can Provide Financing to Debtor for Additional Control

- Disadvantages
 - Time and Expense
 - Risk of Subsequent Bids, Being Overbid
 - Very Difficult to Exercise Termination Provisions, Creditors Could / Will Challenge In Court

Nuts and Bolts of Section 363 Asset Purchase Agreement (APA)



Nuts and Bolts of Section 363 Asset Purchase Agreement (APA)

- Acquisition of Assets and Assumption of Liabilities
- Purchase Price
- Representations and Warranties
- Closing Conditions
- Covenants
- Termination
- Jurisdiction

Nuts and Bolts of Section 363 APA (cont'd)

- Acquisition of Assets and Assumption of Liabilities
- Purchase Price
 - Deposit
 - Cash and/or Credit Bid; Cure Amount; Other Consideration
 - Purchase Price Allocations (Buyer vs Seller Interests)
 - Holdbacks and Escrows Typically More Difficult to Negotiate as Creditors want Certainty on Net Purchase Price
 - Earn-Outs and Other Contingent Payments Not Likely
- Representations and Warranties
 - No Survival of Representations and Warranties Post-Closing
 - R&W Insurance is Available:
 - Mitigate Losses not Extinguished by “Free and Clear” Order
 - Typical RWI Requirements Apply: Fulsome Business and Legal Diligence, etc.
 - Availability of other Insurance in the context of distressed acquisitions

Nuts and Bolts of Section 363 APA (cont'd)

- Closing Conditions
 - Generally No Stockholder or Contractual Consents Condition
 - Exceptions
 - Personal Service Contracts
 - Governmental Contracts
 - Intellectual Property
 - Regulatory Consents Still Applicable
 - Hart-Scott-Rodino Waiting Period 15 Days In Bankruptcy Context (As Opposed To 30 Days)
 - Bankruptcy Process Conditions
 - Court Approval
 - Curing of Defaults on Assumed Executory Contracts and Leases
 - Seller's DIP Financing Not Being Terminated or Adversely Modified

Nuts and Bolts of Section 363 APA (cont'd)

- Covenants
 - Conduct Of Business Prior to Closing Typically Contains Fewer Obligations and Restrictions
 - Debtors must operate in ordinary course anyway
 - Bankruptcy Process Covenants
 - No Exclusivity; Competing Transaction
 - Provisions Regarding the Assignment, Assumption and Rejection of Executory Contracts and Leases
 - Cooperation to Obtain Sale Order and, if Stalking Horse, the Bidding Procedures
 - Seller to Provide Notices to Parties In Interest (Creditors)
 - Court Supervision

Nuts and Bolts of Section 363 APA (cont'd)

- Termination
 - Unique to Section 363 (besides standard provisions)
 - Buyer's Right to Terminate if Court Order Not Approved
 - Seller's Right to Terminate if Alternative Transaction
 - Effect of Termination (Break-Up Fee/Expense/Deposit)
 - If Seller Breaches or Closes Alternative Transaction, Stalking Horse Entitled to Break-Up Fee and Expense Reimbursement
 - If Stalking Horse Not In Breach and Transaction Does Not Close, Stalking Horse Entitled to Expense Reimbursement
 - If a Buyer is in Breach, Deposit is Forfeited (Typically as Sole Recourse)
- Choice of Law/Venue
 - Customary Choice of Law
 - Venue of the Bankruptcy Proceeding for Dispute Resolution

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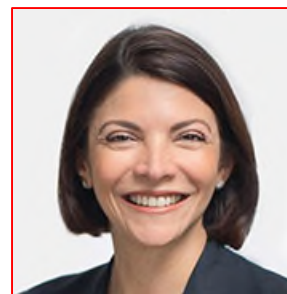


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