

M&A IN UNCERTAIN TIMES

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Uncertainty can result in a deal being delayed, altered or cancelled. Gowling WLG's M&A team is hosting a series of webinars designed to explore, analyze and help clients and friends of our firm navigate the impacts uncertainty can have on transactions.

In this first webinar of our series, our panel of experienced practitioners will provide valuable insights from both the buyer's and seller's perspectives. We will address how the disruptive effect of COVID-19 is impacting M&A transactions in Canada. We will share insights and offer practical steps parties can take now to address these challenges.

Topics covered:

- The dynamics impacting transactions in their infancy
- Considerations for deals that have been signed but not yet closed
- The potential impact on deals already closed.

Transcript

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M&A IN UNCERTAIN TIMES WEBINAR

Kathleen: This is the first installment of Gowling WLG's M&A webinar series. M&A in uncertain times. Today our panel will discuss how the disruptive effect of COVID-19 is impacting M&A transactions in Canada at different points in the deal life cycle. An article covering some of these items that we will discuss today is also posted on our website and we've already set up two further webinars scheduled for this series which I'll highlight at the end of today's program. But before we start there's a couple of housekeeping points we'd like to cover. First of all, to view this presentation and all the speakers please click on the speaker view in the upper right hand corner of your screen. For questions throughout the session please use the Q&A button at the bottom of your screen to ask a question. We'll try our best to answer some of your questions, at the end of session, and you should feel free to reach out to anybody on the team, if you have questions afterwards as well. The presentations being recorded and it will be posted on our website in a couple of days. This program counts for 1 hour of CPD, for example, in the case of Ontario, 1 hour of substantive credits towards CPD requirements of the law society of Ontario. Also, there's a legal disclaimer. Today's session will be a high level overview. For specific advice please contact your legal counsel, often, and as you know the situation is extremely fluid and changing daily. And now to our panel. Participating in today's session from West to East are Cyndi Laval, Ian Palm, Faran Umar-Khitab, Tiffany Bianchi, and I'm Kathleen Ritchie and I'll be moderating the discussion today. Turning to our agenda. Our plan is to cover deals at various stages in the deal life cycle. First, those that were at the LOI stage, or letter of intent stage, when COVID-19 really started to impact transactions in Canada, back in early March. Second, those that are at interim stage, where the definitive acquisition agreement was signed up but the deal hasn't closed yet. And third, those deals that have closed but were there might be a post-closing impact from COVID-19. I'm going to ask our panel members to provide their insights on a number of topics, both from the buyers and the sellers perspectives and to offer some practical steps that parties can take now to address these challenges arising as a result of COVID-19. So let's turn to the LOI stage. Let's talk about some transactions that were in the infancy at the time that this all started. Our first topic is negotiating an exclusivity period for due diligence and for negotiating a definitive acquisition agreement. Let's turn to Cyndi. What

are your thoughts from the perspective of the seller of the target?

Cyndi: Sure. Thanks, Kathleen, and good morning everybody. Good morning because I'm in the West. Parties in the letter of intent stage will likely now be considering how disruptions cause by COVID-19 affect their previously negotiated initial exclusivity period for completion of diligence and finalization of definitive acquisition agreements. Sellers will generally want to push buyers to stick with the exclusivity period they negotiated in the LOI pre-COVID-19, and will want to resist requests from buyers to renegotiate this period to avoid being tied up in limbo for a period of many months, rather than a few weeks as would be common in normal circumstances. As counsel to a seller I would recommend carefully assessing whether you should agree to extend an exclusivity period deadline in the event of delays beyond the seller's control . For example, if the buyer is unable to complete confirmatory due diligence. Sellers will want to push buyers to move as quickly as possible, to sign up definitive binding agreements to remove the sellers deal risk. However, sellers will need to tread very carefully in this area to ensure that failure to provide additional time does not inadvertently allow a buyer to walk from the deal. For example, if a buyer has a due diligence out, failure to extend an exclusivity period to allow a buyer to complete it's due diligence, may force the buyer to terminate the transaction in reliance on the due diligence condition. Tiffany, can you provide some colour on the perspective of the buyer?

Tiffany: Yes. Thanks, Cyndi and hi everyone. I think as a result of the pandemic buyers are recognizing that the economic landscape and overall valuation of the target can look entirely different within a very short period of time. Certainly from what they had originally intended to purchase. So buyers will want to negotiate an extension to the exclusivity period by a few weeks or really as long as possible to allow for potentially significant delays in completing their due diligence, which we'll talk about in just a moment, and further negotiating the purchase agreement. All stemming from the social and economic impacts of COVID-19.

Kathleen: Thanks, Tiffany. Now moving on to due diligence issues, obviously it's not business as usual, and while much of the due diligence could be done and is already done electronically through data rooms, Tiffany, can you comment on how COVID-19 is impacting due diligence by buyers today?

Tiffany: Sure. Absolutely, Kathleen. Although restrictions on non-essential business activities will undoubtedly result in unexpected delays during the due diligence phase of the transaction, as you mentioned, Kathleen, the expansion of virtual data room and video conference usage will at least offer some interim solutions to the buyer. That said, either

on the ground, or in person site visits for physical inspections and physical needs or assets, for the time being will not be able to take place even continuing social distancing measures. Also the buyers need to recognize that due diligence searches from government agencies may take longer to receive, or may not be received at all, due to office closures or staffing shortages. What we're going to see is that by our standard legal diligence checklist will likely be supplemented by a COVID-19 specific set of questions. The questions, of course, should be tailored to the particular target and it's industry, however, buyers will likely shift focus to certain areas in conducting their due diligence to identify and understand the potential impact of COVID-19 on the target business. We may see a more concentrated focus on the target's personnel and it's ability to function remotely, supply chains and possible alternative suppliers, unresolved implications on inventory operations and material contracts to identify provisions that may be adversely affected by COVID-19, including any force majeure clauses. I think that despite the buyer moving forward with it's due diligence exercise during this time, as a result of potential incompleteness of buyer's due diligence investigations, we're also likely to see buyers requesting in the acquisition agreement broader representations and warranties with fewer qualifiers from sellers, specific indemnification obligations and likely the inclusion of the completion of a confirmatory due diligence, as a condition precedent to closing. Faran, will now speak to due diligence from a seller's perspective and I suspect he'll have a very different take on the scope of buyer's diligence.

Faran: Alright, thanks, Tiffany. I agree there's a lot of difficulties these days for seller's or targets in terms of providing buyers with the right level of due diligence, to a degree the average of online data rooms for the last few years will make the process easier because we're all ready used to starting due diligence, getting access to the data room. Some of the items that will make life a little difficult for vendors in this atmosphere is certain contracts made will only be available in hard copy form, maybe at an office where there's nobody physically available to go to the filing cabinets, pull the contracts and scan them to a data room. In several types of businesses they're contracts that are very sensitive or certain types of ... contracts that may be labeled as secret or top secret, that can only be provided in hard copy form, for those types ... certainly will not be occurring at this time. The other item that seller's need to be careful of is we typically we would give buyer's counsel access to a data room and give them quick access on the assumption that they're printing these documents in their secure work premises where people can't get access to those papers, whereas people are now working remotely from all over the place, so you really have to be careful about where people may be printing your sensitive documents. We're hearing a lot of people say facility tours and inspection of assets may be more difficult given the current atmosphere. Some sellers are providing video tours where

buyers can look through somebody who's walking through the premises on video. Again, we will question sellers to be very careful of who's got access to it, what type of materials might actually be shown on the video because you don't want people inadvertently getting access to seeing what's going on your in facility, especially if you've got a skeleton crew working there.

Kathleen: Thanks, Faran. So, our next topic is financing. From the perspective of the buyer, Ian, what challenges are you seeing?

Ian: Well, thanks a lot Kathleen, and great to be with you folks today and thanks for taking the time to join us. So from a financing perspective LOI's that were struck before the pandemic arose have changed. Financing challenges have presented themselves in such a manner that parties need to reconsider a bunch of circumstances. So, the assumptions that were made at the time that the LOI was struck were probably a lot different. So we're seeing parties reconsider a bunch of things around how they intend to actually fund the acquisition. For strategic buyers with a strong balance sheet, the challenge is probably less significant. Obviously a buyer in that circumstance will still be looking for ways to conserve cash, at the present time, and in light of the pandemic they've probably got other things that are more important. But perhaps they've already spent a significant amount of time on an acquisition and they want to continue with the acquisition. In those circumstances we're seeing people look to a potentially change the nature with which the purchase price is paid, perhaps, negotiate with the seller to potentially pay the purchase price over a period of time to conserve cash in the near term. Perhaps test evaluation expectations that they had at the time to consider whether or not it's going to still meet the internal ROI that they have for their investment and look, generally speaking, to try and conserve cash but still proceed with the transaction. And at the same time try to keep the faith of the seller who is probably looking very carefully at how the transaction is going to be financed. The more challenging group of buyers, to deal with in this circumstance, are really the ones who are financial buyers who don't have internal cash resources to do the whole acquisition themselves. In other words ones that are looking to either have co-investors come on board or finance the transaction with a material amount of debt. We are seeing that while banks are open for business and are interactive and very engaged with parties, they are really focused on existing portfolios and they're focused on closing existing transactions as a priority, at least in our experience, and while new investment opportunities are certainly there, we're finding that it's taking more time for them to consider it. And quite rightly so given the nature of the circumstances. From a buyers perspective, a buyer that's looking to still finance the transaction, perhaps they can look to do a bridge financing of some sort, or perhaps do a

full equity acquisition at the time and then look to refinance afterwards when the markets settle down. Similarly I think you need to look at, from the buyer's perspective, if you're a private equity player and you've got a bunch of LP's that are perhaps a little bit nervous about the impact of the market on your existing portfolio, you're also looking at the impact of whether drawing down capital from your LP's for a new acquisition is something that should be the focus, or whether you should be focusing on your existing portfolio for the time being and making sure that they're fully taken care of. Or, frankly, ones that are challenged by the pandemic, you'll probably capitalize those groups. I think it is consistent with what Tiffany and Cyndi had said, we're finding it's taking more time, and so from a financing perspective you need to be engaged with your seller to make sure that they understand the circumstances and what's required to meet the financing requirements and anticipate how you're going to address them.

Faran: Thanks, Ian. From the seller's perspective I'd say many sellers adamantly say there should be no financing conditions to a deal and sometimes the LOI may say that or may be silent on that but the reality of any seller who's sitting on a non-binding LOI without a binding definitive agreement, whether you've got a financing condition or not, you need to realize the reality of the world we're living in now and work with your buyer recognizing that there may be certain impediments, at this day and age, in terms of the timing for the buyer to be able to get their financing in place.

And given the difficulties the buyer's may have, we would not be surprised if we see a lot more vendor take back notes being issued as either a bridge financing, or as part of the overall financing. To get deals done vendors need to realize that if they're serious about getting a deal done in certain circumstances, they may have to take on the financing risk to ensure that their deal gets done. If that's the case, at the LOI stage, when you're having that conversation you should make sure that you are engaged with whoever the senior lender is going to be to make sure that your vendor take back security, while it is going to be subordinated, the senior lender mirrors the events of ... so the reporting requirements, etcetera, so that your kept up to date on whatever the senior lender ... on.

Ian: I think this is a good opportunity for smart parties to be creative about this stuff, as Faran's described, and if you've got a seller and buyer that are prepared to collaborate you can find ways to either do VTB's, or decide that you're going to buy half the company today and decide when this pandemic's over, perhaps buy the second half later or something of that nature.

Faran: That's absolutely right, Ian. Especially for circumstances where you have some shareholder staying on, involved in the business side, keeping the minority stake or where you have management, you may want to see if management wants to roll their equity over

and see what the best manner is for the buyer and seller to get a deal up.

Kathleen: That's great guys, thanks. So why don't we turn to the next stage of transactions. Let's talk about deals that have been signed up but have not yet been closed. Our first topic is material adverse change provisions in acquisition agreements. This topic actually hit the press mid-March. It was addressed by company that was in the middle of a very large transaction and the question came up as to whether their MAC applied in the circumstances. Cyndi, what are your thoughts from the perspective of the seller, the target?

Cyndi: Sure. So, first, just let me explain for the audience what a MAC clause is. So an acquisition agreement will typically include what's called material adverse change or a material adverse effect. A MAC definition, so a typical MAC clause in an acquisition agreement, in an M&A transaction, is defined as any change or effect that individually, or in the aggregate, is material adverse to the business operations, assets, condition of the target's business, or that could delay or impair the ability of a party to consummate the transaction. So MAC clauses really serve two purposes. Typically they will allow a buyer to walk away from a transaction where a material adverse change in the seller's business has occurred between signing of the acquisition agreement in closing and they also act as a qualifier to certain seller reps, warranties, which raises the standard which the buyer must prove to claim such rep and warranty was breached. But MAC clauses also generally are qualified by exceptions, exclusions that limit the application of the clause and it's negotiation of the definition and these exceptions result in an allocation of risk between the buyer and the seller. So typically a buyer's expected to accept broader industry wide risks associated with the acquisition while a seller accepts responsibility for business specific works unique to the target business and unknown to the buyer. So buyers and sellers who have already signed an acquisition agreement, pre-COVID, that have not yet closed their transaction will be looking very closely at their MAC provisions, as Kathleen has noted, it's already been in the news. There's been quite a bit of commentary on it. Whether or not the impact of COVID-19 can constitute a MAC will depend largely on the definition in the acquisition agreement and the facts surrounding the target company. Even if the impact on seller of COVID-19 is materially adverse, as previously mentioned, most MAC definitions will include carve outs for widespread events such as general economic downturn, or even in some cases a pandemic, such that a MAC would only arise if the targets distance was disproportionately impacted by the economic downturn or the pandemic. So carve outs from that clause which will benefit the seller in the current environment include changes in applicable laws, industrial wide fluctuations or risks affecting the sellers industry, generally, changes in general economic or political condition,

acts of God and that's provided COVID does not have a disproportionate effect on the seller or the business as compared to similar businesses. What constitutes a disproportionate effect in the context of the COVID outbreak will be determined on a case by case basis once the full effects of the pandemic unravel. So, Ian, what would be of interest to a buyer in connection with a MAC provision?

Ian: Cyndi, thanks for outlining that and that's a very succinct description of something that's relatively complex and a purchase agreement is documented over many pages in a purchase agreement. It's something that's often hotly contested. I think from a buyer's perspective you've highlighted a few things that are relevant but I'll raise a couple. One is whether or not you can determine that the circumstances that have arisen constitute what would be a MAC for the purposes of that transaction in that business. I think that people need to remember that the courts, to the extent that they've addressed them, and it's pretty rare that they address them in Canada, but in the US they've addressed them a little more often, but the courts set a very high standard with regards to meeting a MAC. It's pretty difficult to get to the standard which would constitute a material adverse change. A lay person coming to the table saying, "Hey, look. This business has had a downturn of 20% or something like that, in the context of its revenue over the quarter because of this pandemic, this has got to be a MAC." While you may have that initial reaction you need to step back and say, "Okay, what does the document say? Do one of the carve outs apply?", as Cyndi alluded to. That's point number one from the purchaser's perspective you need to keep in mind. The other point to keep in mind is what do you want to do with that circumstance? If you decide that yes, it is a MAC, and you want to impress that upon the counterparty to the transaction, are you looking to get out of the transaction? Are you looking to delay closing? Are you looking to negotiate some amendment to the transaction? There needs to be some assessment as to what your intent is and how you want to proceed. The final thing I'll add, with regards to the purchaser's perspective is, if it's a debt funded deal, you're not only dealing with a MAC in the context of your purchase agreement, you're also dealing with a MAC in the context of a credit agreement. So, your lender will have, hopefully, a consistent MAC definition in their agreement and you need to be careful in reviewing that to make sure that your lender doesn't come to the table and say, "We think there's a MAC here. We don't have an obligation to fund on the closing, the credit that we otherwise committed to." Those are things that I think are important from a buyer's perspective.

Kathleen: Thanks, Ian, that's great. What about interim period covenants? Cyndi, can you sort of talk about those and how COVID-19 may be affecting a target?

Cyndi: Sure. For those of you who don't know acquisition agreements commonly provide

that between signing and closing the seller must conduct its business in a certain manner and not undertake certain activities, without the buyer's consent. Typically a buyer's obligation to close is conditioned on the target's compliance with these covenants. From a seller's perspective, a potentially problematic in term covenant, may include a requirement to operate a business in the ordinary course, typically in accordance with past practice. Pre-COVID-19, this would be a very standard operating covenant, very market standard, however, for most sellers this will be challenging if not impossible due to COVID-19, as most businesses are currently not being operated in the ordinary course of business. Similarly, sellers will also need to be thoughtful about how interim period restrictive covenants affect their flexibility to address current conditions, including throughout of the ordinary course, measures to reduce costs and preserve cash. A seller subject to ordinary course of business covenant could be considered to be in breach of the covenant. If it's forced to suspend the meaningful portion of it's business or its employees due to the impact of COVID-19. So from a practical standpoint, sellers need to understand what they can and cannot do within the confines of their acquisition agreement, but they also need to engage and work collaboratively with buyers to get to the closing because that's usually the end game. And need to remember that they will not necessarily be able to act unilaterally in making decisions, even though some of these will need to be made very quickly. The parties really need to balance the desire of the buyer to obtain the target business, in the ordinary course, and the sellers need to respond rapidly to COVID-19 during the interim period. Tiffany, what would be important to a buyer in respect to the seller's interim covenants?

Tiffany: Given the uncertainty of associated with COVID-19, buyers might now want greater oversight, during the interim period, by negotiating additional information and consultation rights. Buyers will likely consider specific provisions and the types of decisions that sellers will take, during the interim period, to not only address the effects of the pandemic on the target business, but also to protect their future investment. These may include any decisions taken by the target to implement or comply with COVID-19 emergency measures or to protect the target's personnel, which would require a buyer's consent. Otherwise, as Cyndi mentioned, the buyer could later assert a breach of covenant and seek indemnification. Where such measures taken by seller would trigger significant additional expenses or have a substantial impact on target's revenue. On the other hand, what we may see and it's something that Cyndi noted as well, depending on the existing relationship between the parties and the level of comfort from the buyer, we may see a more collaborative approach between the parties, with respect to decisions taken by the seller, whereby are they a joint committee, or some type of assembly, representatives from the buyer and seller would collaborate to discuss steps to be taken

to safeguard the business during the pandemic.

Kathleen: Thanks, Tiffany. As one of our viewers has asked in the Q&A, "Why did you skip bring down of reps and warranties?" The answer is I just missed it.

Cyndi: <laughter> But we recovered quickly.

Kathleen: Exactly. So, thank you ... for pointing it out. I'll turn it back over to Cyndi to ... rep and warranty.

Cyndi: So, typically there's a period of time which can range from a couple of weeks to months between the signing of an acquisition agreement and the closing of a transaction. Due to this gap there's typically a bring down obligation imposed on sellers where they are required to confirm, as at the closing date of the transaction, that the reps and warranties they gave on the date of signing of the acquisition agreement remain true at the closing. The pandemic has, in the case of many deals, had an adverse impact on the target company's business and this leading to situations where sellers are unable to bring down, or confirm, the accuracy of reps and warranties that they previously provided in the acquisition agreement, at closing. So COVID-19 may have now rendered some of those negotiated reps and warranties untrue. What does this mean? For sellers, sellers will need to carefully assess their ability to meet the bring down requirement and consider the implications of a failure to meet this closing condition. As counsel to a seller, I would strongly encourage my client to engage the appropriate people within their organization to regularly monitor and review the reps and warranties in an acquisition agreement and to identify any possible breaches and consider the implications for closing. I would also encourage a seller to engage their legal counsel in this process. Sellers should also be very cognizant of which of the reps have been qualified by a MAC provision. As previously mentioned, sellers have more leeway if the bring down condition is qualified by a MAC standard, as this will impose a higher standard on the buyer to prove a breach of such rep. In addition, if the seller has previously provided a buyer with a disclosure letter, which is typically a document that's provided at the time signing an acquisition that qualifies a certain of the reps and warranties, the seller should re-review that disclosure letter to ensure that it still remains accurate. Most importantly, sellers should be prepared to have very frank discussions with the buyers, sooner rather than later, should they identify any potential issues with their previously provided reps and warranties. Ian, can you discuss bring down from the perspective of the buyer?

Ian: Yup. Thank you. Thanks, Cyndi. Certainly. I think, from a buyer's perspective, if you're looking to either terminate a deal or renegotiate some element of a deal, or delay a closing or something of that nature, I think this is going to be an area that is going to be

more fruitful in your negotiations than a MAC clause itself. We often refer to the bring down provision as really a backdoor MAC because if you cannot satisfy the bring down requirement, the condition that the reps and warranties be true and correct at closing as they were at signing, then it's pretty hard to meet that condition. As Cyndi's indicated, a deal, for example, was signed up in January, the circumstances today are materially different, likely in a number of areas. You may have laid off a bunch of employees, if it's a seller. There may be a bunch of customers that are no longer paying on time or that are in good shape. Your supplier may not be able to deliver in the same context as they were before. There may be changes in law such as the essential services legislation that's in many Provinces, it may have impacted your ability to meet certain requirements in your business. To say those things that you said in the reps at time of signing, to say them at closing, they may not be true. Now the devil of course is in the details and whether or not those reps to be given at closing need to be true and correct, absolutely, or whether they need to be true and correct in all material respects, or true and correct qualified by a MAC. You need to look at the detail on that. And then, as I've described before, assuming you get to a conclusion that you're comfortable that this does constitute a condition that cannot be met to close, then what do you want to do with that? I think, as Cyndi's indicated, it's important for the parties to talk. There's very little value in remaining in the weeds about this right up to closing because the circumstances in this kind of world are such that you need to collaborate. I think that really is the scope of what would be relevant for the bring down, from a buyer's perspective.

Cyndi: I think one point that you made is very important. When you look at the reps and warranties there's generally two elements to them. There's the factual element the target has to confirm but then there's obviously the technical, legal implications of much of the language that has been worked through by M&A lawyers. It is very important to sit down with your counsel and go through it. In many bring down situations where I am acting for the target, we have sort of an all parties call, where we walk through in detail the reps to make sure that they're accurate within the meaning of the sort of legal language that's been provided.

Ian: I think it's also probably a good point to raise here as well and it's not just about the lawyers, right? There's other relevant professionals that are involved. Accountants, other financial advisors and the reps, as they relate to other areas of the business which aren't purely legal, you need to collaborate with those other advisors as well.

Cyndi: Yup. Good point.

Kathleen: Thanks, Cyndi and Ian. Why don't we turn to the next topic. Faran, how's

COVID-19 affecting regulatory court and third party approvals?

Faran: Well, Kathleen, as you can expect some of these approvals are taking a lot longer to obtain as, back in the so called normal time as we used to refer to it, that's not to say that these approvals are not being obtained. The Competition Bureau has issued some guidance that it's still reviewing. They issued guidance saying it's going to take a bit longer than usual specially in terms of cases where they have to contact other interested parties and there's delays in hearing back from them. If you are going for a competition review or Investment Canada review you can expect the process to take a bit longer than usual. In terms of corporate approvals, we're hearing that interim orders can be obtained. In fact, I think Kathleen, you obtained one via video recently. So interim orders, some courts are being flexible in terms of being able to obtain interim orders for parties. Temporary approvals is an interesting area and typically buyers and sellers will have a robust discussion about which consents are conditions to closing, which are nice to have, which are must haves for closing. I'll give a simple description of what's happening in the market these days. Landlord consents tend to be items that need to be obtained every time because almost every commercial lease has a consent requirement or either ... signed at the lease. Given what you may have heard in the media a lot of tenants are trying to get rent abatements or are behind on their rent. So, if you're behind on your rent to your landlord, good luck trying to go get a consent to a change of control unless the buyer is someone who, with that same landlord, is either paid up on their rent at other locations or has a stronger balance sheet than the potential target. Those items you need to consider depending on what your negotiations with those third parties are. Another key item to consider is, given how international supply chains are these days, significant customers or suppliers may be located in different jurisdictions. And depending on what's happening there in terms of the business atmosphere, people working remotely, whether the right people are available at the right time to provide that consent within a meaningful period of time or whether it's something the parties decide, may be something to get close to closing, or may be something that is negotiated as a separate indemnity or something else.

Kathleen: Great. Thanks, Faran. Tiffany? Sorry. Ian, actually, I think you were going to talk about ... buyer.

Ian: Oh good. We'll pass it around. Tiffany can respond on it as well if she wants. Faran outlined a lot of points that I think are relevant in this area. I'll just augment it a little bit and say from a buyer's perspective, the things that were negotiated as consents and regulatory approvals at the time the deal with struck, were probably done in the context of, what Faran has described as the normal circumstances, we're obviously now in a

different world. You probably have limited control over the regulatory elements of it but if you take a look at the third party consents, and whether they be landlords, as Faran described, but also customers, third party lenders, potentially other shareholder groups, from a buyer's perspective if this is a transaction you really want to close, you need to consider which are the important ones and which are the ones that are not quite as important. Are you prepared to close over on some of these? Waive the requirement to get certain consents obtained and then proceed to closing. Or if you're not, but the counterparty still wants to close, perhaps you'd negotiate some sort of indemnity, or some sort of arrangement whereby you're going to share the risk or someone's going to bear the risk and close over some of those conditions. For a regulatory standpoint, I think it's also important to take into account that we're all experiencing this social distancing life, and it's not just us and our direct deal team parties, it's also all those regulatory parties. So I think patience and politeness and sort of consistent negotiation but also persistence but make sure that you recognize the fact that the regulator that you'd normally dealt with when he or she was in her office, is probably at home, perhaps with a family trying to manage circumstances, and while they want to do their job they've got to do it in the context of the same circumstances we're in. The last thing I wanted to raise was maybe the transactions we're involved with are cross border. To amplify it further, if it's a US party that's involved in it, you may be engaged with counsel dealing with regulatory approvals in the US. They're dealing with similar circumstances. Same in the context of Europeans. I think we need to step back and say, "Okay. Fine. The timeline we contemplated at the time the deal was signed was X. Is it now X plus 2, X plus 3, how much more time are we going to need to get this thing realistically closed?" I think people need to be realistic about that kind of stuff.

Faran: Just one last comment there, Ian. I think you touched on it so I should point that out for everyone listening. We have a lot of clients and regulators who haven't given much thought to the fact that while some of us have the ability to work remotely, really well, others, especially a lot of government departments, are doing this for the first time. It's been an uphill curve and we've been fielding questions from some of our clients that work with regulatory authorities, "What is the best way to do large size file transfer?" or, "How do you deal with circumstantial filings that were never done before electronically?" It's been a learning curve for a lot of people so, patience, I think, and trying to work together is critical to getting deals done in the situation we find ourselves in right now.

Ian: And the good news is, it's getting done. Right? People that want to close deals are getting it done. The fact that you can't physically be in a place isn't the barrier to getting a deal done.

Kathleen: The regulators are working really hard. ... for example, still reviewing proxy circulars and raising any questions from a 61 101 perspective within 5 days. So they're not putting their pens down at all. We're sort of moving through this fairly quickly and almost running out of time. I think, Faran, if you want to make a quick one termination provisions, but then we'll move onto the next stage.

Faran: Happy to do that, Kathleen. From a seller's perspective, typically a seller is not given much of a choice in terms of terminating an agreement by a buyer, so we would have limited walk rights unless the consideration is shares in the buyer, in which case, you may have better conditions to closing. All sellers generally need to take a close look at what their conditions to closing an agreement are and if they wish to not close, see where the business has been affected such that one of the conditions in a seller's favour may be triggered and it can walk away from the deal. But typically if a buyer is ready to enter and waive it's conditions sellers may not have much of a choice in terms of whether they want to close or not. But I'll let one of the parties speaking for the buyer take the ... buyer may wish to do.

Kathleen: Tiffany?

Tiffany: I would say in addition to what the group has already mentioned with respect to MAC clauses and bring downs and any regulatory approval delays, I think from a buyer's perspective, a buyer may also pay particular attention to any outside date provision that's provided for in the agreement, to determine whether to terminate. Since it's likely that there's other closing conditions, as we've all previously discussed, would be significantly impaired in light of continual business closures. I would say the other thing is that if the parties have negotiated a reverse termination fee, or also what's also known as a risk rate fee, whereby an amount of money is paid by the buyer to the target after the buyer accepts the deal. The buyer will really need to consider whether the quantification of exposure under the purchase agreement to determine whether it's worth the risk of early termination by the buyer.

Kathleen: Great. Thanks. So why don't we, in the time that we have left, let's talk about some transactions that have already closed. We do think that there are still COVID-19 impacts for those types of transactions. Our first topic in the context of a private M&A transaction is earn-out clauses or post-closing incentive payments. Which are typically tied to post-closing milestones. Faran, do you want to comment from the seller's perspective, what your concerns are here?

Faran: Sure. From a seller's perspective, most amounts are set out in metrics that are either financial or tied to the ... performance business and then tied to a certain period of

time, that is to say the business needs to do a certain thing by a certain amount of time, in order to trigger the earn-out for the vendor's to get a payment. It's typically, earn-outs are set up against the historical performance of the business, as in, if you did a hundred million of revenue at closing, next year revenue needs to be a hundred and ten million or a hundred and 20 million, if that's achieved within a year or 18 months, a certain payout is triggered. The concern here may be that given what's going on, if it's a non-essential business it may not be operating. Depending on what type of business it is revenues may be down, profits may be down. It may be more difficult for a vendor to be able to, while it's doing everything in its power to try and make the business achieve those plateaus, it may not be enough time or business may be affected such that earn-outs may not be achievable. In that case a seller may try to go and negotiate with a buyer, try and get a longer timeframe, or perhaps take out the few months that businesses has been disrupted and focus on a different time frame. The other side of this may be that businesses that closed 2 or 3 years ago, transactions that closed 2 or 3 years ago, where the earn-out is now close to being payable and certain buyers may gain what's happening in the market right now, try and get the business to show a lower revenue or lower profit, to avoid paying out a substantial earn-out that may have been already earned. But those are facts sellers who have earn-outs need to be aware of and go back and review with their legal counsel what their agreement said.

Ian: So, thanks, Faran. I think from a buyer's perspective, there's two elements that I think are particularly important. One is often these earn-outs are set up in a manner to motivate the people that are actively involved in the business to see the business be successful. So, if it's a revenue threshold you need to meet then you've got the team that's in there trying to make it happen. From a buyer's perspective, these are your employees. This is your team now, or it's part of your team, and you need to make sure they remain motivated. It may well be a bit of a windfall for you that you wouldn't otherwise have to pay this earn-out, because the threshold wasn't met, and maybe that's a good thing from the standpoint of a company that is otherwise challenged because of the pandemic. But you need to step back and say, "Okay. So that was part of the compensation for the sellers, some of whom are now my employees, what do I want to do to make sure that they're still motivated to make a success of this business going forward?" You need to think about the long term. In that context you need to say, "Okay, look. Perhaps we push out the earn-out date," as Faran described, "for another year. Or another 2 years." I wouldn't push it out too far because one of the challenge with earn-outs is it limits the buyer's ability to make changes in business while the earn-out is still potentially due. There's a bit of a delicate balance to be played in that circumstance. I think the last point I'll raise is while we don't advocate gaming the system in any circumstance, I think one of

the ways to make sure you protect against those kind of circumstances is put in certain covenants into an earn-out clause so that the seller, and the parties that may be entitled to the earn-out, are getting access to information that's necessary so that they can assess whether the earn-outs been met or not. Even where they may not be involved in the business.

Kathleen: Thanks, Ian. Faran had mentioned VTB's under takeback mortgages, earlier, Ian do you want comment on those promissory notes, other means of payment? What will we be seeing in the post-closing context?

Ian: Yup. Sure. Thanks a lot, Kathleen. I just want to mention one point here and I know we're limited on time so I'll just raise it quickly. You think about the conducts of transactions that have already closed, and you think about a company that you've just acquired as the buyer, and you think about, let's assume it's a relatively highly levered business at the time, if it's revenue is materially impacted by the pandemic, all of sudden you've got a material amount of, perhaps you don't have the same revenue to support the necessary debt on the business. If part of the consideration, the deal was a lender takeback mortgage in favour of the sellers, chances are that VTB is significantly subordinated to senior lenders, such that you're going to be negotiating with your senior lenders to try and get some sort of abatement, or some sort of delay or arrangement such that you can survive this period of time. You're going to have to do the same thing with your former sellers and make sure that they're comfortable, even though they may not be security, even though they may be subordinated and may have very little role in the actual decision making, you've got to keep them happy. Where as a VTB looked like a good idea at the time, perhaps it may put yourself in a bit of a challenge as a result of the pandemic for transactions that have already closed.

Faran: Okay. I'll just add on to that. If the senior lender is bring into forbearance or renegotiating terms of it's senior deck, as the holder of a VTB you may want to then try and see if you can match, if you didn't do this before, try and get the same reporting and understanding of what's going on so that your security matches the risk profile of the business now, as opposed to what it had been at closing.

Ian: Yup.

Kathleen: Thanks, Faran. Cyndi, so quick thoughts on transitioning services agreements?

Cyndi: Yeah. Sure. If you're a seller and you're party to a transition service agreement where your providing services, post-closing, to the buyer to help with the buyer's transition as the new owner of the purchased business, you need to look very carefully at the

wording of that agreement. Particularly if there's an inability on the part of the seller to perform the services under that agreement in light of COVID-19. Where you are unable to perform the obligations under a transition services agreement you might, as a seller, be able to avail yourself of any force majeure clause in such agreement. But the ability to rely on that clause will depend on whether it was drafted in a manner that would cover public health emergencies such as COVID-19, or otherwise contains adequate catchall provisions. Additionally, you'll want to discuss with the buyer's their expectations relating to performance under the transition services agreement rising as a result of the pandemic. Tiffany, do you want to speak from a buyer's perspective?

Tiffany: Thanks, Cyndi. In TSA agreements, buyers will be more focused on supply arrangements and related goods and continuity arrangements in light of COVID-19. Particularly where material services are outsourced to third parties to ensure that the obligations under these arrangements can be met during the TSA period, under current conditions. As Cyndi mentioned, the buyer will also be looking at any force majeure language in the TSA to ensure that the seller will not be able to excuse it's inability to perform under the TSA. I think buyers should also consider whether the current climate could affect the timeline for any pre or post completion separation activity and therefore, the duration of the transitional services themselves and buyers will likely, in light of this, want to extend the TSA period. Especially given the uncertainty of non-essential businesses remaining closed for at least another few months. So where it may be difficult for the seller to perform it's obligations the TSA at the moment, an extension would allow the sellers performance to resume while centered on essential business ban would be lifted.

Kathleen: Great, thank you, Tiffany. Last but not least, indemnification claims. Tiffany, your final thoughts as a buyer?

Tiffany: Sure. From a buyer's perspective in light of COVID-19, and it's impact on businesses, buyers are likely to scrutinize the acquisition agreement to identify the seller's reps and warranties, and may make a claim for indemnification where significant losses have been identified. And we're seeing, those including, arising from supply chain disruptions or contract breaches or terminations. Also, where representation and warranty insurance, a policy has been put in place within the context of the transaction, the buyer should be looking to the policy to determine whether or not it can seek compensation under the policy. The policy language should be carefully reviewed to determine whether the buyer could rely on the policy or business interruptions or losses related to COVID-19 or whether there's exclusionary language relating to any virus or pandemic related business losses. Depending on when the transaction has closed, for example, if it closed

before the COVID-19 outbreak, there's likely no specific language included in the policy relating to COVID-19 but it's possible an expansive exclusion general language relating to a pandemic or virus may prevent the buyer from pursuing compensation under the policy. Definitely a proper review of the policy will be important.

Kathleen: Cyndi?

Cyndi: Yeah. Sure. I don't have much to add from what Tiffany said. I think the important point is a seller should be aware that in the current environment buyers are likely going to be looking very carefully at the reps and warranties that were provided in an acquisition agreement to see if they can have a claim for. Indemnification if they feel that the business that they acquired has been significantly impacted in adverse manner given the current economic conditions. Again, just getting back to the previous point relating to agreements, bring down reps and warranties. It's very important in the environment to re-review your reps to ensure that there is no exposure for a seller for an indemnification claim on a go forward basis.

Kathleen: Great. Thanks, Cyndi. So, there you have it. From other LOI stage to post-closing. So the impacts that COVID-19 is having for buyers and sellers that they need to consider in the M&A context. Before we turn to questions and we have a few that we're going to cover, I just want to highlight our upcoming webinar in the series, M&A In Uncertain Times. You can join us same time next week, on April 21st at 1:00pm, Eastern, for the our next webinar on how to prepare for M&A deals coming out of COVID-19 and then there's another session on April 28th where we'll cover deal dynamics post pandemic. We do have a couple of questions. The first one that I wanted to address was, maybe I'm going to put this to you, Ian, what are the current impacts on cross border activity? What are seeing there in terms of transactions?

Ian: I think in the context of cross border deals I think it depends upon the jurisdiction and it depends upon where in a jurisdiction. As most people in Canada doing transactions will know that very few of the deals that were involved in do not have a cross border component to them, whether it's a multi-nationally your dealing with that's headquartered outside of Canada, or it's a financing party based in the US, or based in Europe. Many of the deals, I would say the majority of the deals where I'm actively involved in have cross border components to them. I think we're being particularly careful in assessing where the particular business is that's the cross border component to the deal. So if you've got a lender that is based in Texas, you may be in a better position than a lender that's based out of New York, at the particular time. If you're counterparty is somewhere in the Far East, perhaps it's less of an impact but I think if you take it down to the individual levels,

the counterparties you're dealing with, or the lenders you're dealing with, these are people who are actually in those places. So we are seeing impact. We're seeing delays but, frankly, we're not seeing people that are just dropping tools and saying, "We'll get back to you when this is over." These are people that want to engage and, as Faran has relayed earlier, there finding ways to make it happen and I think one of the things that I am sort of discovering about this whole pandemic is there are some business continuity plans in place and to a large measure, at least as far as the stuff we do, you can engage in business going forward. It's impacting cross border deals but it's not stopping deals. It's delaying them.

Faran: And if I can chime in for a second, Kathleen, to Ian's point it really depends on how you view cross border. I mean, 6 or 8 weeks ago I had a Canadian buying a Canadian business deal go on hold because of the impact of what was going on in China on the buyer's larger world wide business. You wouldn't think of somebody in Canada as a cross border issue but it had an effect. Last week we kicked off a deal where a US party is coming into a by a Canadian asset, we're having to do diligence and we're all systems go. So, it's having some impact but people who want to do deals are still going ahead and doing deals. Sometimes the timeframe may be a little modified but deals are still happening.

Kathleen: Great. Thanks, Faran. We've got a couple more questions. If people have to drop off, that's fine. We understand. As I mentioned before we are recording this and it will be posted on our website and we're happy to answer questions of people who can't stay on the line but we will stay on for a few more minutes. The next question is, probably for Cyndi, she had mentioned material changes to the company. This viewer is wanting to get a bit of understanding what is a material adverse change or effect? You did cover that in your comments but do you want to just make that quickly.

Cyndi: Sure. So it's usually a significant impact on your business. First of all it has to be a change. That's kind of the quick and easy answer. And then it has to be adverse and generally quite significant. What that would like would really depend on the particular target and their particular business, the size of the company, etcetera, because what's material and adverse to a smaller company is not going to have the same impact as a larger company. So you have to look at it on a case by case basis but I do think what is really important is the carve outs and to a MAC because if you're struggling, if you're company has had a significant, material adverse change due to COVID-19, if the carve outs include a general economic, against I assume it won't be a MAC if it's a change caused by general economic conditions, then a MAC hasn't occurred to your company even if your struggling at the current time. The definitions can inclusion is very important.

Not just the actual effect that you're having at this time.

Kathleen: Thanks, Cyndi.

Ian: I was going to say, take it to an example, all the restaurants in Canada, and I'm sure elsewhere in the world are currently closed. Right? You can't go to a restaurant. So if you're buying a business that is a restaurant group, that restaurant group is definitely impacted but it's probably impacted in a simpler way to some other restaurant group. So you'd have a hard time arguing that the carve out would not apply in that circumstance. But if your restaurant group had a fire at its distribution facility, perhaps, or some significant, you lost some major lease in respect of the certain sites you needed for that restaurant, then it's disproportionately impacted, because compared to the industry as a whole. So, it's a nuanced fact specific analysis that needs to be done.

Kathleen: Great. Thanks, Ian. Somebody else has asked whether a MAC is a valid reason to drop a deal at the LOI stage. Of course, looking at that, usually what we see at the LOI stage is those are non-binding agreements, in the first place. Anybody want to talk about that?

Cyndi: Well, I think, I rarely see a MAC provision in an LOI, because as Kathleen pointed out, they are typically non-binding. But if you have a letter agreement sometimes they'll have a MAC provision and I think, at the end of the day, it really depends on, as Ian alluded to when we were talking about this, what's the goal of the buyer? If the buyer wants out of the deal because they are concerned about the future and the current environment and it's just not the time to do the deal that they thought they wanted to do in January, then if they can rely on a MAC clause they can terminate the LOI. But also as Ian alluded to, it's a very standard. So, if you have a seller that wants to push on the MAC clause and claim that there wasn't a MAC, it's going to be harder, I think, for a buyer to prove that a MAC has occurred.

Kathleen: Thanks, Cyndi. We have another question which is if there is a force majeure clause, for either the buyer or the seller, can the company use that not to fulfill obligations? It's an interesting question. I don't really normally see force majeure clauses in an M&A context, but certainly in contracting generally speaking, before I put it to the panel, I will point out that we've done a number of webinars that are posted to our website on force majeure provisions. Both generally speaking and in a construction context. I encourage you to look on our website and find those webinars if you want detailed analysis on those particular types of provisions. Does anybody have a comment on that? No?

Faran: I'd just say, Kathleen, echoing your point, I wouldn't typically see those in M&A agreements. I would see them in a TSA, which I think we chatted about, you may see seller use that as a reason for not providing certain transitional services but I would not generally see that as an out from closing a transaction.

Kathleen: It is a topic that I think would come up more so now in the due diligence process. We look at sorts of different provisions in a due diligence context, change of control provisions, consent provisions, things like that, but I suspect in, particularly material contracts, we would be looking quite closely at those force majeure provisions nowadays. Another question is whether we feel that many inquiries from sellers in relation to any pre-existing earn-out performance targets. Are there any examples that we have where amendments have been agreed to and were these extending performance timeframes or more wholesome target revisions? I personally haven't had to deal with that yet but I work in a public M&A field more than private. That's not really something that we would see in that context.

Faran: I think, Kathleen, it's early days. If you look at March 15th as the date where a month in and I think as the next few weeks and months progress, we'll actually see what the impact is on businesses and financials and so on, because you might have a blip of a month and then the business may change depending on what it's doing and what's happening. I still think it's early days but I think it's something that sellers and buyers will want to keep an eye to see what is there and depending on, as you said, what the relationship between the parties is post-closing and how involved the sellers in the business, you may want to revisit that to preserve relationships and ensure a better continuity for the business going forward.

Ian: I agree with Faran in this one. This is on the to do list but it's not an urgent to do. I think it's more focused on the very urgent items that are the key right now.

Kathleen: Great. Thanks, Ian and Faran. We have one last question. I'm not sure were the ones who can answer this because it does sort of go into the employment law context, but how would a company's staff currently laid off at the time of sale affect a closing, assuming a sale could actually be closed on all other fronts. Anybody want to take that one?

Faran: I'll throw something out and maybe Ian will contradict me.

Ian: Yeah. <laughter>

Faran: My view, Kathleen, would be, to a degree I think it would depend on the industry

whether layoffs are common in that industry or not, and if they are and that's part of the employment work force, you treat them as any other business where employees may or may not be laid off. I don't think in those industries much would change. In terms of industries where it's not the norm and employment agreements don't have those employee layoff type provisions where there's a risk of constructive dismissal, being something that employees may bring up. I think you would want to either have a specific indemnity or, again, depending on whether the agreement has been signed, or it's about to be signed. If you're negotiating the agreement I think a buyer would want to make sure that the work force will be available to it post-closing when things go back to normal, and that it will not be left on the hook for any severance or constructive dismissal costs. In the same ... the seller may want to make sure that it's covered on its basis in terms of it's not left on the hook for any severance costs if the business is fundamentally different post-closing.

Kathleen: That's great. Ian, any final thoughts?

Ian: Yeah, I would just add that most purchase agreements will have detailed provisions related to employment and Faran raised a few points but I think that, to answer this specific question, could you get to closing in a circumstance where there's a bunch of employees that are currently laid off, I think the simple answer is yes. I think it's going to require both seller's counsel, the buyer's counsel and then their specific employment experts to sit down and say, "Okay. So, this group of employees are currently laid off but the expectation is when the pandemic has passed, to a point where these people can come back to work and we don't have to close, except for essential services." There's a way to make it happen. Faran raised some good points about are those employees going to be available when they come back. As Kathleen rightly pointed out, there's a bunch of other webinars we've run specifically on employment considerations and these are things we're dealing with in real time. It's changing from day to day but my view, it can be done, and we just need to roll up our sleeves and figure it out.

Kathleen: That's great. Thank you, Ian. I think we are out of time. We've appreciated the opportunity to discuss this topic with your audience today. Until next time, stay positive, stay healthy and our very best to everyone. Thank you very much.

Cyndi: Thanks.

Ian: Thanks all.

Faran: Thank you.

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