
M&A and Acquisition Financing

Introduction, Documentation, Experiences

Practice Group M&A

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Agenda

- » Structure of acquisition financing
- » Standard Swiss or German loan agreement vs. international loan agreement (LMA-Standard)
- » Standard loan agreement for international transactions
- » Supporting documents (legal opinions etc.)
- » Experiences, questions

Structure of acquisition financing

Senior A: highly secured with repayment schedule

Senior B/C: secured without repayment schedule („bullet“- endfällig)

- » Term Loan Facilities
- » Revolving Facilities (e.g. working capital line).
- » Ancillary Facilities: e.g. local currency needs derivatives or guarantee bonds („Avalé“)
- » Specified Facilities: capex, restructuring, further acquisitions

Mezzanine Financing

- » Subordinated or deferred payment of interest and no repayment schedule / Equity Kicker

Vendor Loan / Deferred Purchase Price / Holdback / Earn Out

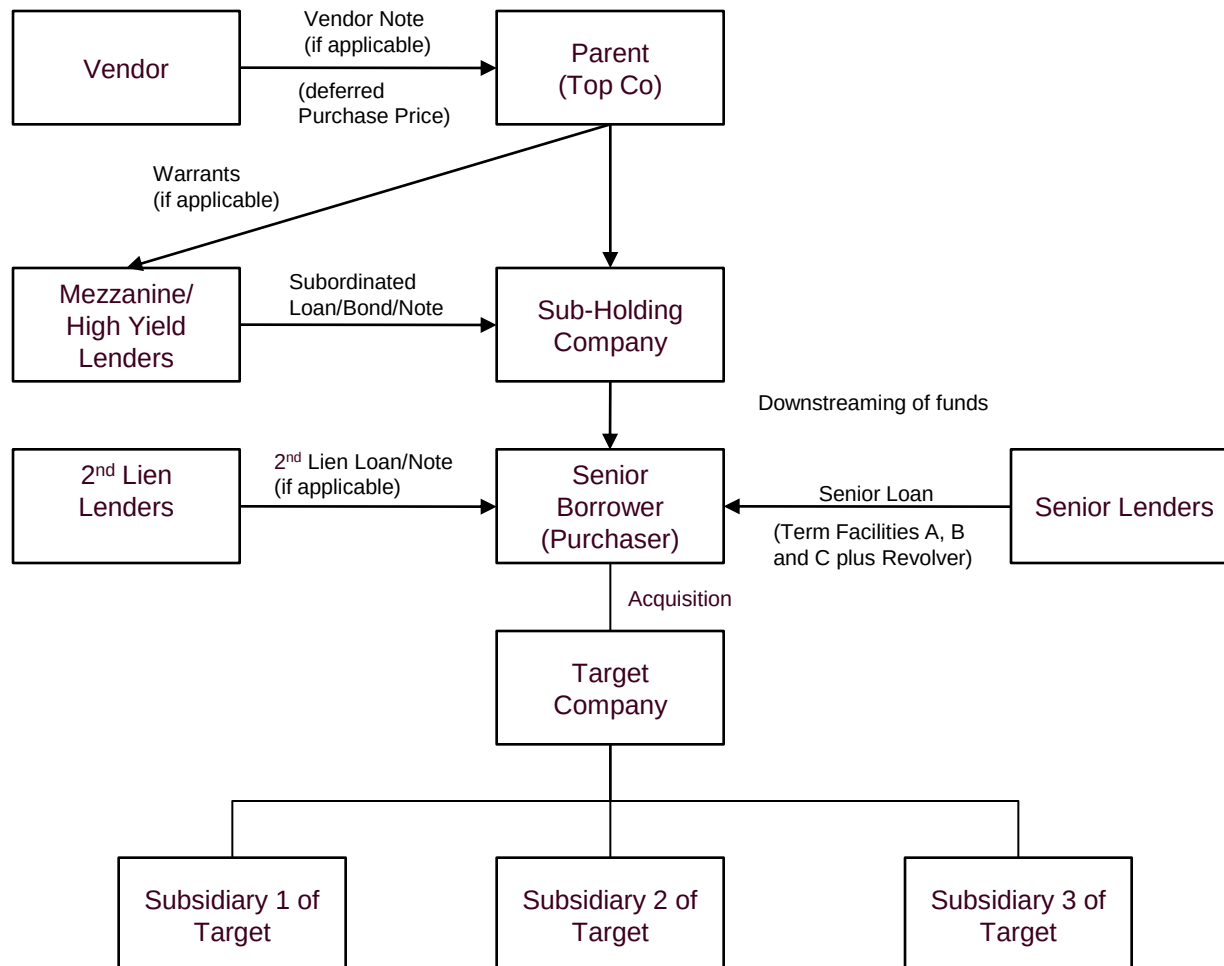
Private Equity Investors

Equity Investors

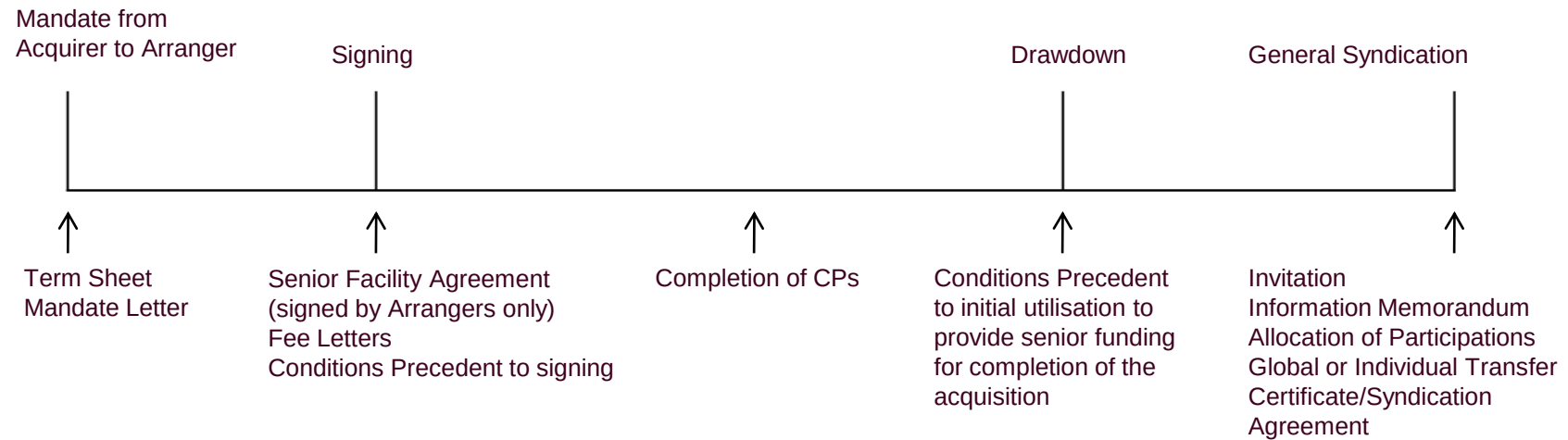
Documentation for Acquisition Financing

- » Mandate Letter
- » Term Sheet
- » Information Memorandum
- » Senior Syndicated Facility Agreement
- » Security Documents / Collateral Structure
- » Intercreditor Agreement
- » Intra-Group Loan Agreements
- » Mezzanine Facility Agreement
- » Hedging Letter
- » Fee Letters
- » Other Documents

Structure of a Leveraged Financing



Sequence of Acquisition Financing



Introducing LMA – The Loan Market Association

The LMA was opened for membership in 1996 with the objective of fostering an environment in the Euromarkets that would facilitate the constructive development of a secondary market for loans by:

- Simplifying and standardizing loan agreements
- Establishing market best practice in the loan market

By 2010, over 430 organizations, mainly banks, institutional investors and law firms are members of the LMA

Both meyerlustenberger and Beiten Burkhardt are members of the LMA.

Visit the LMA website on: <http://www.lma.eu.com/>

Documentation – The Loan Market Association recommended forms

- » The standardized LMA Loan Agreements are widely accepted throughout Europe
- » Standard form for acquisition financing
- » LMA forms serve as point of orientation and starting point in negotiation between the loan parties
- » They leave room for individual tailoring in each underlying case
- » (e.g. representations, undertakings, financial governances)

Standard loan agreement

- » Based on the LMA Standard Loan Agreement
- » Type of transactions
- » Similar structure
- » Similar wording

Implementation of finance transaction

1. Mandate letter / Term Sheet
2. 1st draft of loan agreement and security agreements (**Finance Documents**)
3. Ongoing negotiations and due diligence by MLA(s) (including co-ordination with foreign counsel)
4. Signing of Finance Documents (usually PDF signing), completion of CPs
5. Utilisation request and disbursement of the loan

Structure of the loan agreement

1. Administrative provisions (loan amount, calculation of interest, repayment etc.)
2. Draw down/conditions precedent (CPs)
3. representations, undertakings, covenants and events of default
4. Boilerplate clauses (notices, applicable law, jurisdiction, relationship between the lenders)

Key Concerns of the Borrower

1. Control
2. Certainty of funds

Key Concerns of the Lender(s) (1)

1. Seniority (preference in position over other lenders) or at least equality with other lenders/creditors (*pari passu*)
 - Corporate structure
 - Intercreditor agreement
2. Information (up front and ongoing)
3. Certainty as to the effect of the agreement
4. Ability to withdraw
5. Maintenance of the Borrower's assets and income

Key Concerns of the Lender(s) (2)

Assessing Acquisition:

» business case

- Industry considerations: consolidation trends, cycles, structure
- Synergies via economies of scale in production, sales, R & D
- Diversification of product lines, customers, distribution networks, geographic presence
- Consistency with core business
- Management expertise
- Execution risk

» purchase terms

- due diligence reports (in particular financial, tax and legal), approvals, appraisals, etc.
- SPA, Asset Purchase Agreement, Earn Out Agreements
- Terms and conditions of all financing (and equity issue, if any) for the deal

» purchase price: EBIT/EBITDA multiples, etc.

Key Concerns of the Lender(s) (2)

» Financial Metrics

- Consolidated projections
- Base case model
- sensitivity analysis
- Worst case model (cash flow only of acquiring company)
- Reasonable EBITDA cushion
- Loan/security structures: term, amortization and committed/uncommitted appropriate to risk

» Ongoing Risk Mitigation and Monitoring

- reporting requirements (annual accounts, annual updated business plan etc.)
- Interim (monthly or quarterly) financial reports with comparison of actuals to plan
- financial covenants to be reported on a monthly or quarterly basis and reviewed annually
- Strict non-financial covenants (no restructuring, no acquisitions, etc. without lenders' approval)
- Regular communication between bank and acquiring company's management

Undertakings and covenants (Clauses 12 and 13)

The purposes of the undertakings and covenants are to ensure that the Lenders have the information they need:

to ensure good housekeeping by the Borrower; to give the Lenders leverage;

and to protect the Borrower's assets.

It makes little difference whether any particular issue is dealt with as an undertaking or as an Event of Default since a breach of an undertaking is an Event of Default. The tradition is to include as undertakings those things which the Borrower can promise (e.g. not to grant security) and as Events of Default those which he cannot (e.g. failure to pay, bankruptcy, material adverse change).

Real Life Example: Excerpt of General Undertakings

25.1 Change of business

The Company shall procure that no substantial change is made to the general nature of the business of the Borrower or the Group from that carried on at the date of this Agreement.

25.2 Change of Group structure

The Company shall procure that without the prior written consent of the Lenders no change to the existing structure of the Group is made if such change, in the reasonable opinion of the Lenders, would negatively affect the substance of an Obligor or NewCo. Other changes in the structure of the Group (including intra-Group mergers) shall be permitted.

25.3 Merger, Joint Ventures and further Acquisitions

No Obligor shall (and the Company shall ensure that no other member of the Group will) enter into any merger, joint venture or further acquisition with companies outside the Group with an Enterprise Value of more than CHF 10'000'000 in aggregate for the Group for the financial year 2011 and of more than CHF 20'000'000 p.a. in aggregate for the Group for the financial year 2012 and thereafter (whereby "Enterprise Value" shall be defined as purchase price for the equity plus net debt) without the prior written consent of the Lenders. In any event, the Lenders shall be informed in advance about any merger, further acquisition or joint venture.

25.4 At arm's length trading

No Obligor shall (and the Company shall ensure that no other member of the Group will) enter into transactions either within the Group or with third parties other than at arm's length terms.

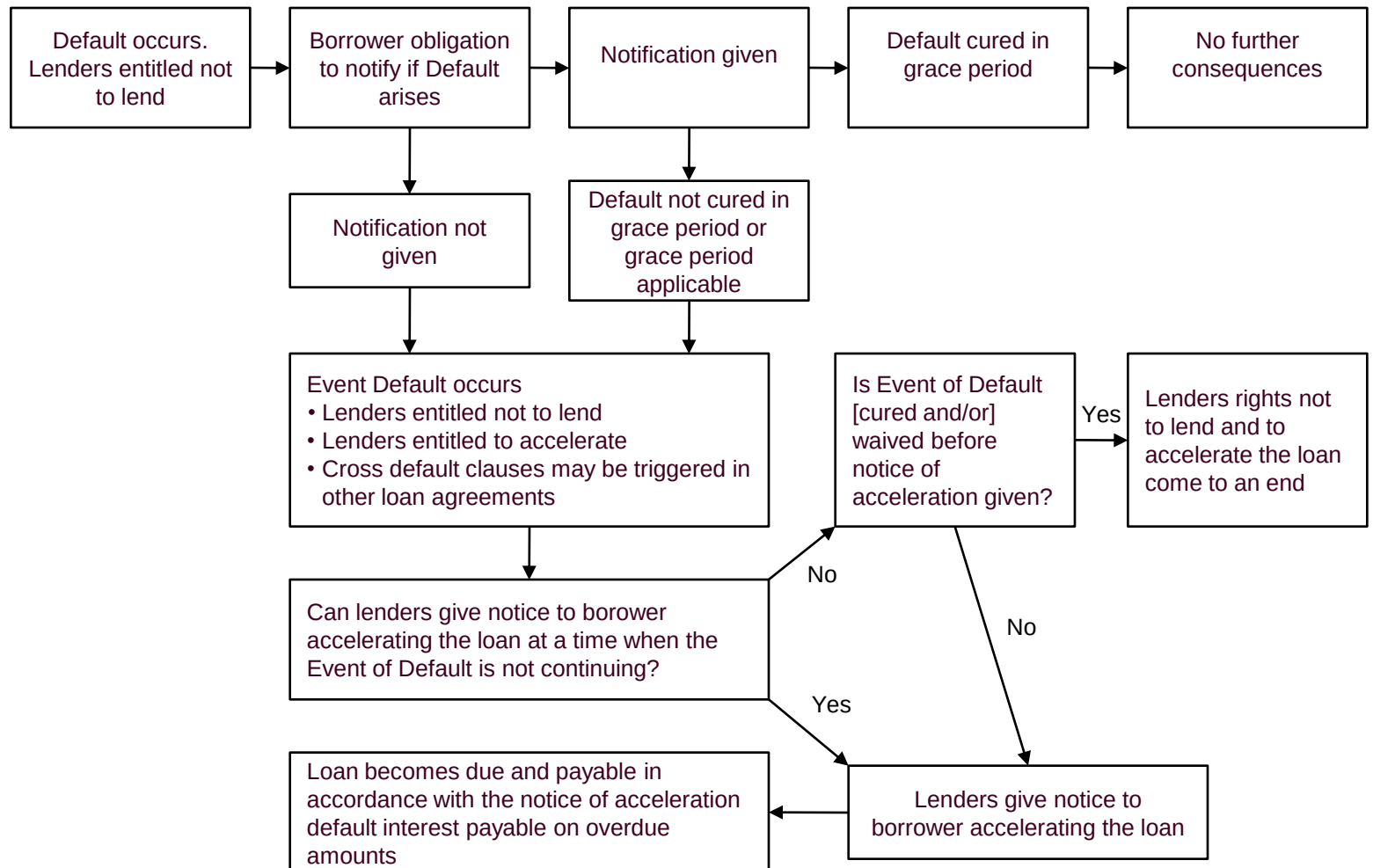
25.5 No participation in physical cash pooling agreements

- (a) The Guarantor shall not be a party to a cash pooling arrangement with any other participant than the Borrower.*
- (b) The Borrower shall ensure that bank accounts which will be credited by a Utilisation under this Agreement are not subject to any physical cash pooling arrangement.*

25.6 Closing of the Acquisition

The Borrower shall supply to the Agent in sufficient copies for all the Lenders not later than three Business Days after the initial Utilisation under Facility A, an executed copy of the closing memorandum concerning the Acquisition signed by all parties to the Acquisition Agreement which shows that NewCo has acquired all assets pursuant to the terms of the Acquisition Agreement and that the Acquisition has been consummated in accordance with the Acquisition Agreement and that no material part of the Acquisition Agreement was amended, modified or waived without the prior written consent of the Finance Parties.

Stages of a Default flow chart



Financial Covenants

Financial Covenants need to be fulfilled at signing of the Facility Agreement and as long as any amounts are outstanding.

- » Loan-to-value ratio (LTV)
- » Level of indebtedness (Gross Debt divided by EBITDA)
- » Interest Cover Ratio (ICR)
- » Minimum Net Equity
- » Minimum Equity Ratio
- » Subordinated or deferred payment of interest and repayment schedule

Risks in aligning finance documents and SPA

1. Potential conflict between provisions
2. Due diligence reports (reliance issues)
3. Veto rights of lenders v. planned restructurings/integration measures
4. Aligning of time table
5. CPs v. “certain financing”

Conditions Precedent (CP) (1)

1. Utilization of the Facilities only after completion of all CP's
2. Scope of legal Due Diligence
 - Borrower(s)
 - Guarantors / Third Party Pledgors
 - Target Company(ies)
3. Individual tailoring of the CP-List according to the transaction structure

Conditions Precedent (CP) (2)

1. Corporate Documents of the Parties

- Constitutional documents
- Resolution of the Board of Directors
- Company Certificates

2. Legal Opinions

- Confirmation that the Obligors are authorized to enter the Finance Documents
- Confirmation that all obligations contained within the Finance Documents are legally binding for and enforceable against the Obligor
- Security interests are enforceable
- Realization of the security is possible by the Lender
- Validity of the choice of law and jurisdiction

Conditions Precedent (CP) (3)

3. Finance Documents

- Duly signed Facility Agreement
- Duly signed Security Agreements
- (Process Agent Agreement)

4. Acquisition related documents

- DD reports financial, legal, environmental, pension etc.) each capable of being relied upon by lenders
- Structure memorandum
- Funds flow statement
- (Signed) acquisition agreements
- Shareholders agreements etc.
- Other transaction documents
- Merger approvals, if any

Conditions Precedent (CP) (4)

5. Other

- Signed transfer forms, including blank endorsement, if required for foreclosure
- Account opening formalities
- Regulatory or governmental approvals, if necessary

Conditions Precedent (CP) (5)

1. Preparation of a detailed CP-List at an early stage of the transaction
2. What documents are required from each Party
 - Borrowers, Guarantors, law firms involved for Legal Opinions
3. Who is responsible for the delivery of the CP?
4. Is the CP in form and substance satisfactory to the Lender?
5. Keep the CP-List up to date at all times of the transaction
6. Organization is everything

Real Life Example: Excerpt of CP Schedule

3. Acquisition

- (a) *A final version of the structure paper of KPMG [●], 2011, setting out the final structure and the terms as well as the tax consequences of the Acquisition.*
- (b) *Commercial, financial, and tax due diligence report of KPMG dated May 29, 2011, and legal due diligence report of meyerlustenberger dated May 25, 2011 regarding the Acquisition.*
- (c) *Reliance letters in a form and substance satisfactory to the Arranger, addressed to the Arranger for the benefit of the Finance Parties in respect of the reports designated in (a) and (b) of this item 3.*
- (d) *A complete set of the duly executed Acquisition Agreement including all amendments to the Acquisition Agreement.*
- (e) *Copies of any clearance from any merger or competition authority obtained or confirmation, satisfactory to the Arranger, that no clearance is required.*

Public Takeover Financing (Germany)

Sec. 13 sub. 1 sentence 2 German Takeover Act (WpÜG)

In case that the offer has a consideration in the form of a monetary payment, the bidder has to instruct a securities services company independent from the bidder, that the bidder has taken the required steps to secure full payment of the consideration when due and payable.

- “Hard” financing confirmation is required, the contents of which are non-negotiable and may not be subject to any conditions.
- The securities services company is directly liable to investors that accepted the offer in case of non-payment of the consideration.
- The Facility Agreement needs to be carefully adjusted to reflect the above (alternative: separate letter agreement).

Public Takeover Financing (Switzerland)

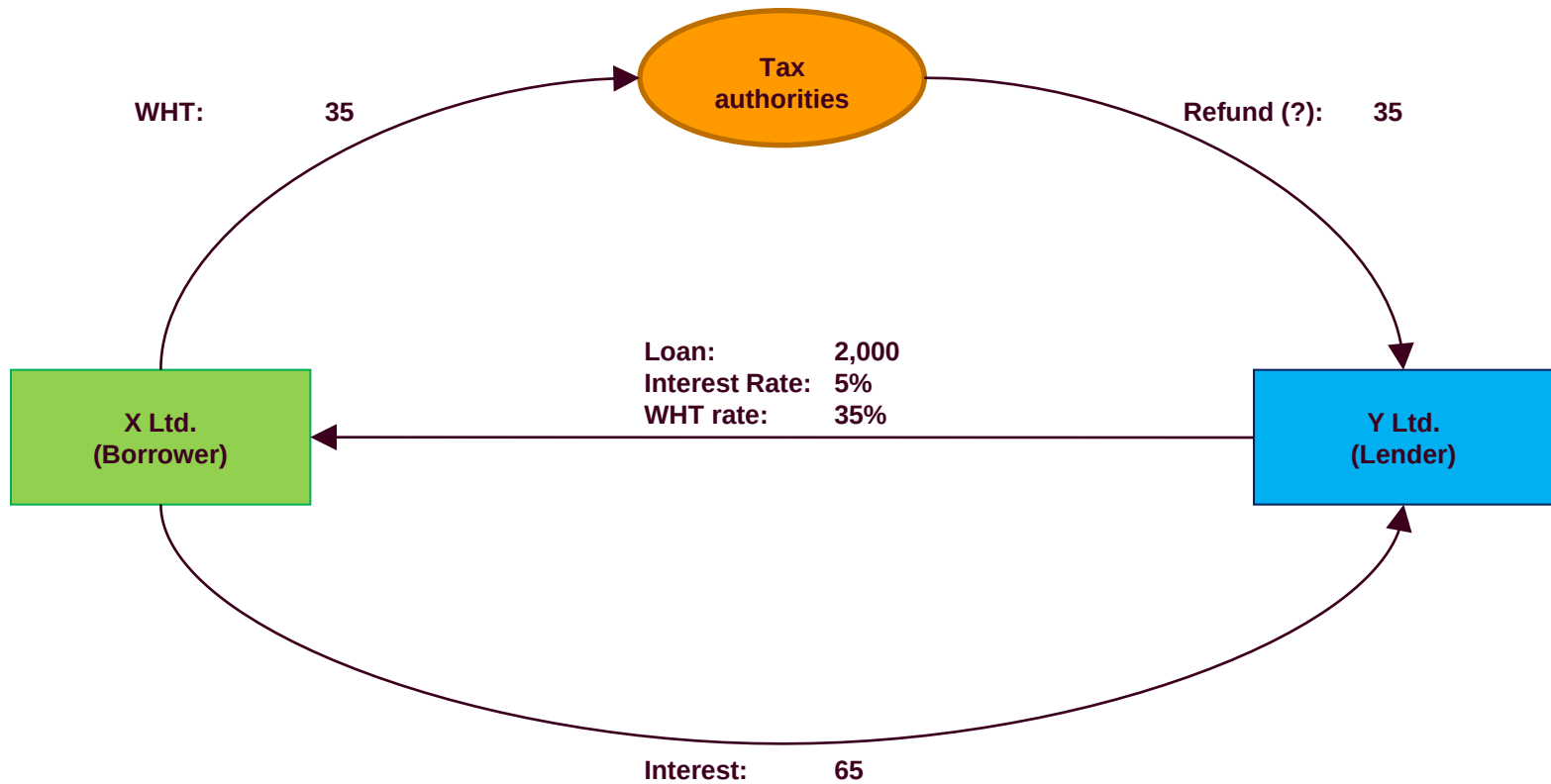
Article 20 Ordinance of the Takeover Board on Public Takeover Offers (UEV)

- 1. The offer prospectus shall contain the essential details of the financing of the offer as well as confirmation from the review body that the offeror has taken the necessary measures to ensure that the required funds are available on the implementation date.*
- 2. If securities offered in exchange are not yet available, the review body must confirm that the offeror has taken all the necessary measures to ensure that the securities are available on the implementation date.*

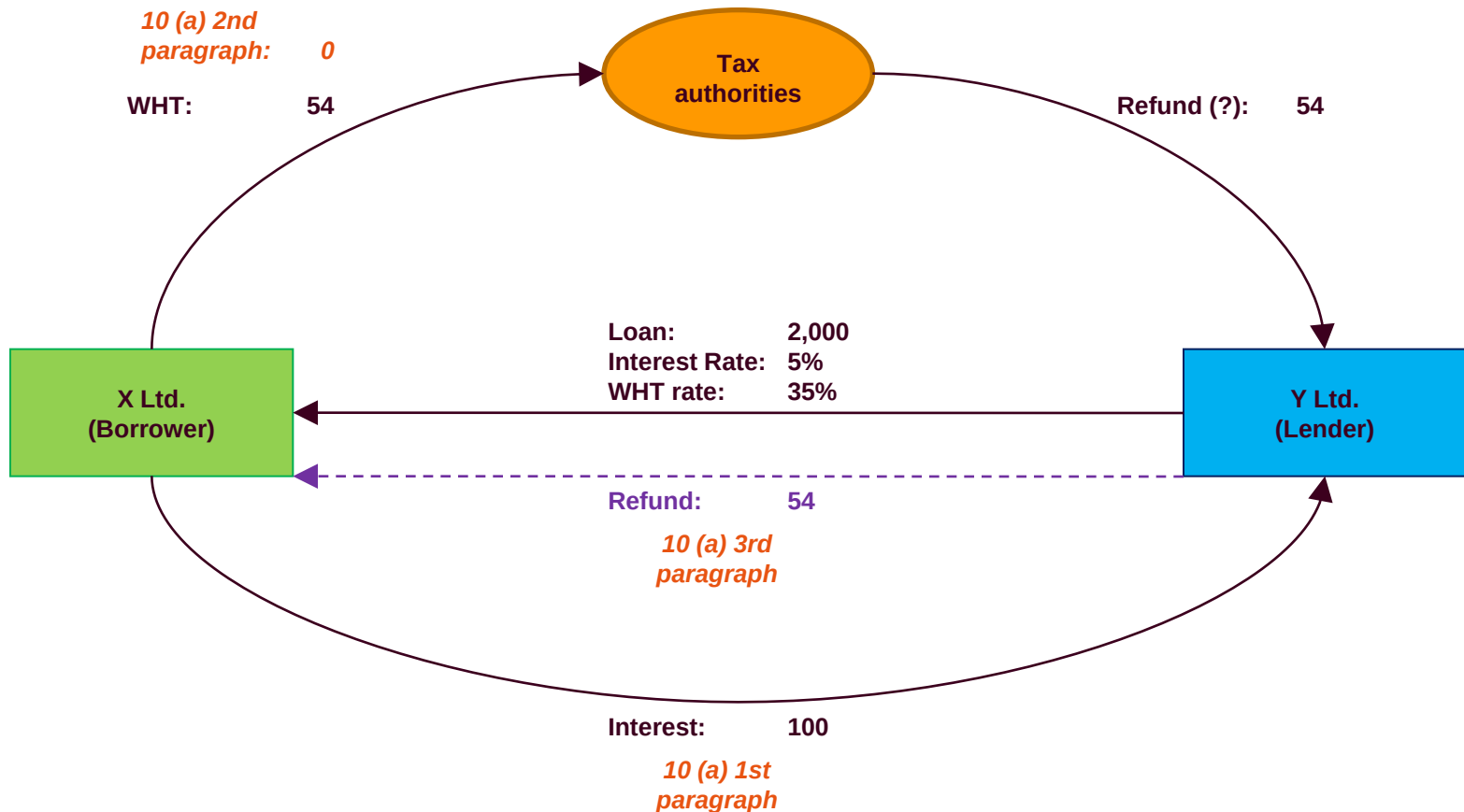
Withholding tax on interest...

- » ...is levied in many countries (e.g. France, UK, USA, etc.)
- » ...depends on the specific finance transaction
- » ...may amount to up to 50% of interest paid
- » ...is payable by the borrower
- » ...is normally refundable to the lender based on domestic law or double tax treaty

Modus operandi: Standard situation



Modus operandi: Gross-up according to Clause 10



Clause 10 (a) 4th paragraph, (b), (c) and (d)

- » These clauses specify that the Lender shall receive the agreed interest notwithstanding any taxes other than income tax on interest received
- » The Borrower shall indemnify (reimburse) any such taxes to the Lender

Credit Support: Collateral / Guarantees

- » Share pledge (acquirer)

- » Account pledge (acquirer)

- » Guarantees (upstream v. downstream/cross stream)

 - Enforceability (financial assistance rules : § 71a AktG / capital protection rules: freely distributable equity)

 - » Tax issues

- » Pledge of target assets: -→ upstream securities

Buzzwords

- » Finance Documents
- » Default vs. Events of Default
- » Obligor / Group
- » MLA

Thank you for your attention

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