

# Private Acquisitions Notes

## SGS 1: AUCTION SALE

### 1. How does the auction process actually work and how does it differ from a normal private treaty sale?

private treaty sale- only one buyer

auction sale- Process of witting down the buyers to the one seller wants to engage with

Def: Auction sale, which involves the seller seeking bids for the target company or business from several prospective buyers in a competitive tender process.

### 2. What would be the advantages and disadvantages of selling Eurolearn in this way, both for ourselves and for the potential purchasers?

#### Advantages of auction sales for us (sellers)

- The seller can usually **reach a larger pool of potential buyers** through an auction process.
- The competitive process **maximises the price** by encouraging potential buyers to bid against each other
- Enable the seller to **secure better sale terms** than might be achieved on a bilateral sale. The seller also has the advantage of being able to run **simultaneous negotiations with more than one bidder**, thus allowing it to defer committing to any one bidder until the principal deal terms have been settled.
- The **seller controls the due diligence process**, including the number and scope of the documents it will share with participating bidders, and the time they have to complete their investigation into the target company or assets.
- The **seller can control the transaction timetable**, in particular to reduce the time it takes to proceed from agreement in principle to completion of the sale

#### Disadvantages of auction sales for sellers

- **Not all businesses are suitable for sale by auction.** If the market sector is limited and there are only one or two potential buyers, an auction may not be appropriate.
- An auction may also be **inappropriate where the structure of the target business is particularly complicated, or where there are significant external factors affecting the transaction** (such as regulatory or competition issues, or material third party consents).
- The **seller's transaction costs are usually higher** than in a bilateral transaction.
- **significant management time commitment** by the seller (and, in the case of a share sale, the target company).
- Some bidders may not be serious about acquiring the target business and are **interested only in finding out information about a competitor.**

#### Key drawbacks of an auction process from the bidder's (buyer's) perspective include:

- It may be forced to pay a **higher price** for the target business than it might have done had it been the only suitor.
- The presence of other bidders reduces its chances of concluding a successful deal, thereby **increasing its risk of wasting management time and professional fees on an abortive deal.** It is therefore

important for bidders to keep a tight control over the costs they incur in participating in the auction process.

- Bidders are likely to receive more **limited due diligence information** about the target business than on a typical bilateral transaction, thereby increasing the transaction risk they are assuming.
- The level of **warranties, indemnities and other contractual protections** given by the seller in an auction sale is **likely to be lower** than on a typical bilateral sale.
- Bidders will have **less opportunity to build relationships with the target's management** before the transaction completes.
- There is a **greater risk of damage being caused to the target's business** due to news of the sale getting out before the auction process has concluded.

### **Smith New Court Securities Limited v Scrimgeour Vickers (Asset Management) Limited**

While the seller or its financial advisers may be tempted to overstate the degree of interest or terms offered by other bidders with a view to maximising competitive tension, doing so could give rise to liability for fraudulent misrepresentation

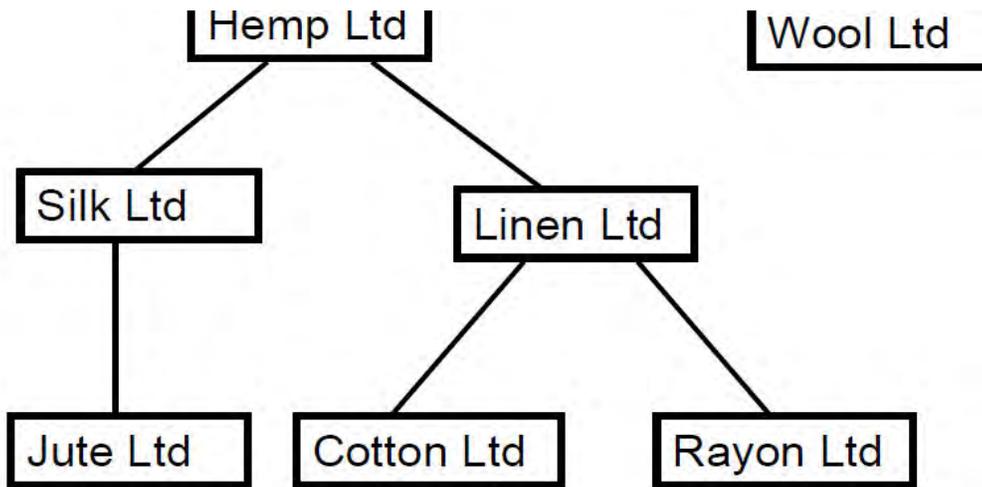
#### **1. Why might Eurolearn want to be able to rely on the terms of the Confidentiality Agreement? Is it able to do so?**

2 ways of allowing a party to rely on the document

- Making them a party to the agreement (Eurolearn is not a party to the agreement only LTC is a party and LTC would have no interest in enforcing this agreement)
- Another way is ensuring Eurolearn has third party rights

#### **2. How long should the period in clause 4 be?**

- Important if bidder is unsuccessful
- Indefinitely/[x] number of years from date of agreement



- 1) If Jute is sold to Wool, who will receive the sale proceeds?
- 2) If Linen is sold to Wool, what will happen to Cotton?
- 3) If the business of Cotton is sold to Wool, who will receive the sale proceeds?
- 4) If the business of Linen is sold, what will happen to Cotton and Rayon?
- 5) Jute is being sued by one of its suppliers. If Jute is sold to Wool, what will happen to this litigation?
- 6) How would your answer to question 5 differ if the business of Jute is sold to Wool instead?
- 7) If Cotton is sold, what will happen to Cotton's employees?
- 8) If Rayon's business is sold, what will happen to any real property Rayon owns?
- 9) What will happen if Wool buys the entire issued share capital of Hemp?

- 1) Silk Ltd (It would have to pay corporation tax on it and buyer would have to pay stamp duty).
- 2) Cotton's direct ownership does not change but it's ultimate ownership will
- 3) Cotton, shareholders would then have to extract it through dividend or liquidation
- 4) Depends on what has been agreed with the buyer.
- 5) litigation would continue against Jute but since the buyer buys shares in Jute, indirect concern to the buyer
- 6) litigation would still remain with Jute but in this case not a concern to buyer since buyer can opt out of choosing the litigation and only pick the assets it wants
- 7) Employees remain with Cotton, Cotton as a co. is sold to the buyer
- 8) depends on the agreement with the buyer
- 9) The Buyer wool would become the parent co. of the whole group

## Case Study: What might attract a buyer?

- **Strong brand name**
- **Client list and data base**
- **Innovative new product – skills and cultural awareness training**
- **Good cash flow – many clients pay in advance**
- **Strong management team – keen to expand**

### Locked box mechanism

It should be noted that as an alternative to using completion accounts to adjust the purchase price, a mechanism called a '**locked box**' may be used. Instead of setting the purchase price by reference to completion accounts, the parties may agree to use accounts that have been previously drawn up (the 'locked box accounts').

### Part (a) identify the key differences between a sale by way of auction and a private treaty sale.

main differences to be in relation to the following: (i) the number of bidders; (ii) the due diligence process; and (iii) who is responsible for drafting the documents and identified what those differences were.

### Part (b) identify the preliminary documents relevant to an auction sale as well as the purpose of each document.

Students were required to identify the confidentiality agreement: required to protect the knowhow of the business being sold; the information memorandum: required to provide information on the business to the bidders; the process letter: required to provide information to the bidders on how to make their bids; and indicative bids: the way by which bidders will detail the terms on which they are prepared to buy the business. This '**process letter**' will set out the process for the auction, including a list of details the bidders have to provide to the seller in their *indicative bids*, which can assist the seller in its analysis of which bidders are more committed to the acquisition.

### MCQ

Price Prior's client, Shakers Movers Limited ('Shakers'), wants to sell its subsidiary Tarrants Limited ('Tarrants'), which runs a residential removals business. Shakers' financial adviser has identified a number of companies that might be interested in buying Tarrants (the 'Potential Buyers') and therefore has suggested that Shakers should consider running the sale as an auction. Shakers sold another of its subsidiaries last year by way of private treaty sale and has asked for advice on the auction process. Which of the following statements should you include in your advice?

- An auction process is likely to be cheaper for Shakers than a private treaty process because in an auction it is normal for the Potential Buyers' solicitors to be responsible for preparing the first draft of all the main acquisition documents.
- Selling by way of auction will ensure that Shakers obtains a higher price for Tarrants than if it sells by way of private treaty.
- In an auction sale, the Potential Buyers will conduct their due diligence on Tarrants via a data room rather than by supplying Shakers with a questionnaire and expecting responses to that questionnaire.