



UIA 8th Winter Seminar

Legal Challenges and Impacts of Financial Crisis

M&A with Distressed Companies
Structuring Issues and Pitfalls

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Introduction (1/2)

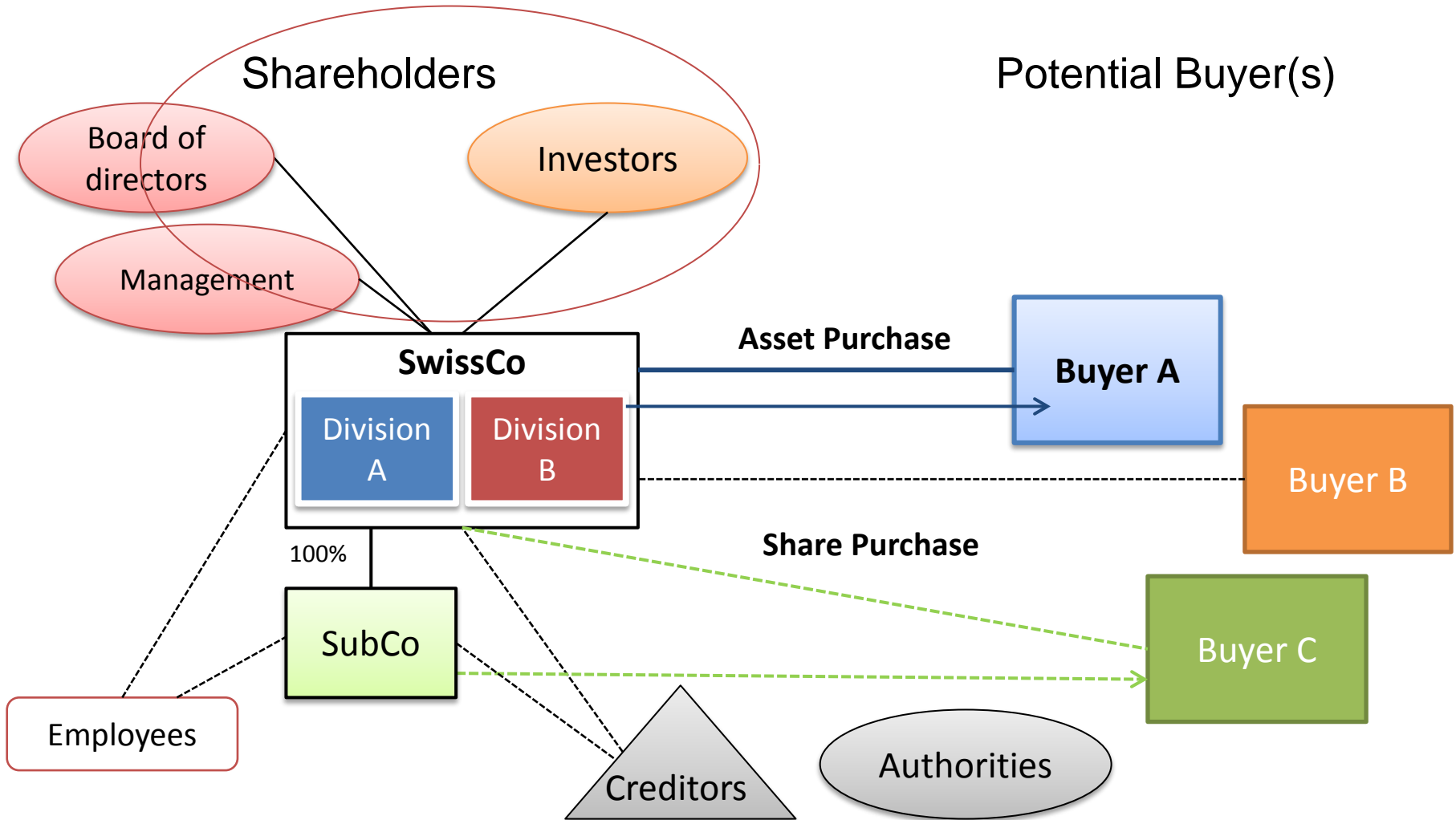
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Introduction (2/2)

- Companies in financial distress
 - What is financial distress?
- Distressed M&A
 - Does financial distress impact an M&A deal?
 - Which additional considerations apply?
 - Who is exposed in a distressed M&A deal?
 - Structuring issues and precautions taken in practice
 - a. Seller's precautions, taken by its board of directors / management
 - b. Buyer's precautions, as buyer of distressed company or business
 - What are the crucial points for outside counsel?
- Comparative view
 - How do other jurisdictions address distressed M&A?

Case Study – The Facts (1/2)



Case Study – The Facts (2/2)

- SwissCo is a share corporation
- SwissCo faces financial difficulties
 - Board of directors considers / evaluates options:
 - Financial restructuring (recapitalization, operational measures, etc.);
 - Divestiture of Division B with related assets, liabilities, contracts, employees (asset deal) or sale of SubCo (share deal).
- Informal talks with potential Buyers
- Parties seek advice on appropriate structuring of transaction and process with the aim of limiting risks

Distressed M&A – Particulars (1/2)

- SwissCo - financial distress situation
 - Business, strategic and operational perspective
 - Legal perspective / criteria
 - illiquidity situation
 - loss of capital situation
 - (threatened) over-indebtedness

- Risk of bankruptcy, moratorium or similar procedure
 - Need for a forward-looking focus (creditors' / administrator's view)
 - relevance for process, structuring and pricing of M&A deal

Distressed M&A – Particulars (2/2)

- Arguments of creditors / administrator / shareholders
 - Violation of fiduciary and other statutory duties
 - Inadequacy of consideration
 - Favoring of creditors by use of proceeds
 - Favoring of creditors through (unusual) deal structure

- Legal means to enforce potential claims
 - Challenge validity of M&A transaction
 - Claw-back claims (avoidance actions, actio pauliana)
 - Director's liability
 - Criminal charges

Seller's Side – Considerations (1/3)

- Negotiation and approval of M&A deal
 - Preparation and negotiation of structure and terms
 - Board of directors
 - Delegation of parts to a committee or to executive management
 - Approval of transaction
 - Board of directors
 - Shareholders' approval if transaction leads to change of company's purpose and/or to a de facto (partial) liquidation
- Approvals and third party consents (e.g. authorities, creditors, contract parties)

Seller's Side – Considerations (2/3)

Duties of Board of Directors

- Ultimate management and oversight, financial planning
- Fiduciary duties
 - Safeguard interests of the company
 - Proper structuring and process of M&A deal
 - Aim to achieve highest price / fairness of price
 - Alternative buyers, auction process
 - Valuation, fairness opinion
 - Duty of loyalty: avoid or properly address conflicts of interest
- Special duties in financial crisis
 - Duty to analyze financial status, to propose financial restructuring measures and, in a worst case, to notify bankruptcy judge
 - Equal treatment of creditors

Seller's Side – Considerations (3/3)

- Avoid or mitigate risk of claw-back claims
 - Type of avoidance actions under Swiss bankruptcy law
 - Voidability of gifts or transactions not at arm's length
 - Voidability due to insolvency
 - Voidability for intent
 - Claimant: bankruptcy estate or creditor(s) of SwissCo
 - Respondents: Buyer of business or shares or other party otherwise benefitting from transaction
 - Suspect period(s)
 - Consequences: unwinding of transaction
- Pre-transaction financial restructuring
- Other aspects (e.g. tax, employee matters)

Buyer's Side – Considerations

- Focus of due diligence review
 - Regular dd review topics
 - Financial situation of Seller
- Deal structure and purchase agreement
 - Request corporate approvals from Seller
 - Request financial restructuring
 - Staggered purchase price payment
 - Asset deal vs. share deal
 - Depending on financial status of Seller
 - Limit acquisition to assets (e.g. shares of SubCo)
 - No set-off of claims in lieu of payment of purchase price in cash
- Other precautions



Critical situations / pitfalls

Critical situations (examples)

- Seller is faced with (threatened) over-indebtedness
 - Need for financial restructuring
 - Immanent risk of favoring creditors (e.g. asset deal with liability transfer)
- Fast „fire“ sale
 - Risk of inadequacy of price
 - Risk of inadequate M&A process (e.g. due to timing, other constraints)
- Debt / asset swap transaction
 - SwissCo sells assets to a Buyer (also a creditor) and purchase price is not paid in cash, but by set-off of claims
 - Risk of favoring creditors
- Bankruptcy or moratorium procedure is inevitable and initiated
 - Seller's scope of action changes and additional rules apply
 - Involvement of administrator, bankruptcy or moratorium judge

Discussion

- Distressed M&A deals involve cross-over legal topics and require careful analysis
- Financial distress adds complexity to M&A deals
- Common topics in different jurisdictions

Contact

Thank you for your attention

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