Private Treaty M&A Dictionary

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Important notices

Contents


10.74
12.54

Foreword

Mergers & Acquisitions (M&A) has, like many areas of specialty, a lexicon all of its own. The use of technical jargon can, and is sometimes intended, to overwhelm those new to the field. The purpose of this dictionary is to provide users with clear and simple explanations of the meanings of many commonly used terms in unregulated sale and purchase transactions in Australia. For reasons of brevity, it is outside the scope of this dictionary to discuss the many and varied nuances of numerous terms. Also, this dictionary does not, and is not intended to, define terms used in transactions that are regulated by statute law, such as takeovers and schemes of arrangement, although many terms that are defined in this document have the same or similar meanings in a regulated context.

I hope that you find this dictionary useful. If you have any questions or comments, or requests for new definitions, I would be delighted to hear from you.

Jonathan Cheyne

Partner

Private Treaty M&A Dictionary

ACCOUNTING STANDARDS: The accounting rules that businesses and entities who are governed by them must apply in recording financial transactions and preparing financial reports. In Australia, the Accounting Standards are promulgated by the Australian Accounting Standards Board and are known as A-IFRS (see separate definition). These are the standards that apply under the Corporations Act. The Accounting Standards may not always apply in a particular case: not every form of business entity is required to apply the Accounting Standards; there may be alternative accounting treatments available under the Accounting Standards; or different interpretations of a particular standard. It is therefore common to specify in a sale document, in order of precedence, the accounting rules to be applied for the purposes of preparing accounts or determining balances under the sale documentation. For example, the sale documentation might provide that the Accounting Standards to be applied in the following order of precedence: AIFRS; interpretations approved by the Australian Accounting Standards Board, the requirements of the Corporations Act relating to the preparation and consent of financial reports and, to the extent a matter is not covered by the preceding rules, generally accepted accounting principles, policies and procedures applied from time to time in Australia by entities similar to the Target. If accounting rules different from those applicable under a general definition of Accounting Standards are to applied, these will usually be specified in Agreed Accounting Principles.

AGREED ACCOUNTING PRINCIPLES: A set of accounting rules agreed between the parties to a sale transaction to be used when calculating either balance sheet or EBIT/EBITDA items for the purposes of Completion Accounting adjustments or Earn-out calculations. They are particularly relevant where the accounting treatment is, or may, differ from the requirements of the Accounting Standards or where the Accounting Standards permit more than one approach (each of which may have very different accounting consequences) or where a departure from the Accounting Standards, a generally accepted approach or past practice has been negotiated. The Agreed Accounting Principles are typically set out in a schedule to the sale document.

AGREEMENT (1): A legally binding Contract between parties for which the basic requirements of contract – offer and acceptance, intention to create legal relations and consideration – have been satisfied.

AGREEMENT (2): Often used loosely to refer to a legally binding arrangement between parties, the terms of which arise under a contract or pursuant to a Deed. In this context no distinction is made between the different legal forms of sale documentation.

A-IFRS: Australian equivalents to International Financial Reporting Standards, the Accounting Standards issued by the Australian Accounting Standards Board, which are similar but not in all cases identical to the International Financial Reporting Standards (IFRS). Because of differences between A-IFRS and IFRS, great care is required when specifying which standards are to be applied when preparing accounts for Completion Accounting or Earn-out accounting purposes, particularly if AIFRS is not to be applied. This is because different accounting rules can have significant financial consequences.

ASIC: Australian Securities & Investments Commission, Australia's corporate regulator.

ASSET SALE: A means of structuring a sale of a business pursuant to which the assets comprising the business are transferred to the Buyer. Except to the extent expressly agreed, the Buyer will not assume any liabilities of the Sellers and will only acquire those assets specifically agreed. In an asset sale, any employees of the business who are to remain engaged in the business will need to have their employment with the Seller terminated and be re-employed by the Buyer (or a related entity). In an Asset Sale there can be multiple Sellers and multiple Buyers. Stamp Duty will be payable on the transfer of certain assets. Contrast: Share Sale.

ASSIGNMENT: Under the law of contract, a party can transfer (or assign) its rights under a contract but not its obligations, without the consent of the counterparty. This is the case unless the contract prohibits assignment or imposes conditions on assignment (such as consent). While statue law has modified the operation of the common law rules of assignment, it remains the case that if, in a contract originally between party A and party B, it is intended that party C is to replace party B, with party C to assume the rights and obligations of party B under that a contract, a Novation is necessary.

BACKGROUND: An explanation, usually at the front of a document, that explains in simple and plain language the purpose and intended effect of the document, together with some of the relevant history. The Background is not usually intended to be legally binding but has, as its purpose, providing context for a reader not familiar with it. Also called Recitals.

BOLT-ON: An acquisition of a business that is similar or complementary to the acquirer's existing business. Usually a "bolt-on" refers to a business that is materially smaller than the acquirer's existing business.

BSA: Business Sale Agreement.

BUSINESS SALE AGREEMENT: Agreement used for an Asset Sale. Contrast: Share Sale Agreement.

BUYER: A party who is purchasing an asset. Synonymous with Purchaser.

BUY SIDE: A reference to advisers (financial and legal) acting for a prospective purchaser.

CA: see *Confidentiality Agreement.*

CAP: A reference to a maximum amount that may be payable where the amount payable may be variable. For example a party's liability for something (e.g., under an Indemnity for breach of a Representation and Warranty) may be capped or the amount payable under an Earn-out may be capped. Contrast: Floor.

CASH FREE/DEBT FREE: It is common for a business to be sold on a cash free / debt free basis, meaning that the Purchase Price is calculated on the basis that the assets of the business or entity will include zero cash (avoiding the need for the Buyer to pay the Seller cash for cash in the Target) and on the basis that the business or entity is completely ungeared (i.e., zero debt). It is usually not possible to ascertain with precision on the Completion Date whether this objective has been completely achieved. Accordingly, the sale documentation will usually include an adjustment mechanism so that if the Completion Accounts (showing balances of cash and debt) indicate that there is positive net debt (debt less cash), the Seller must refund this amount to the Buyer or, conversely, if there is a cash surplus, the Buyer must pay an additional amount equivalent to the surplus to the Seller.

CGT: Capital Gains Tax. Tax payable by a Seller on the capital gain (assessable consideration less the cost base for tax purposes) of the asset being sold.

CHANGE OF CONTROL: A change in who controls (either directly or ultimately) a business or entity. The concept of "control" is defined in the Corporations Act (see section 50AA) although an expanded notion of control, and therefore what constitutes a change in control, is often used in commercial agreements. As the identity of a counterparty can be a key, if not fundamental, feature of many commercial arrangements, it is often important to protect against an effective change in the identity of a counterparty. Direct changes in the identity of a counterparty can be restricted through prohibitions on the assignment of rights under a contract. A Change of Control clause can be used to protect against indirect changes in the counterparty – i.e., where the counterparty (as a legal entity) remains the same, but those controlling it change by providing , for example, that the party not in breach may terminate the arrangement if their prior consent to the change is not obtained.

CLOSING: The US term for Completion. Commonly used in financing transactions.

COLLAR: A reference to a situation where money is or may be payable (e.g., under an Earn-out) and the amount payable is subject to both upper (Cap) and lower (Floor) limits, such that it must be within a range.

COMPETITIVE PROCESS: A sale process in which the Buyer seeks offers from more than one prospective purchaser. The objective of a Competitive Process is to increase "competitive tension" between prospective purchasers with a view to maximising the price that they are prepared to pay and otherwise achieving the best sale terms for the Seller.

COMPLETION: The transfer of ownership (of assets in an Asset Sale, or shares in a Share Sale) from Seller to Buyer. Also used to refer to the process by which this occurs.

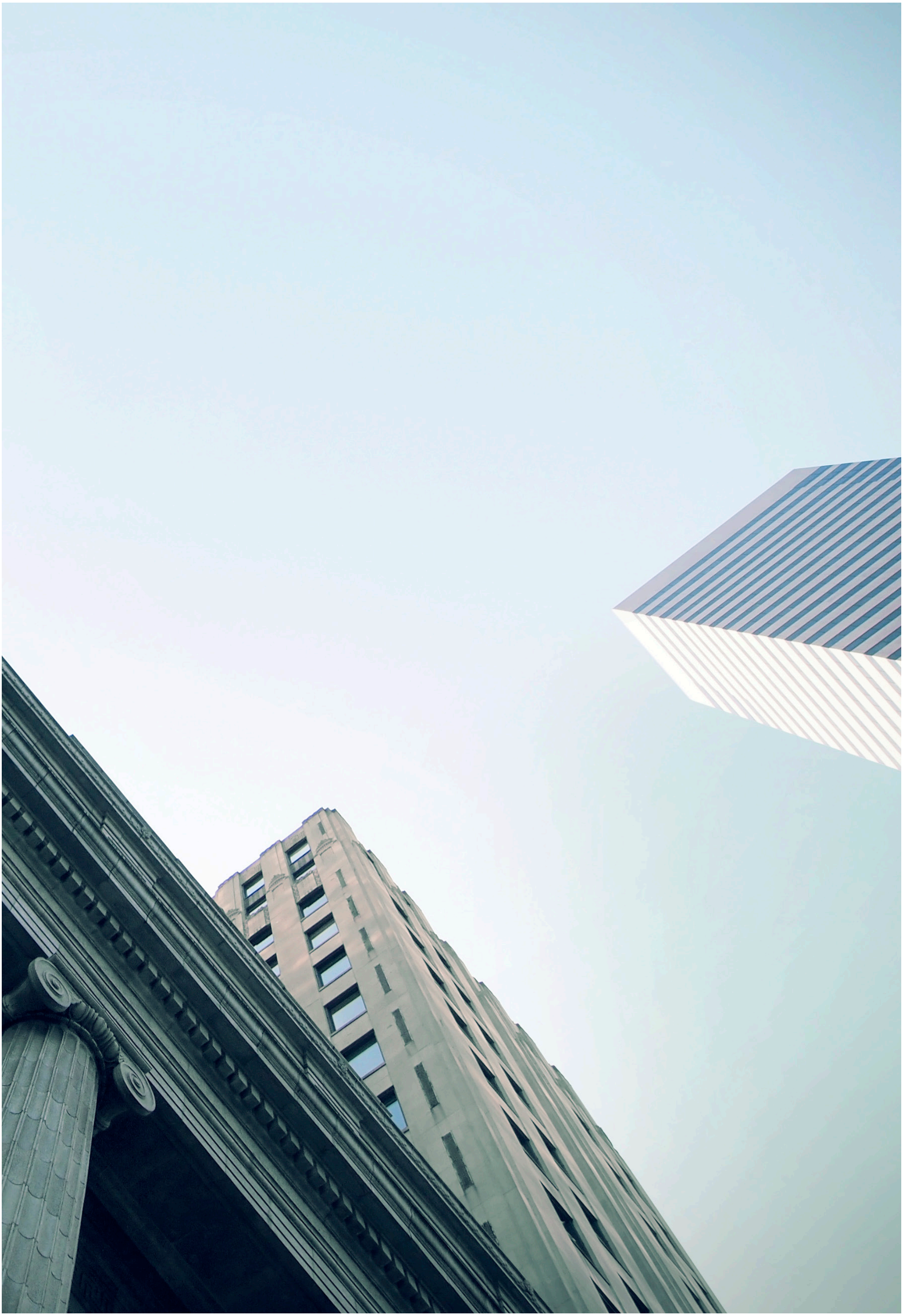
COMPLETION ACCOUNTS: Accounts that are prepared Post-Completion in respect of the target business or entity for the purposes of determining the balances of agreed items, such as Working Capital or Net Assets. Completion Accounts are usually necessary because the Purchase Price for a business or entity frequently includes an agreed amount of Working Capital or Net Assets. As it is not generally practicable or desirable to cease trading in advance of Completion occurring to enable the precise calculation of these amounts as at the Completion Time to be determined, it is easier to Complete based on estimated balances and then post-Completion prepare accounts that set out the final balances as at the Completion Time. If there is a net difference between the actual and estimated balances of the items taken into account in determining the Purchase Price then an adjustment will be payable by one party or the other. For example, if the parties determined the Purchase Price on the basis that Net Assets would be $10 million, and in fact they were $11 million, then the Purchaser has acquired a business or entity with $1 million more of Net Assets than was assumed. Commonly it would therefore need to pay the Seller for these additional assets (i.e., pay a further $1 million).

COMPLETION DATE: The date scheduled for Completion. Note that Completion occurs at a point in time, not on a day. See Completion Time.

COMPLETION TIME: The point in time at which Completion occurs.

CONDITION PRECEDENT (TO COMPLETION): A condition that must be satisfied or a circumstance or state of affairs that must (or must not) exist before Completion can occur. A Condition Precedent can be expressed in the negative: e.g., the sale document might provide that it is a Condition Precedent that no Material Adverse Event (MAE) has occurred. A Condition Precedent for Completion is structured so that a legally binding arrangement exists when the sale document is signed and terminates (or is terminable) if the condition is not satisfied or waived by a pre-determined “Sunset Date”. A Condition Precedent may be for the benefit of one or more parties to the sale document. Where a CP is for the benefit of a party it will typically have the right to rely on the failure of that Condition Precedent to terminate the arrangement.

CONDITION PRECEDENT (TO FORMATION): A condition that must exist or be satisfied before a legally binding agreement for sale and purchase can exist. This may be necessary for example, if a foreign investment authorisation is required as the foreign investment rules prohibit parties from acquiring or to acquire shares or assets if an approval is required, and that approval has not been obtained or ceases to be required. This means that if the condition is not satisfied, no contract comes into existence.



CONDITION SUBSEQUENT: This is a condition or requirement that must be satisfied after Completion has occurred. If the Condition Subsequent is not satisfied the parties may be required to "unwind" the transaction. Conditions Subsequent are not often used because of the issues of undoing what has already been done.

CONSIDERATION: In contract law, the amount paid or given in return for a contractual promise. Consideration need not be money – it might include the assumption of an obligation or the proffering of something else of value. In the business or share sale context, Consideration is typically a synonym for the Purchase Price.

CONFIDENTIALITY AGREEMENT/DEED: An Agreement or Deed pursuant to which the parties to the document agree to keep specified information confidential for an agreed period (or indefinitely). A Confidentiality Agreement/Deed will also typically set out the use that may be made of confidential information provided under the document (often referred to as the "Disclosure Purpose") and the other conditions with which the recipient of that information must comply: e.g., when information provided must be returned or destroyed, when it can be retained, what reliance can be placed on that information and the consequences if confidential information is disclosed in breach of the applicable terms of disclosure. Also called a Non-Disclosure Agreement or NDA.

CONTRACT: A legally binding agreement between parties in respect of which the basic legal requirements of offer and acceptance, and intention to create legal relations and Consideration are satisfied. Contrast: a Deed.

CORPORATIONS ACT: The *Corporations Act 2001* (Cth), the Commonwealth legislation that regulates companies.

COVENANTOR: A covenant is an obligation assumed by a party under a Deed and a Covenantor is someone who makes or assumes a covenant. In private treaty M&A a Covenantor usually more loosely refers to someone (other than the Seller) who has given a representation or warranty in favour of the Buyer. This may be desirable, for example, if the Seller has limited financial means and there are other parties with greater financial resources, and who have a detailed knowledge of the Target's affairs, or aspects of them, who the Buyer would like to be able to claim against if a representation or warranty is breached (e.g., shareholders or controllers of the Seller).

CP: see *Condition Precedent.*

CURRENT ASSETS: A technical accounting term, defined in Accounting Standard AASB 101 to mean an asset that is expected to be recovered no more than twelve months after the reporting period. Contrast: Non-Current Asset.

CURRENT LIABILITIES: A technical accounting term, defined in Accounting Standard AASB 101 to mean a liability that is expected to be settled no more than twelve months after the reporting period. Contrast: Non-Current Liability.

DD: see *Due Diligence.*

DATA ROOM: Either a physical or, more commonly, an electronic, repository of documents concerning a target business or entity that is compiled by the Seller and its advisers for the purposes of allowing prospective purchasers to undertake Due Diligence. A Data Room may contain information across a range of areas including corporate records, accounting, employment and HR, property (owned and leased), financing, contracts, supply arrangements, IT, IP, insurance, litigation and others.

DEED: A means by which parties can legally bind themselves to an arrangement or obligation without the need for Consideration (which is a requirement for a Contract). A Deed must be in writing (contrast a Contract, which need not be) and has formal execution requirements. Deeds differ from Contracts in other respects also. For example, without contrary words, a party is immediately bound by their Deed upon signing and delivering it even if the other party has not done so and have a longer Limitation Period.

DEFERRED CONSIDERATION: A portion of the Purchase Price the payment of which is deferred to a point in time Post Completion. Deferred Consideration is usually a fixed amount – i.e., the amount of Deferred Consideration does not change and is not (unlike an Earn Out) contingent on the future performance of the target business or entity. In contrast to a Retention, the obligation to pay Deferred Consideration is usually not subject to conditions, although a Buyer may (depending on the terms of the sale document) be able to deduct from Deferred Consideration the amount of a Set-Off owing by the Seller to the Buyer (e.g., money owing by the Seller for breach of a Warranty or Representation or a Completion Adjustment). Contrast: Retention.

DEPOSIT: An amount of money that may be payable by a Buyer (or a related party) on execution of sale documentation. A Deposit represents security for the Buyer against a Seller default. A Deposit may be required if the Seller has concerns about a Buyer's financial capacity or willingness to Complete (and therefore wants some security for its costs). Deposits are not common in larger deals.

DISCLOSURE LETTER: A letter provided by the Seller at or before the time of execution of the sale documentation that sets out any matters that would constitute a breach of a Representation or Warranty given by the Seller. Under a typical sale document the Buyer cannot sue the Seller for breach of warranty in respect of a matter that has been fairly disclosed in the Disclosure Letter.

DUAL TRACK PROCESS: A sale process in which a Seller simultaneously pursues two potential avenues for selling its stake in the subject business or entity. A typical Dual Track Process would involve simultaneously running a Competitive Process and preparing for an IPO.

DUE DILIGENCE: A process that may be undertaken by Buyer or Seller. In the case of Buyer Due Diligence, the purpose is to test that key assumptions made concerning the business or entity (e.g., as to sales and earnings potential, capability etc) are correct and to identify any key risks or issues that may be relevant to a decision by the Buyer whether or not to proceed with the acquisition or that may affect the price or terms upon which it is prepared to do so. Due Diligence will frequently be conducted across a range of disciplines including accounting, tax, legal, insurance, environmental, commercial and cultural. For Due Diligence undertaken by Sellers, see Vendor Due Diligence.

DUE DILIGENCE QUESTIONNAIRE: A questionnaire prepared by or on behalf of the Buyer that is provided to the Seller and/or management of the target business or entity requesting information in each of the areas in respect of which Due Diligence is being conducted. It is intended to elicit relevant information and to provide a basis for legal redress in the event that the responses to the questionnaire are incorrect or misleading or deceptive, whether by inclusion or omission. It is common for legal and financial advisers to prepare separate Due Diligence Questionnaires.

DUE DILIGENCE REPORT: A report that sets out the findings of the due diligence exercise. A report may be an “exceptions” report that sets out only major issues or may be a full report which, in the case of a report commissioned by a Buyer, may include a summary of all material legal arrangements in place in connection with the target business or entity.

EARN-OUT: A method of paying for a business under which the payments to the Sellers depend in whole or in part on the performance of the target business or entity over a future period of time. A typical Earn-out will comprise an upfront payment of part of the Purchase Price with the balance contingent on relevant performance conditions being met. These conditions commonly include the business meeting minimum EBIT/EBITDA thresholds.

EARN-OUT PERIOD: The period over which the Earn-out mechanism applies. A 12 month Earn-out Period means that the financial performance of the business or entity being sold will be measured over a period of 12 months from Completion (or some other agreed starting point), and the Earn-out component of the Purchase Price determined based on that performance.

EARN-OUT PROTECTIONS: Contractual restrictions required by the Seller on the way in which the Buyer of a target business or entity can run that target business or entity during the Earn-out Period. They are designed to preserve the capacity of the target business/entity, and the Seller (if they are to have an ongoing role in management), to generate earnings and to prevent the Buyer from taking action that might be in the (longer) term interests of the Buyer but that will have a negative effect on the earnings of the target business or entity, (e.g. transferring business to another entity in the Buyer group or increasing long-term staff incentives or paying short term bonuses to staff etc). It may be in the Buyer's interests to increase costs or reduce revenue during the Earn-out Period because an Earn-out is generally based on a multiple (e.g., 4 times) earnings. If a multiple of 4x is payable a $1 increase in expenses will result in a $4 reduction in the Earn-out payable all other things being equal. There can therefore be strong incentives for Buyers to take actions that are, in the short-term, to the detriment of the target business or entity's earnings so as to reduce the amount of the Earn-out.

EBIT: Earnings before interest and tax (a proxy for the earnings of an ungeared business). EBIT is not defined in the Accounting Standards and care is therefore required to ensure that the component parts (earnings, interest and tax) are all appropriately defined in the sale documentation.

EBITDA: Earnings before interest, depreciation, amortisation and tax (a proxy for the cash generating capacity of a business, assuming no capital expenditure is required). Like EBIT, EBITDA does not have a defined meaning in the Accounting Standards and care is therefore required to ensure that the component parts (earnings, interest, tax, depreciation and amortisation) are appropriately defined in the sale documentation.

EFFECTIVE DATE/EFFECTIVE TIME: Used when the ownership of the target business or entity is to notionally change hands at a date or date and time different to the Completion Date. For example, parties may Complete a sale and purchase on 1 December but agree that the Effective Date for the acquisition is 1 July of the same year. This means that the Buyer assumes the economic risk of the target business or entity from 1 July even though legally they do not acquire ownership until 1 December.

END DATE: see *Sunset Date.*

ENTERPRISE VALUE: The agreed market value of the target business or entity (i.e., how much a Buyer will pay for the Target on a debt free, cash free basis). Enterprise Value can also be expressed as Equity Value plus Net Debt. There are a number of ways in which Enterprise Value can be calculated. Commonly, Enterprise Value is calculated as a Multiple of Maintainable Earnings. For example, if Maintainable Earnings are calculated to be $25 million per annum, and the Multiple applied is 4, the Enterprise Value will be $100 million (4 x $25m). Alternatively, Enterprise Value can be calculated by forecasting the free cash flows of the target business or entity and discounting these by a weighted average cost of capital (WACC). Often both valuations methods are used in a valuation exercise as a cross check.

EQUITY VALUE: Enterprise Value less Net Debt (i.e., the value in the Target belonging to the equity contributors).

ESCROW: An arrangement under which funds, documents or other assets are held by a third party (commonly a legal or financial adviser to one of the parties), on the basis that they will be paid/released to a specified person on the occurrence of a specified event. A simple example of an Escrow arrangement is that the solicitors to the parties may exchange executed sale documents on condition that they will be held by the recipient in escrow, and legally binding obligations will not arise between the parties, until, for example, a payment is made. A more complex Escrow arrangement may involve an Escrow Agent holding a Deposit or a Retention on the terms of a formal Escrow Agreement or Escrow Deed, which prescribes in detail the circumstances in which the money held by the Escrow Agent are to be applied, the parties' respective rights to direct the Escrow Agent how to act.

EXCLUSIVITY: A prospective Buyer will often seek to reduce the risk that the Seller will sell the business or entity to another party by demanding the right to undertake Due Diligence and negotiate sale terms on an exclusive basis for an agreed period of time. A Buyer may also request the Seller to agree to No-Talk and/or No-Shop restrictions, under which the Seller agrees that it will not, during the Exclusivity Period, discuss the sale of the business / entity with, or provide information concerning the business / entity to, Third Parties (a No-Talk restriction) or approach, seek or invite expressions of interest or proposals from Third Parties (a No-Shop restriction).

EXCLUSIVITY PERIOD: The period during which Exclusivity applies.

EXECUTION: The process of signing an Agreement or Deed, sometimes also called Signing. Completion may occur at this time or later.

EXIT: The means by which the owners of a business or entity realise the value of their investment. The common means by which an Exit may be achieved include a Trade Sale, an IPO, an MBO or a sale to Private Equity.

FATA: *Foreign Acquisitions & Takeovers Act 1975* (Cth). This is the Commonwealth legislation that regulates foreign investment in Australia.

FINANCIAL ADVISER: An adviser to the Seller or Buyer who advises on a range of non-legal matters relating to the transaction. The Mandate for a sell-side adviser may include advising on sale options, vendor financial due diligence, pre-sale restructuring, preparing financial models and accounts, preparing the IM, identifying and contacting prospective buyers, negotiating the Heads of Agreement and commercial aspects of the sale documentation, managing a sale process and assisting with Post-Completion matters. The Mandate for a buy-side adviser may include providing strategic advice, locating potential acquisition opportunities, undertaking financial due diligence, preparing financial models, advising on Purchase Price and other financial matters, negotiating financial aspects of the transaction and managing the acquisition process generally.

FIRB: The Foreign Investment Review Board, which is the Commonwealth Government agency that administers Australia's foreign investment regime. See also FATA.

FLOOR: A reference to a minimum amount that may be payable where the amount payable under a transaction document may be variable. For example, a sale document may provide that the Purchase Price payable will have a minimum (Floor) amount payable and that further amounts may be payable depending on other factors. Contrast: Cap.

GUARANTEE: An undertaking by a Guarantor to guarantee the performance of some or all of the obligations of another person. A Guarantee may be limited to financial obligations (e.g., to pay the Purchase Price, or to pay money owing in respect of a Representation or Warranty or under an Indemnity), or may extend to a Guarantee of the due performance of all of another party's obligations. A party to sale documentation may seek a Guarantee if it is concerned that the party with the primary obligation may lack the actual or financial capacity to comply with the obligations it has assumed.

GUARANTOR: A party who gives a Guarantee.

HEADS OF AGREEMENT: A document that sets out the key terms that the parties negotiating a sale and purchase have agreed will form the basis of the sale and purchase agreement (SPA). Typically a Heads of Agreement will not be legally binding except for certain specific provisions, e.g., clauses relating to confidentiality, Exclusivity and non-competition. A Heads of Agreement may also be referred to as a Term/s Sheet or Memorandum of Understanding.

HOLD-BACK: See Retention. The term may also be used to refer to Deferred Consideration.

IB: Investment Bank.

IM: see *Information Memorandum.*

INDEMNITY: A contractual undertaking by a party to make good the loss of another on the occurrence of a specified event. In the case of a pure indemnity it is not necessary to establish causation: i.e., that the occurrence of the event caused the loss sustained; rather it is merely necessary to show that the event occurred and the loss was sustained. By contrast, in Contract, to be able to recover damages it is necessary to prove a breach of contract, establish loss and establish that the loss is recoverable under the contractual rules relating to damages, which require both causation and foreseeability.

INDICATIVE OFFER: Typically a legally non-binding offer by a prospective Buyer that sets out the Purchase Price the party is prepared to pay, any key assumptions underpinning that offer and any other key terms. In a Competitive Process, a Seller may admit one or more prospective purchasers to the next phase of the process based on their Indicative Offers.

INFORMATION MEMORANDUM (IM): A document usually prepared by the Financial Advisers to a Seller that describes the business or entity that is being sold. An IM is a selling document that is designed to provide prospective Buyers with enough information to determine whether or not they are interested in proceeding further, for example by conducting Due Diligence or putting in an Indicative Offer.

INVESTEE: A term used by Private Equity to refer to an entity in which they have invested.

INVESTMENT BANK: A general reference to (usually large) enterprises whose activities including providing financial advisory services, debt and equity underwriting and trading in financial instruments. For any entity that does not hold a banking authority, or a specific approval from APRA, the use of the word “bank” and “investment bank” is prohibited in Australia. Many Investment Banks hold banking authorities.

IPO: Initial Public Offer. An IPO may involve either or both an offer by the Company of its shares for subscription, or an offer by an existing shareholder of its shares for sale pursuant, to a prospectus prepared in accordance with the requirements of the Corporations Act. An IPO usually also involves the applying to ASX (or another recognised securities exchange) for admission and for the quotation of one or more classes of its securities on the stock exchange operated by ASX.

LEVERAGED BUY OUT (LBO): The acquisition of a target business or entity usually involving either or both management (an MBO) or Private Equity that is heavily reliant on debt to fund the Purchase Price, with the cash flows of the target (from operations and asset sales) the primary (or sole) source of repayment of that debt.

LOCKED BOX: A method of structuring a Purchase Price under which the Buyer agrees to value the target business or entity as at an agreed date prior to the date of signing (the Effective Date), based on a balance sheet as at the Effective Date, and bears the economic risk of the business or entity from that date. Under a Locked Boxed mechanism, although the Buyer bears the economic risk of the business/entity from the Effective Date, they do not gain control until Completion. During this period the Seller is effectively operating the business as the Buyer’s agent. It is therefore important for the Buyer to ensure that no leakages (e.g. payments or transfers of things of value) occur from the Target to the Seller, except as contemplated by the Buyer.

MAC: Material Adverse Change.

MAE: Material Adverse Event.

MAINTAINABLE EARNINGS: The underlying earnings of the Target (usually calculated on an annual EBIT or EBITDA basis) that it is expected the Target will be able to maintain into the future. An assessment of maintainable earnings is usually made having regard to past performance, future upside opportunities and downside risks. To estimate maintainable earnings it may be necessary to make normalisation adjustments – i.e., to adjust for known or expected one-off windfall gains or abnormal losses or other costs or revenues. Such normalisation adjustments may include adjustments to revenue associated from sales to other entities in the Seller group that will not continue post sale, or additional costs imposed by the Seller on the Target that won't continue or be replaced by equivalent charges by the Buyer – e.g., head office charges. Assessing what are the Maintainable Earnings of a Target is a critical aspect of the Buyer's valuation exercise, which requires both skill and judgement and testing the inputs and key assumptions made in this analysis is one of the most important purposes of the Buyer's financial Due Diligence.

MANDATE: As a verb, to engage and, as a noun, the terms of that engagement. Usually used to refer to the appointment (or the terms of appointment) of Financial Advisers. A "buy-side Mandate" is an engagement to advise a prospective buyer. A "sell-side Mandate" is an engagement to advise the Seller.

MBO: Management Buy Out. An MBO involves the management (alone or commonly with the financial backing of others) buying the Target, business or entity. See also Leveraged Buy Out.

MEMORANDUM OF UNDERSTANDING: see *Heads of Agreement.*

MERCHANT BANK: see *Investment Bank.*

MOU: see *Memorandum of Understanding.*

MULTIPLE: A reference to the number by which the earnings of a business or entity (calculated on a particular basis – e.g., EBIT or EBITDA) are multiplied to calculate the Enterprise Value. For example, a business with EBITDA of $10 million that is being valued on a multiple of 4x will have an Enterprise Value of $40 million. The Multiple used to calculate Enterprise Value, and the method of calculating earnings for this purpose, are matters for negotiation.

NDA: Non-disclosure agreement. See *Confidentiality Agreement.*

NET ASSETS: Total Assets (Current Assets plus Non-Current Assets) less Total Liabilities (Current Liabilities less Non-Current Liabilities). Net Assets equals owners' equity: Assets (A) – Liabilities (L) = Owners Equity (OE).

NET DEBT: Total debt less total cash. The constituent components of debt and cash do not have precise or universal definitions.

NON-COMPETE: An undertaking by a party not to compete against a specified business or entity for an agreed period of time in an agreed area. A Buyer will typically request a Seller and parties related to the Seller to agree to a Non-compete to protect the goodwill and earnings of the Target (i.e., to prevent a competitive business being established for a specified period post Completion). The extent and duration of a Non-compete are matters for negotiation although, as they are anti-competitive in nature, such clauses are vulnerable to challenge in the courts unless the restrictions are reasonable and have been given in exchange for something of value. Also called Restraints.

NON-CURRENT ASSET: A technical accounting term, defined in Accounting Standard AASB 101 to mean an asset that is expected to be recovered more than twelve months after the reporting period. Contrast: Current Asset.

NON-CURRENT LIABILITY: A technical accounting term, defined in Accounting Standard AASB 101 to mean an asset that is expected to be recovered more than twelve months after the reporting period. Contrast: Current Liability.

NON-DISCLOSURE AGREEMENT: see *Confidentiality Agreement.*

NORMALISATION: An adjustment that is made to the accounts of a business or entity to ostensibly reflect or adjust for matters that are “one-off” or non-recurring or that relate solely or predominantly to ownership of the business or entity by the Buyer or Seller. The purpose is to seek to portray the ‘real’ or underlying Maintainable Earnings of the business or entity. A common normalisation when calculating the earnings of a business is to add back certain head office costs imposed by one owner or another (which has the effect of increasing earnings) or to reduce revenue (thereby reducing earnings) resulting from intra-group transactions that will not be repeated once the business or entity changes hands.

NO-SHOP RESTRICTION: see *Exclusivity.*

NO-TALK RESTRICTION: see *Exclusivity.*

NOVATION: If in a contract between party A and party B it is intended that party C will step into the shoes of party B, and assume its rights and obligations, it is necessary that parties A, B and C enter into a deed or agreement of novation. The effect of a novation is, in law, to terminate the original contract between party A and party B, and create a new contract between party A and party C on the same terms as the original document (as modified by the terms of the Novation). It is usual for a novation to be effected by a Deed between all parties (outgoing, continuing and incoming).

OWNERS' EQUITY: An accounting concept referring to the book value of surplus (or deficit) of Assets minus Liabilities. Owners' Equity equals Net Assets and may be positive or negative.

PORTFOLIO COMPANY: A company in which a Private Equity investor has an investment; i.e., which is in its investment portfolio. See also Investee.

POST-COMPLETION: The period following Completion (of no definite duration) during which administrative matters relevant to the sale and purchase (e.g., lodgement of documents with regulators, payment of Stamp Duty, obtaining consents) must be attended to or during which legal obligations (e.g., in relation to Representations and Warranties, Earn-outs or Non-competes) exist.

POST-EMPLOYMENT RESTRAINT: A contractual restraint on an employee of a business or entity from competing with the business or entity for a specified period after their employment with the business or entity ceases. The nature of the restraint (what activity is prohibited), the area of the restraint (the places where conduct is restricted) and the duration of the restraint should be determined having regard to factors including the seniority of the employee; the knowledge and/or access the employee has to the sensitive commercial information of their employer (and therefore their capacity to harm its interests if this information is used improperly) and the consideration provided by the employer to the employee in consideration for the restraint. As Post-Employment Restraints limit the capacity of the restrained party to earn a living from the restrained activities they will be unenforceable if they are not reasonable having regard to the circumstances.

PRE-COMPLETION: Generally a reference to the period after Execution/Signing of the sale documentation and before Completion.

PRE-EMPTIVE RIGHT: see *Right of First Refusal.*

PRICE CHIPPING: A strategy used by prospective purchasers to reduce the Purchase Price. It involves seeking to reduce the initial indicative price that was offered to the Seller on the grounds of issues subsequently arising or identified in due diligence or otherwise.

PRIVATE EQUITY: A category of investors who typically raise investment funds (from wholesale investors) for the purposes of acquiring a target business or entity (or an interest in a target business or entity) with a view to Exiting that investment at a future date (usually within three to five years) for a profit. Private Equity often seek to improve the performance of Investees by playing an active role in strategy, management and operations, providing additional capital to allow business expansion (expansion capital) and restructuring the Investee's funding (e.g., re-negotiating financing agreements).

PRIVATE M&A: see *Private Treaty M&A.*

PRIVATE TREATY: An Agreement (2) between two or more parties for the sale and purchase of assets, a business or shares. It is private at least in the sense that unlike a public transaction such as a takeover or scheme of arrangement, the process is not regulated in detail by the Corporations Act and does not involve the investing public.

PRIVATE TREATY M&A: M&A achieved through Private Treaty. Also called Private M&A. Contrast: Regulated M&A.

PROCESS LETTER: A letter prepared on behalf of a Seller, typically by the Seller's Financial Adviser in the context of a Competitive Process, that sets out how the sale process is to be conducted, including timeframes, requirements for bids and terms and conditions of participation.

PURCHASE PRICE: The price paid by (or on behalf of) the Buyer for the acquisition of a target business or entity. The Purchase Price can be structured in a variety of different ways. These include basing the Purchase Price on the Enterprise Value of the target business or entity including an agreed (baseline) level of Working Capital (and then adjusting the Purchase Price Post Completion if the actual Working Capital (as shown in the Completion Accounts) is greater than, or less than the agreed baseline; basing the Purchase Price on the Net Assets of the target business or entity; or using either of the foregoing options together with an Earn-Out mechanism that rewards the Seller if the target business or entity performs as well as or better than expected. Depending on how the Purchase Price is structured, the negotiating strength of the parties and other transaction specific factors, the Purchase Price may be paid as a lump sum at Completion (with a Post Completion cash adjustment); the Seller may require a Deposit up front with the balance of the Purchase Price payable later; or the Buyer may pay a portion of the Purchase Price at Completion (subject to Post Completion adjustments) and a portion later (as Deferred Consideration, under a Retention, or under an Earn-Out).

PURCHASER: see *Buyer.*

RECITALS: see *Background.*

RED FLAG: Often used in the context of Due Diligence, to refer to an important or significant issue or matter that may affect the willingness of a Buyer to proceed with the acquisition or the material terms upon which it might be prepared to do so.

REGULATED M&A: M&A achieved through a Regulated Transaction. Contrast: Private Treaty M&A.

REGULATED TRANSACTION: Generally a reference to M&A transactions such as takeovers and schemes of arrangement, that are subject to detailed regulation under the Corporations Act. Contrast: Private Treaty transactions.

REPRESENTATIONS AND WARRANTIES: Statements made by a party as to certain state of affairs on which one or more parties to the sale documents have relied in entering into the arrangement. Breach of a Representation and Warranty (i.e., a Representation or Warranty being incorrect) is a breach of contract as a result of which the Warrantor may be liable for damages (under the law of Contract, the law of tort or statute (e.g., the Competition and Consumer Act for misleading and deceptive conduct or conduct that is likely to mislead and deceive)) or under an Indemnity that it has given.

RESTRAINT: see *Non-Compete* and *Post Employment Restraint.*

RETENTION: A portion of the Purchase Price that is retained (or held back) by the Buyer Post Completion and which is only payable in agreed circumstances, which might include the occurrence (or non-occurrence) of a specified event (e.g., an approval being granted or transferred, a litigation claim being discontinued) or a certain state of affairs existing (or not existing) (e.g., a period for a claim being made by a third party against the Target expiring). From a Buyer's perspective, if its assessment of the Purchase Price is predicated on some future event or state affairs, it is a lower risk approach to hold back some of the Purchase Price and only pay it if the payment condition is satisfied than to pay it upfront and try to recover from the Seller the amount paid if the payment condition is not subsequently satisfied. Conversely, it is in the Seller's interests to receive payment as quickly as possible and not have any ongoing exposure to the Buyer (i.e., until the Buyer actually pays, the Seller is exposed to the risk that the Buyer will not, or cannot, pay the balance outstanding). This tension between the interests of Buyer and Seller is frequently addressed through the use of an Escrow arrangement. Contrast: Deferred Consideration.

RIGHT OF FIRST REFUSAL: A right of an existing shareholder, co-venturer or partner to acquire the interest of an existing shareholder, co-venturer or partner. These rights may be contained in a Shareholders' Agreement (in respect of a Company), partnership agreement or joint venture agreement or elsewhere. Also may be called a Right of Pre-emption.

RIGHT OF PRE-EMPTION: see *Right of First Refusal.*

ROLL OVER RELIEF: A deferral of the obligation of a Seller to pay Capital Gains Tax on the sale of Shares or assets where the proceeds of sale are re-invested in qualifying assets.

SALE OF A GOING CONCERN: Where in an Asset sale all of the assets that are needed to conduct a business are transferred or acquired by the Buyer, the Sale may be classified for GST purposes as the sale of a going concern and will be GST free. As stamp duty is payable on the GST inclusive value/consideration of a dutiable asset, this may also result in a stamp duty saving.

SELLER: A party who is selling an asset, whether that is shares (in a Share Sale) or a business or specified assets in an Asset Sale.

SELL SIDE: A reference to advisers (financial and legal) acting for a prospective Seller.

SHAREHOLDERS' AGREEMENT: An Agreement (1) between the shareholders of a company, and frequently the Company also, that documents how the company is to be operated and managed and which sets out the rights and obligations of the shareholders. Commonly a Shareholders' Agreement will contain provisions concerning shareholders' rights to appoint and remove directors; shareholders' obligations to fund the company; the circumstances in which shareholders may or must transfer their shares; decision making rights (including rights of the board and shareholders) and provisions regarding other aspects of internal management.

SHAREHOLDERS' DEED: A Shareholders' Agreement in the form of a Deed.

SHARE SALE: A means of structuring an acquisition pursuant to which the Buyer acquires some or all of the shares in the target company from its shareholders. A Share Sale may result in a change in control of the target company but (subject to provisions in arrangements to which the target company is party) does not affect its underlying legal and commercial arrangements (e.g., contracts remain in place, employment arrangements are unaffected and the target company will remain responsible for all of its accrued and contingent liabilities).

SIGNING: see *Execution.*

SPA: Share purchase agreement or sale and purchase agreement. In the latter case, the term can be used to refer either to a document to effect an Asset Sale or a Share Sale.

SPONSOR: a Private Equity investor.

SSA: Share Sale Agreement.

SSD: Share Sale Deed.

STATUTE OF LIMITATIONS: Commonwealth and State and Territory legislation that limits the capacity of a party to bring legal proceedings for breach of the terms of a Contract or Deed or some other legal right unless the action is commenced within a specified time period. There is no one limitation period that applies. Limitation periods vary across jurisdictions and, within a jurisdiction, can vary depending on the applicable legislation or the nature or circumstances of the cause of action.

SUNSET DATE: The deadline by which all Conditions Precedent must be satisfied or waived. If the Conditions Precedent are not satisfied or waived by this date, the document will usually provide that it can be terminated by one or more parties. In some cases it may automatically terminate. Also may be called an End Date.

TARGET: A general reference to a target business, company or other entity.

TEASER: A short flyer, commonly issued by a Sell-side Financial Adviser, that advises that a particular business or entity is for sale and inviting prospective Buyers to contact the Financial Adviser for more information. Once contact is made and a prospective Buyer vetted, they will usually be invited to sign a Confidentiality Agreement before being given an IM or other process document (such as a Process Letter).

TERM SHEET: see *Heads of Agreement.*

THIRD PARTY: A person (who may be a natural person or another form of legal person, e.g., a company) who is not a party to the sale documentation (e.g., customers, suppliers, financiers, competitors etc.).

TRADE SALE: A sale of a business or entity to another participant in the industry (or a new entrant to the industry). To be contrasted with other forms of Exit such as a sale to Private Equity, an MBO or an IPO.

VENDOR: A Seller.

VENDOR DD: see *Vendor Due Diligence.*

VENDOR DUE DILIGENCE: Due Diligence undertaken by the Seller of a business or entity the purpose of which is to identify any issues that may be relevant to potential purchasers that may affect their willingness to proceed with the acquisition or the terms upon which they may be prepared to do so. By identifying issues upfront, the Seller can either seek to address them in advance or disclose them to potential purchasers, minimising the chance of Price Chipping.

WARRANTOR: A person who gives a Representation and Warranty. See also Covenantor.

WARRANTY: see *Representation and Warranties.*

WARRANTY CAP: The maximum amount for which a party who has given a warranty is liable in damages (or under an indemnity) to a party in whose favour the representation or warranty has been given. Typically the cap is expressed as a percentage of the Purchase Price (e.g., 100%, 50% etc).

WARRANTY AND INDEMNITY INSURANCE: Insurance for a buyer or seller against a claim for breach of a Warranty or a claim against a tax indemnity. If taken out by a Buyer, a W&I policy will cover the Buyer from the loss that it sustains as a result of the breach of the Warranty. In the case of a Seller, a W&I policy can provide protection against the risk of a claim by the Buyer against the Seller for innocent (i.e., unknowing) misrepresentations by the Seller.

W&I: see *Warranty and Indemnity Insurance.*

WORKING CAPITAL: In general terms Working Capital means Current Assets less Current Liabilities (but the parties may agree that it includes items that are not normally taken into account or that it excludes items that typically form part of the calculation). A businesses' Working Capital requirement is the amount of money that is needed to enable the business to trade in the ordinary course without the need for its owners to contribute additional funding. As a simple example, if a business has expenses per month of wages ($6 million), rent ($3 million) and other expenses ($9 million), total outflows per month would be $18 million. Unless there is enough cash generated to pay the current monthly expenses (such as through the sale of stock), and/or enough accounts receivable (to be collected and turned into cash) to pay the following month's expenses, the business will have a funding shortfall in the following month and will require further funding (capital or debt) in order to continue to trade. A buyer will usually require that a business or entity be sold with sufficient working capital to enable it to trade without the buyer needing to contribute additional capital. In such a case, if there is a shortfall in the Working Capital (as disclosed in the Completion Accounts) the sale agreement will usually contain a mechanism under which the purchase price is reduced by the amount of the shortfall (or if the purchase price was based on an estimated level of Working Capital, by the difference between the actual level and the estimate). A corresponding adjustment mechanism will usually apply in the event that Working Capital is higher than agreed/estimated. What the Working Capital requirement of a business or entity actually is, and how it is to be measured, is often a matter of significant commercial negotiation. In the majority of instances, the amount of Working Capital agreed between the parties (and forming part of the Purchase Price) is represented by a net amount, being working capital assets less working capital liabilities. For example, if stock, accounts receivable and other working capital assets equalled $20 million and creditors and other working capital liabilities equalled $15 million, the amount of Working Capital agreed would be $5 million.

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Johnson Winter & Slattery represents Australian and international clients on their most strategic, complex and demanding transactions throughout Australia and surrounding regions. Members of our Transactional and Advisory team have advised on some of Australia's largest and most complex transactions. We have been described as "a really excellent firm which is making a mark" (Chambers Asia-Pacific, 2014).

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Reflecting the high profile of our work, members of our Transactional and Advisory team are ranked as leading lawyers in the area of M&A in Chambers Global, Asia Pacific Legal 500, Doyle's Guide to the Australian Legal Profession and Best Lawyers International: Australia.

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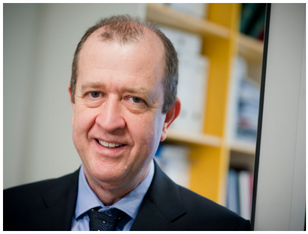

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