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MCC INTERVIEW: Troy Dahlberg & Kristy Serviss / KPMG

It Ain't Over Till It's Over

Post-acquisition disputes are as much a part of the deal landscape as closing dinners.

MCC: You've each made your mark in post-acquisition disputes. Tell us about the area and how companies find themselves embroiled in such disputes.

Serviss: The culmination of the sale of a business can be a complex and lengthy process. Purchase and sale agreements often include anticipated or targeted closing accounting and financial metrics that were used to price the deal. After the closing of the transaction, accounting and financial adjustments are required as part of the determination of the final purchase price. Such price adjustments may include working capital, indebtedness, cash, transaction-related expenses, and earn-outs. When calculating such adjustments, buyers and sellers are often inclined to interpret the agreement adjustment provisions differently, with each side preparing a calculation that is most favorable to their own interests. The purchase price adjustment process can involve prolonged complex negotiations regarding fundamental accounting differences between the parties' adjustment calculations, which if not resolved can lead to a formal dispute process and have a significant impact on the overall price of a transaction.

MCC: If adjustments have a tendency to spawn disputes, why do parties include them in their agreements?

Dahlberg: Despite the risk of a dispute, parties almost always include purchase price adjustments to ensure they are receiving the value that was negotiated at the time the purchase price was determined. With significant due diligence, regulatory and financing considerations, and contract negotiations, it's not surprising that companies often experience substantial delay between the determination of the purchase price of the transaction and the actual closing of the deal. Accordingly, it's critical that any accounting and financial changes that occurred between the pricing and the closing of the transaction are accurately accounted for. These final accounting and financial metrics are not known until after the closing, therefore such adjustments are needed in purchase and sale agreements to ultimately determine the final purchase price as of the closing date.

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MCC: Given how common such scenarios must be, you'd think such disputes would be relatively easy to head off. Apparently, that's not the case.

Serviss: Post-acquisition disputes can be surprisingly difficult to settle, largely due to the accounting and financial language contained in the purchase and sale agreements. For example, there may have been a lack of attention paid to the adjustment mechanism clauses, which can give rise to trouble later. The parties may have used standard boilerplate agreements not tailored to the specific needs of the transaction. Or they may have accepted vague and imprecise accounting language regarding closing financial statement requirements – all of which can give rise to a post-acquisition dispute.

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Dahlberg: Consider a phrase commonly found in these agreements: "Generally Accepted Accounting Principles (GAAP), consistently applied." On its face, this may seem sufficiently straightforward, but it's not. GAAP is open to interpretation, and the parties in most deals exercise judgment that is most beneficial to their own interests. Another example would be an agreement that requires a post-closing adjustment related to cash but that fails to provide for a specific valuation of that cash. Parties then may tangle over whether the cash should be valued in accordance with cash recorded on the balance sheet or in the

bank. These issues arise far more frequently than you might expect.

MCC: What are some of the steps a company can take to mitigate the risk of getting enmeshed in a post-acquisition dispute?

Serviss: Many deals are signed under pressure-filled, high-stakes conditions. In the rush to get the agreement done, it is imperative that the parties review the accounting and financial contractual language and closely scrutinize the ways in which contracts are structured. While the parties may have different objectives, by focusing on certain issues before the contract is signed they can minimize future misunderstandings and corresponding conflicts. We recommend that buyers and sellers, before they execute an agreement, put greater emphasis on an effective program of contract vetting of the financial and accounting language related to post-closing purchase price adjustment provisions to avoid costly disputes later. This vetting process should include not only counsel, but forensic accountants and other advisors well versed in post-acquisition dispute matters. For example, we often assist companies preparing to execute a transaction by reviewing and determining, with our client and their counsel, whether the sale and purchase agreement reflects their intentions and serves their best interests. Our clients find it extremely beneficial when we review the financial and accounting provisions, such as the determination of working capital, indebtedness, and financial definitions, and steer them through the numerous drafts, prolonged negotiations, and, finally, execution of an agreement.

MCC: Are there fundamental differences between post-acquisition disputes and the many other legal battles companies face?

Serviss: The difference is that most disputes arising from a transaction typically provide for resolution by a court or legal arbitrator. However, purchase price dispute provisions almost exclusively require resolution of disputes by an independent accountant. The agreement, however, seldom provides specific guidance as to the process and procedures that should be employed by the independent accountant.

MCC: What are some of the most noteworthy risks companies should be aware of regarding post-acquisition disputes?

Dahlberg: We focus on three areas: preparation of the closing statements, discovery and objection process, and the independent accountant and resolution process. With regards to the preparation of the closing statement, the risk is that the accounting and financial metrics are not supported by the language of the agreement or accounting evidence. A typical purchase agreement requires that the buyer or seller prepare the closing financial statements, which will determine the post-closing adjustment. Preparation of the statement typically depends on who controls the books and records of the company post-closing, which means the responsibility most often lies with the buyer. After the preparation of the closing statement, the agreement typically provides the opposing side with the opportunity to review the statements and, if necessary, submit an objection. This process most often falls upon the seller. The major risk is that the party required to review the closing financial statements may not be granted sufficient access to the books and records it needs to assess the statements and prepare a timely notice of objection. Some agreements are unclear, if and when such a dispute arises, on how it should be resolved – by the independent accountant or through a court of law. Since agreements typically provide that objection notices be filed within a definitive time or the right to file such objection is waived, timely discovery is often critical.

Serviss: Finally, the parties may designate that a specific independent accounting firm serve as the arbitrator to resolve the dispute. However, there is a substantial risk that the designated firm may not have personnel experienced in post-acquisition dispute matters. Additionally, there is risk that the independent accountant identified may not utilize a resolution process that will allow the parties to best present their claims. Moreover, if a specific accounting firm is not designated, the process in choosing an independent accountant and agreeing on the procedures for resolution can lead to a dispute. These issues are often not contemplated by the parties and happen more often that one would expect.

MCC: What specific benefits do companies realize by engaging an accounting or consulting firm to work alongside counsel in managing a post-acquisition dispute?

Serviss: Dispute resolution can be a long, uncertain, expensive process. Accountants are well equipped to provide unbiased advice in disputes, alongside counsel. We regularly help companies vet contracts to identify ambiguous and problematic language, guage, pinpoint the relevant facts, handle discovery requests, and uncover the mitigating weaknesses of their positions. From there, we work with them to formulate the key points of their positions, identifying the relevant accounting and financial information needed to support them. Additionally, since accountants are typically those charged with resolving disputes, we understand how they typically would interpret contractual language and the implications of that interpretation as it relates to the financial and accounting requirements in agreements. That gives us a unique vantage point from which we can deliver distinct benefits and provide additional value to a company.

Dahlberg: When you add substantial experience in post-acquisition disputes to that, it's a potent combination. We understand, as few can, the complexities involved in evaluating and drafting positions so that they are as clear and concise as possible for a third-party independent accountant. On top of that, we often serve as the independent accountant appointed to resolve post-acquisition disputes. That's a hard combination to beat.