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Deloitte M&A Views podcast:
M&A technology: Turbocharge your transactions

Transcript

Greg Jarrett: Welcome to Deloitte M&A Views, a Deloitte podcast series exploring the latest trends and topics in mergers and acquisitions. I'm Greg Jarrett, and today we discuss using technology to turbocharge your M&A transactions, specifically how AI (artificial intelligence) can bring efficiencies to the M&A processes. We're joined today by Joni Young, managing director with Deloitte Consulting LLP's M&A supply chain practice, and Janet Roth, M&A partner Deloitte and Touche LLP.

To help set the stage for today's discussion, Joni, can you please help us understand why contracts are so important to the M&A deal?

Joni Young: Thanks, Greg. In my experience reviewing supplier and customer contracts, the majority of contracts contain terms that restrict assignability and use post–Day One integration. That being said, it is true that these restrictions have different degrees of impact that may depend on the type of deal—for example, buy side or sell side, divestiture or integration. Let me explain. Many buyers may assume that the contracts of the company they are buying will come over automatically with the sale, and then they can do what they want with respect to the contracts. Although a large portion of contracts may generally allow assignment in the event that the entire company is being purchased by another company, even in this situation, we may see upwards of 25 percent of contracts that simply do not allow assignment under any circumstances. So if the acquirer was interested in merging or terminating such a contract, they may be subject to termination penalties or other conditions which have bearing on the timing and degree of synergies captured and deficiencies realized.

For divestitures and carve-outs, it's even more important to understand the restrictions within the contract, and what divestiture provisions exist to support transition services, agreements, and use after Day One, as these conditions may pose disruptions to the day-to-day operations.

Greg Jarrett: Well, it seems like you'd need a lot of legal eyes, especially with a large company that's involved with a lot of activity. What can these companies do if they want to understand the terms and conditions of their contracts as they prepare for an M&A event?

Joni Young: So thankfully there's some good news on that front. Our experience has been that one person can review on average only about four to five contracts per day manually to extract key metadata needed to provide information critical to the transaction. Since the average company today is doing business with over 100 technology suppliers and likely has upwards of thousands of contracts across all businesses, there's a significant amount of time and cost required for these manual reviews. Today there are artificial intelligence, AI products on the market that can accelerate this process using a combination of optical character recognition (OCR), natural language processing, machine learning, and then supplemented with human review. Because corporate contracts are not standardized but are written on unlimited variations of company and third-party paper, we find it necessary to use a highly flexible AI engine to locate key data along with human reviewers for quality control and final determination. The results are, in many cases, fantastic. For the example of the 1000 contracts that I mentioned earlier, it would take approximately 1600 hours of human review to manually extract key metadata. Today, with the help of a cognitive engine, it takes approximately 180 hours in total.

In addition to the timeliness of getting insights into contract restrictions, we've also found that the combination of human and machine costs less and is more accurate than prior manual-only reviews.

Greg Jarrett: Joni, let's take a minute to talk about divestitures and carve-outs. Now I understand contracts may be an even bigger issue in these situations, but can you explain to me why that is?

Joni Young Sure, thanks, Greg, that's a great question. I often hear that the parent company says that they will sign over all of the contracts used by a business that they are planning to spin off. It is likely that, that is their intent, and it is also the intent of the buyer of the business units if it is being stood up. However, given the nature of today's corporations, it's likely that the day-to-day operations of a business unit rely heavily on shared corporate contracts, and even the contracts that may be created solely for a specific business unit's use may have been executed by the corporate parent. This makes the parent the owner of that contract and not the business who is using it. Therefore, it's likely that the majority of contracts governing the business of any to-be spin-offs are owned by the corporate parent, and therefore are subject to the nuances of the contract terms and conditions.

Thus, this adds up to even more contracts that need document review and clause capture to understand the restrictions and the limitations. At one recent client, we experienced that even the spin-off business unit contracts that were in the business unit's name had been expanded for use by other corporate units, and therefore, those contracts also needed review to see if they contained the rights to provide services back to the parent.

Greg Jarrett: Okay Janet, let me ask you, are there any other areas that benefit from the accelerators that you've seen companies leverage?

Janet Roth: Yes, Greg, there's a couple areas. First, during the financial due diligence process, we often review key contracts. Leveraging AI to gather data such as guarantees, take-or-pay requirements, most favored nation clauses, and renewal options, can really reduce your diligence timelines.

In addition, post-diligence, the accounting function is one area that has also benefited from the use of AI. The accounting roles, such as ASC 842, recently required all companies review their contracts that may constitute a lease and record them as liabilities on the balance sheet. Thus, the AI tools can address this need at the same time they're compiling the contract data needed for key terms, the rights of use, etc. as Joni was describing before.

Greg Jarrett: Thanks Janet, and thanks Joni. You've certainly provided a lot for me and for our listeners to consider as we evaluate leveraging emerging technology for M&A deals.

Greg Jarrett: I'm Greg Jarrett. Thanks for listening to Deloitte M&A Views, sponsored by Deloitte's M&A Institute. This podcast is provided by Deloitte and is intended to provide general information only. This podcast is not intended to constitute advice or services of any kind. For additional information about Deloitte, go to deloitte.com/about. We also release new podcasts regularly, and if you subscribe, you won't miss a single one.

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