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M&A Hot Takes
Turbocharge your next transaction
Leveraging new technology can elevate your M&A deal

In this issue

Introduction

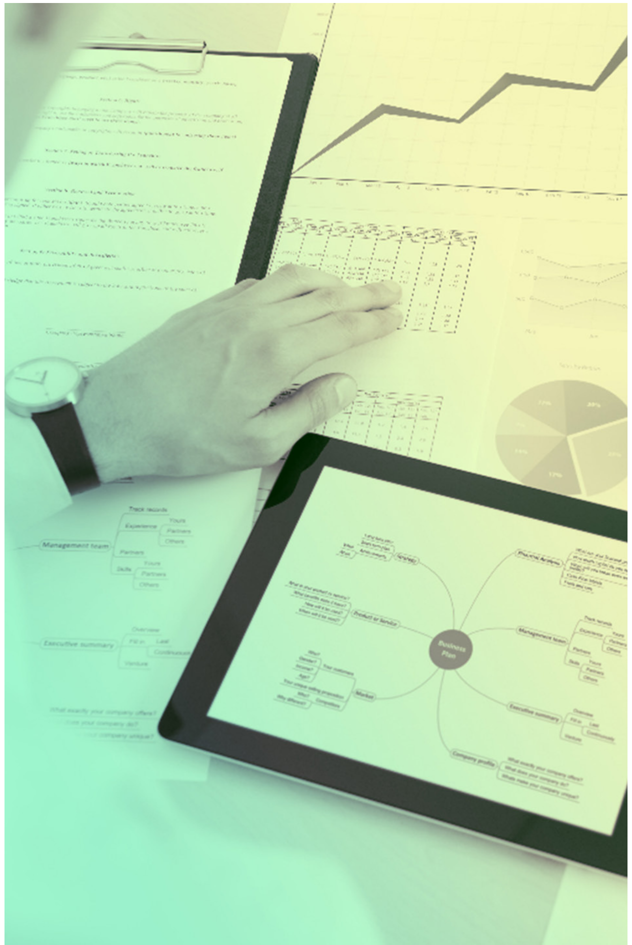
The well-worn adage "the devil is in the details" is very much relevant to mergers & acquisitions (M&A). That's because, based on our experience, about half of all corporate contracts contain conditions that restrict assignability. There's more: parties in transactions also can benefit from knowing if contracts will need to be renegotiated or terminated to yield desired synergies and justify the deal price.

If you think these details seem trivial, think again, because contract clauses can be costly. Even if contract terms provide for "assignment upon mutual consent which shall not be unreasonably withheld," one recent software provider requested a $1.5 million payoff for consent to assignment, noting the request wasn't unreasonable and was standard practice for their company. Until recently, the only way to assess the extent of potential liabilities and opportunities lurking in contracts was to review manually thousands of agreements and record key terms and provisions. That's a slow and tedious process and requires considerable resources and time, factors that may not be available while preparing for an M&A transaction. Further, manual reviews can be hampered by lengthy and complex documents that may have terms impacting key provisions buried throughout subsequent pages, amendments, and SOWs.

Those days may be over.

Advances in cognitive technology—such as artificial intelligence (AI) software—now enable the rapid identification and extraction of key provisions through review of thousands of contracts and other documents within a few weeks' time. Having a provider on your deal team that specializes in deal strategy and that can leverage state-of-the-art technology can enable companies to markedly speed up the M&A process and free up resources. Further, the use of cognitive technology is becoming more accurate, limiting human tendencies to tire, get distracted, or overlook information.

It's important to note that advanced technology is not a substitute for people; rather it's a force multiplier that allows people to turbocharge their work—and get deals done more quickly, more efficiently, and often at a lower cost. Let's look at how new technology can impact different transactions and phases of the entire M&A life cycle, from purchases to divestitures and from due diligence to Day 1 integration.



Due diligence

The review of key supplier contracts is a common task performed during financial due diligence. In the past, this process was handled manually; reviewers sifted through documents looking for supplier contracts and capturing key provisions, such as take-or-pay requirements, renewal dates, and fixed fee amounts. While pricing information often is redacted or scrubbed in the contracts during due diligence, assignability provisions have been aggregated and summarized manually by due diligence teams for years.

Today, these data can be pulled through software and put into a visualized format to show the buyer the financial exposure and costs associated with the contracts that come with the transaction. The process is far quicker and more accurate than manual review.

It's not just assignability issues that can be improved. Here are a few examples of how technology can help in other areas of the due diligence phase:

- New accounting standards have required gathering data elements associated with leases. Technology can expedite this process and inform the buyer regarding what additional liabilities would come onto the balance sheet.
- Technology can be used to analyze employment agreements and capture one-time costs (such as severance and bonus payouts) and other employment costs.
- In the oil and gas industry, land leases are one type of contract that is manually reviewed by attorneys. It is not uncommon for attorneys to charge legal fees (hours) by each lease they read, even if the leases are standard. For example, if there are 200 leases, and there are 10 standards, attorneys will charge for reviewing 200 rather than the 10 standard leases. Thus, using technology for this process can potentially reduce attorney fees during diligence.

One company we worked with recently spent eight weeks (and $400,000) and had nine reviewers combing through more than 1,000 contracts. That work could have been handled in no more than three weeks for approximately 20% of the cost had the company brought in the right advisor to leverage available technology for their contract review.

Mergers and acquisitions

Contracts often are a window into supplier and customer relationships, which can be pivotal in a merger and acquisition.

Due to time constraints, the prior approach to reviewing contracts relied on sampling some contracts and extrapolating company-wide results. New AI technology, however, shifts the prior balance between limited time and the desire to plan and understand (and then mitigate) risk. The new technology enables a more comprehensive view in the same—if not a shorter—time period, enabling analysis to go beyond just review and into helping plan next steps.

This enables companies involved in a deal to better realize synergies and address obstacles immediately upon close. For example, technology can help in Day 1 planning by standardizing supplier outreach to amend License Agreements as needed. Here are some more areas in which an experienced strategic advisor can drive value by leveraging the use of new technology in terms of contract review and analysis:

- Contract management—end dates, spend commitments, and termination requirements
- Sourcing and negotiation—pricing, service level agreements (SLAs), and general terms
- Customer audits—pricing rights, payment terms, usage restrictions, and customer obligations
- Alliance/partner review—balance of trade, training, and sales obligations
- Supplier audits: pricing, SLAs, and payment terms
- Risk assessment: standard clauses, liability and indemnification, termination rights, dispute resolution, and risk mitigation obligations

During the recent acquisition of a multinational technology services business, technology-enabled review and dispositioning of more than 4,500 agreements facilitated centralizing and streamlining contract separation of more than 800 suppliers associated with about $775 million in shared spend and resulted in the cost-free transfer of perpetual licenses valued in excess of $100 million.

Divestitures, sales, and spinoffs

The highest potential for risk is often seen with corporate divestitures, because companies increasingly bundle spend and contracts across numerous divisions, creating complexity when separating a business unit.

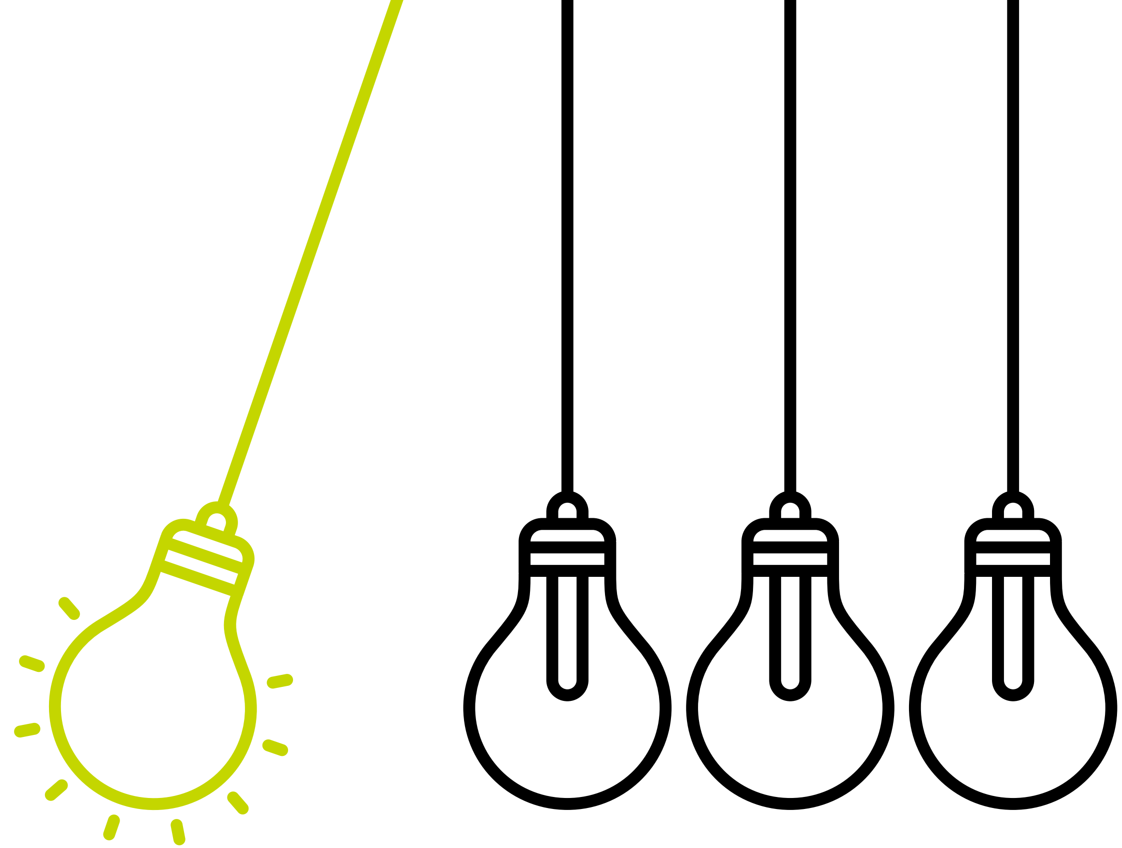
Contracts generally are not business unit–specific, nor are they designed to account for an event such as a divestiture. Further, supplier contracts, particularly those related to software, typically have significant embedded restrictions of which companies are often not aware.

AI can help companies realize their full exposure before deciding to divest a unit. There are often big payoffs for companies who take the time to assess their contracts and execute strategies to obtain the rights needed. Managing these contracts can simplify the transaction, offer a more valuable spinoff, and can potentially increase the price of a sale in a number of ways:

- Proactively addressing licensing restrictions
- Preserving preferential pricing in supplier agreements
- Simplifying the customer transition process

For a recent carve-out with over $2 billion in spend with shared suppliers, AI-based contract reviews enabled dispositioning for more than 4,500 agreements, which led to bifurcation of more than 1,800 agreements, allowing continued use of about 800 suppliers associated with approximately $775 million in spend with shared suppliers.

Conclusion



As deal activity persists, companies can save resources and benefit from better, more accurate, and more comprehensive information embedded in contacts by leveraging the latest in cognitive technology. It's a next-generation approach to deal making: combining strategy with technology.

Whether a company is looking to integrate or divest a business, it's beneficial to understand the nitty-gritty details of all corporate contracts to prepare and make sure there are no hidden surprises. In addition, companies can capture valuable insight into third-party and customer relationships in contracts.

What used to be a laborious, expensive, time-consuming, and error-prone process can turn into a way for companies to turbocharge their next M&A event.

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