

**M&A TRANSACTIONS:
HOW TO NEGOTIATE KEY PROVISIONS
IN A PRIVATE COMPANY ACQUISITION AGREEMENT**

JOHN C. ALE
Southwestern Energy Company

DAVID W. COOK
Kelly Hart & Hallman LLP

CLIFF ERNST
Graves, Dougherty, Hearon & Moody, P.C.

State Bar of Texas
14TH ANNUAL
CHOICE, GOVERNANCE & ACQUISITION OF ENTITIES
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CHAPTER 9



John C. Ale

Senior Vice President, General Counsel & Secretary

Southwestern Energy Company



John Ale became Senior Vice President, General Counsel & Secretary of Southwestern Energy Company in November 2013. Southwestern is an independent energy company whose wholly-owned subsidiaries are engaged in natural gas and oil exploration, development and production, natural gas gathering and marketing. It is the third largest natural gas producer in the Continental United States and is listed on the New York Stock Exchange. Additional information on the company can be found at <http://www.swn.com>.

Prior to joining Southwestern Energy, John was Vice President and General Counsel of Occidental Petroleum Corporation. Before that he was a partner with Skadden, Arps, Slate, Meagher & Flom LLP in the firm's energy and infrastructure projects practice group and leader of the firm's Houston office. From 1998 until 2002, he served as Executive Director and General Counsel of Azurix Corp., a global water company listed on the NYSE. Previously, he was a partner with Vinson & Elkins L.L.P., including time as head of the firm's London office and its project finance practice. He also served as a law clerk to Chief Justice Warren E. Burger at the U.S. Supreme Court and Judge Edward Allen Tamm of the U.S. Court of Appeals for the District of Columbia Circuit. John graduated from the University of Virginia School of Law (Order of the Coif, *Virginia Law Review*) and College of Arts and Sciences (B.A. in economics with highest honors, Phi Beta Kappa).

John is a former Chair of the 4,000+-member Business Law Section of the State Bar of Texas, for which he also chaired committees on partnership law and choice-of-law legislation. He is a frequent lecturer and author on topics in energy and partnership law and on professional ethics. John is a former adjunct professor of law at the University of Texas and the author of *Partnership Law for Securities Practitioners* (Thomson Reuters Securities Law Handbook Series).

John has served on the Alexis de Tocqueville Committee of the United Way of Greater Houston and as a trustee of The Regis School. He and his wife live in Houston and have two grown sons.

David W. Cook is a partner at Kelly Hart & Hallman LLP and is based in the firm's Fort Worth office. His practice focuses primarily on mergers and acquisitions and energy transactions, including negotiated acquisitions and divestitures, leveraged acquisitions, recapitalizations, controlled auctions and the purchase and sale of producing properties. He has substantial experience in representing clients (both private equity firms and management teams) in connection with private equity investments. He also regularly counsels clients in connection with compliance issues and statutory required filings and motions, including with respect to the Hart-Scott-Rodino Antitrust Improvements Act of 1976. He is an adjunct professor at Texas A&M University School of Law, has spoken at a number of conferences and CLEs, including the Business Law and Corporate Counsel Forum at the State Bar of Texas Annual Meeting in 2013, has been recognized as a "Texas Super Lawyer, Rising Star" by Thomson Reuters, as published in *Texas Monthly* magazine (2008-2010, 2013-2016) and a "Top Attorney" by *Fort Worth, Texas* magazine (2008, 2010-2015), is a Fellow of the Texas Bar Foundation and the Tarrant County Bar Foundation, is a "40 Under 40" honoree by the *Fort Worth Business Press* and serves on the Texas Business Organizations Code Committee. He graduated first in his class at Texas Wesleyan University School of Law (now known as Texas A&M University School of Law) where he served as Editor-in-Chief of its Law Review.

CLIFF ERNST
Graves Dougherty Hearon & Moody,
A Professional Corporation
401 Congress Avenue, Suite 2200
Austin, Texas 78701
512-480-5672
FAX: 512-480-5872
cernst@gdhm.com

BIOGRAPHICAL INFORMATION

EDUCATION

- Admitted to bar, 1978, Texas.
- University of Texas (J.D., 1978). Order of the Coif; First Place Team - Kemp, Smith Mock Trial.
- Oklahoma State University (B.A., English, 1975). Outstanding Graduate in College of Arts and Science 1975; Blue Key; Omicron Delta Kappa; Phi Eta Sigma; Student Senate.

PROFESSIONAL ACTIVITIES

Member: Austin Bar Association (Business, Corporate and Tax Section); American Bar Association (Business Law Section); State Bar of Texas (Business Law Section).

UT Law Continuing Legal Education, LLC's, LP's and Partnerships; Planning Committee Co-Chair, since 2014.

SELECTED HONORS, PUBLICATIONS AND PRESENTATIONS

Listed in The Best Lawyers in America® published by Woodward/White, Inc., Banking and Finance Law; Mergers & Acquisitions Law; Securities / Capital Markets Law, since 2010.

“Choice of Entities – Who Owns the Deal; Model Company Agreements for Simple LLCs,” (co-authored with Prof. Elizabeth S. Miller), State Bar of Texas, 9th Annual Advanced Real Estate Strategies Course, December, 2015.

“Model Company Agreements for Simple LLCs,” (co-authored with Prof. Elizabeth S. Miller), University of Texas CLE seminar, July, 2015.

“Top Ten ‘Gotchas’ in Drafting LLC and Partnership Agreements,” University of Texas CLE seminar, July, 2015.

“Exploring the Flexibility Offered by the TBOC Merger Provisions,” University of Texas CLE seminar, July, 2014.

“Acquisitions of Professional Firms,” State Bar of Texas, 12th Annual Choice and Acquisition of Entities Course, May, 2014.

“Primer: Nuts and Bolts of LLCs, LPs and Partnerships,” University of Texas CLE seminar, July, 2013.

“Duties of Managers and Members of LLCs and Partners of Partnerships,” State Bar of Texas, Advanced Real Estate Law Course, July, 2013.

“2012 Choice of Jurisdiction Considerations: Texas vs. Delaware,” University of Texas CLE seminar, July, 2012.

“Distributions, Profit and Loss Allocations and Tax Reimbursement Provisions,” University of Texas CLE seminar, July, 2012.

“Considerations Relating to Negotiating and Drafting Purchase and Sale Agreements,” State Bar of Texas, Choice and Acquisition of Entities in Texas Course, May, 2012.

“Capital Contributions, Capital Calls, Financing, Funding and New Equity: Key Planning and Drafting Issues for LLCs, LPs and Partnerships,” University of Texas CLE seminar, July, 2011.

“Planning, Drafting and Implementing Capital Call Provisions,” University of Texas CLE seminar, July, 2009.

“Sale of Partnership and LLC Interests: A Walk Through Purchase and Sale Agreements,” University of Texas CLE seminar, July, 2007.

“Rules for Investment Advisers – Changes to the Texas Registration Exemption,” Texas Lawyer, July 18, 2005.

Drafting and Closing Settlement Agreements.

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M&A Transactions: How to Negotiate Key Provisions in a Private Company Acquisition Agreement

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The Contents of Purchase Agreements

- Preamble
- Recitals
- Definitions
- Basic Transaction
- Purchase Price & Adjustments
- Closing Mechanics & Deliverables
- Representations & Warranties
- Pre-Closing Covenants
- Post-Closing Covenants
- Closing Conditions
- Termination
- Remedies for Breach & Procedures
- Miscellaneous Provisions

Key Definitions

“**Knowledge**” [Buyer Favorable] – the knowledge of *any officer or employee* of the Company after having conducted *reasonable investigation* and made *reasonable inquiry* as to the fact or matter in question.

“**Knowledge**” [Seller Favorable] – the *actual, present* knowledge of *[Named Individuals]* without any inquiry obligation.

Key Definitions

“**Knowledge**” [Middle-Ground] – the *actual* knowledge of *any of* *[Named Individuals]* after having made *reasonable inquiry* of the *employee or employees of the Company* having *management responsibility* for the fact or matter in question.

Key Definitions

“Material Adverse Effect” [Buyer Favorable] – any change, effect, occurrence or development that has, or could reasonably be expected to have, a material adverse effect on (a) the business, results of operations, properties, financial condition, prospects, assets or liabilities of the Company or (b) the ability of the Company to consummate any of the transactions contemplated hereby.

Key Definitions

“Material Adverse Effect” [Seller Revisions] – any change, effect, occurrence or development that has, ~~or could reasonably be expected to have,~~ a material adverse effect on (a) the business, results of operations, properties, financial condition, ~~prospects~~, assets or liabilities of the Company or (b) the ability of the Company to consummate any of the transactions contemplated hereby; provided, however, that none of the following will be deemed (either alone or in combination) to constitute, and none of the following will be taken into account in determining, whether there has been a Material Adverse Effect: [carve-outs]

Common MAE Carve-Outs

Changes in:

- Law
- Economy
- Marketplace
- Industry
- GAAP

Resulting From:

- Force Majeure Events
- Announcement of Deal
- Identity of Buyer
- Actions Contemplated by Agreement or Approved by Buyer
- Failure to Meet Projections

Buyer will likely want some qualified with “no disproportionate impact.”

Purchase Price Adjustments

- “Market” Varies by Industry
 - e.g., Oil & Gas Adjustments based on Effective Time
- Working Capital Adjustment
 - Carefully Define Working Capital
 - Watch Out for “in accordance with GAAP”
 - Consider Including Example Calculation as Exhibit
 - Adjust Only Post-Closing vs Both at Closing and Post-Closing
 - Bands / Collars (two way street)
 - Dispute Resolution Mechanics
 - Recourse Issues (e.g., covered by basket/cap?, recovery from large group of Sellers?)

Certain Representations & Warranties

- Use of Knowledge Qualifiers
- Use of Materiality and MAE Qualifiers
- Condition/Sufficiency of Asset Representation
- Full Disclosure / 10b-5 Representation
- Disclaimer of Other Representations

Condition and Sufficiency of Assets Representation

Condition of Assets. The Assets constitute all of the assets, properties and rights required for or used in the conduct of the Business. The buildings, structures, storage facilities, furniture, fixtures, machinery, equipment, vehicles, and other items of tangible personal property included in the Assets are structurally sound, are in good operating condition and repair, and are suitable for the uses for which they serve.

Seller Markup to
Condition and Sufficiency of Assets Representation

Condition of Assets. Except as set forth on Schedule [X], ~~T~~he Assets constitute all of the material assets, properties and rights required for or used in the conduct of the Business as presently conducted. Except as set forth on Schedule [X], to the Knowledge of Seller, ~~T~~he ~~buildings, structures, storage facilities, furniture, fixtures, machinery, equipment, vehicles, and other~~ items of tangible personal property included in the Assets are ~~structurally sound,~~ are in good operating condition and repair (subject to ordinary wear and tear and items to be repaired in the ordinary course of business), and are suitable for the purposes for which they are currently used by Seller ~~uses for which they serve.~~

Full Disclosure / 10b-5 Representation

Full Disclosure. No representation or warranty by Seller set forth in this Agreement, whether in Article X or otherwise, nor in any agreement, statement schedule or certificate furnished or to be furnished to Buyer hereunder or in connection with the transactions contemplated hereby, contains or will contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements contained herein or therein not misleading.

Seller Markup to
Full Disclosure / 10b-5 Representation

~~Full Disclosure. No representation or warranty by Seller set forth in this Agreement, whether in Article X or otherwise, nor in any agreement, statement schedule or certificate furnished or to be furnished to Buyer hereunder or in connection with the transactions contemplated hereby, contains or will contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements contained herein or therein not misleading.~~

Disclaimer of Other Representations

No Other Representations. Except as expressly set forth in Article X, Seller makes no representation or warranty, express or implied, at law or in equity, in respect of the Company, the businesses of the Company, or otherwise (including as to condition, value, quality, merchantability, usage, suitability, fitness for a particular purpose, non-infringement, risk associated with ownership or otherwise), and any and all such other representations or warranties are hereby expressly forever disclaimed.

Closing Conditions: How Certain is Your Deal?

Common Conditions:

- [Material] Accuracy of Reps
- [Material] Compliance with Pre-Closing Covenants
- No Restraining Litigation
- Material Consents

Other Conditions:

- Board Approval
- Due Diligence
- Financing Contingency
- No MAE

Remedies for Breach

- **Survival Periods**
 - Fundamental vs. Non-Fundamental Reps
 - Covenants
- **Limitations on Indemnification**
 - Eligible Claim Threshold
 - Baskets (Deductible vs. Tipping)
 - Caps
 - Exclusions
 - Losses Covered
 - Materiality Scrape
 - Exclusive Remedy
 - Sandbagging vs. Anti-Sandbagging
- **Sources of Recovery / Ensuring Performance**

Common Fundamental Representations

- Existence
- Organization
- Authorization
- Enforceability/Validity
- Capitalization (if equity deal)
- No Conflicts (relating to organizational documents only)
- Title to Assets/Equity (depends on industry)
- Taxes
- No Brokers

Survival Periods

Buyer Proposal:

Survival. The Fundamental Representations shall survive the Closing indefinitely. All other representations and warranties herein shall survive the Closing for a period of 3 years. All covenants in this Agreement shall survive the Closing until fully performed.

Seller Markup

Survival. ~~The~~ Each Fundamental Representations shall survive the Closing ~~indefinitely~~ until the expiration of the statute of limitations that is applicable to the subject matter of such representation. All other representations and warranties herein shall survive the Closing for a period of ~~3 years~~ 1 year, at which time they shall terminate and be of no force or effect. ~~All~~ Each covenants in this Agreement shall survive ~~the Closing~~ until such covenant is fully performed.

Eligible Claim Thresholds & Baskets

Eligible Claim Threshold

“Seller shall not be obligated to indemnify the Buyer Indemnified Parties pursuant to Section [___] [i.e., non-fundamental representations] for any individual item where the Loss relating to such claim (or series of claims arising from the same or substantially similar facts or circumstances) is less than [\$___].”

Deductible Basket

“Seller shall not be required to indemnify the Buyer Indemnified Parties pursuant to Section [___] [i.e., non-fundamental representations] for Losses until the aggregate amount of all such Losses exceeds [\$___ / __% of the unadjusted Purchase Price] (the “Deductible”), in which event Sellers shall be responsible only for Losses exceeding the Deductible.”

Tippling / First Dollar Basket

“Seller shall not be required to indemnify the Buyer Indemnified Parties pursuant to Section [___] [i.e., non-fundamental representations] for Losses until the aggregate amount of all such Losses exceeds [\$___ / __% of the unadjusted Purchase Price] (the “Threshold”), in which event Sellers shall be responsible for all Losses regardless of the Threshold.”

Materiality Scrape

Materiality. For purposes of this Article [Indemnification Article], the representations and warranties contained in this Agreement shall be deemed to have been made and Damages calculated, in each case, without any qualifications as to materiality, Material Adverse Effect, specified dollar thresholds or similar qualifications.

Seller Markup to Materiality Scrape

Materiality. ~~Solely~~ ~~F~~for purposes of determining the amount of Damages sustained (and not for purposes of determining whether a breach has occurred) ~~this Article [Indemnification Article]~~, the representations and warranties contained in this Agreement (other than the Fundamental Representations, for which this Section shall not apply) shall be deemed to have been made ~~and Damages calculated, in each case,~~ without any qualifications as to materiality, Material Adverse Effect, ~~specified dollar thresholds~~ or similar materiality qualifications.

Other Limitations on Indemnification

- Cap
 - Applies to What?
 - Fundamental Representations? (maybe separate cap of Purchase Price)
 - Other Representations? (generally a cap applies)
 - Covenants? (generally does cap does not apply)
- Type of Losses
 - Punitive, Consequential, etc.
 - Diminution in Value / Lost Profits
- No Double Recovery (e.g., insurance)
- Exclusive Remedy (other than Specific Performance)
- Sandbagging

Sandbagging

Pro-Sandbagging

A Party's right to indemnification for a breach of any representation or warranty in this Agreement will not be affected by any investigation conducted or any Knowledge acquired at any time with respect to the accuracy or inaccuracy of such representation or warranty.

Anti-Sandbagging

No party shall be liable under this Article for any Losses resulting from or relating to any inaccuracy in or breach of any representation or warranty in this Agreement if the party seeking indemnification for such Losses had Knowledge of such breach before Closing.

Sources of Recovery / Ensuring Performance

- Does Counterparty Have Sufficient Assets?
- Third Party Escrow
- Holdback / Reverse Holdback
- Personal or Parent / Affiliate Guarantees
- Source / Priority of Recourse / Recovery
- Specific Performance

