

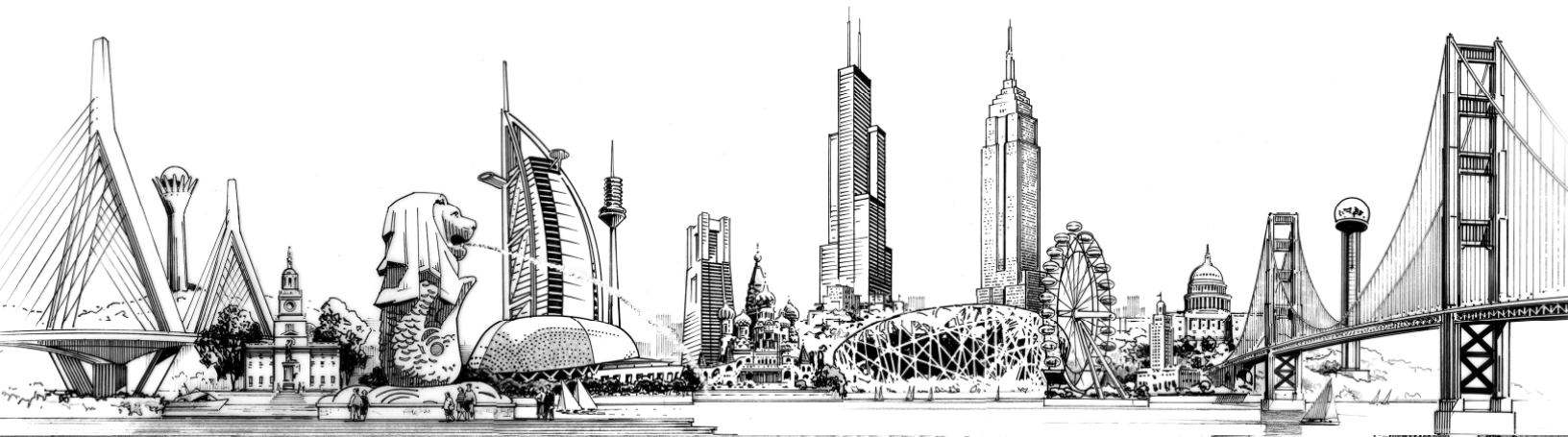
Morgan Lewis

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**NON-DISCLOSURE AGREEMENTS AND LETTERS OF
INTENT (OCTOBER 20, 2015)**

Presenter: John Utzschneider

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Non-Disclosure Agreements and Letters of Intent [October 20, 2015]

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Q: Why allow the confidentiality obligations to ever expire? Would that not mean the recipient then has the right to disclose your confidential information? Outside of information that would become stale over a period of time, such expiry seems risky.

A: Your analysis is correct that, analytically, there is no reason the basic non-disclosure obligation should ever go away. However, buyers and sellers (who are often in the other role, so they see both sides of this) understand the difficulties that arise if, for example, a corporation has amassed 1,000 confidentiality agreements over the last 15 years, and none of them have expired, so theoretically the corporation must monitor compliance with all of them. So a market practice has developed where disclosing parties agree to cut-offs on the confidentiality obligation that gets them comfortable that there is a low likelihood that the information will be valuable after 3 years (for example). This presence of a sunset provision is one of the reasons why these agreements have the provisions requiring return or destruction of the disclosed material – it gets the disclosing party more comfortable that the likelihood of harmful disclosure after the cut-off period is low.

Q: What is your opinion regarding the reasonableness of a limitation of liability clause in an NDA (when consequential damages are generally the primary form of damages suffered)?

A: I almost never see this in an M&A confidentiality agreement, and I think it is unreasonable unless the cap is really high. Even though equitable relief may be available and is typically the remedy that disclosing parties will use to stop future breaches, I think it is tough to argue that a receiving party can breach the agreement, and only be responsible for a portion of the damage this does to the business.

Q: If the seller prefers a stock deal, does the buyer have the option of selecting a 338 election whereby the transaction is treated as an asset sale and realize future tax benefits?

A: The seller can affect the sale as a sale of stock, but the decision to make a Section 338(h)(10) election and have it treated for tax purposes as an asset sale is a mutual decision, so one side can't do this unilaterally. We will cover this issue in more detail in our M&A Academy session on tax issues on January 19, 2016.

Q: Can you explain more fully what clubbing is and how it works? How should clubbing be dealt with in the confidentiality agreement? Can you share a sample provision dealing with clubbing?

A: "Clubbing" is when two or more private equity firms team up to make a joint bid for a target. Sellers do not like these bids because it can eliminate the universe of potential buyers and potentially make the sale process less competitive. The sample NDA provisions used as part of the session yesterday (and available on our webpage) includes a provision that restricts the potential buyer from joining up with other bidders without the seller's consent.

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Q: Can you more fully explain a "clean team." When should it be used? How do you set it up? Can you share a sample provision? Thanks!

A: A "clean team" is a subset of the buyer's due diligence team that is either outside advisers or officers and employees not involved on a day to day basis in pricing and marketing decisions or otherwise is in a position to use the sensitive information in a way that could damage the seller's business or raise antitrust issues. This process is typically set up in a separate agreement between the buyer and the seller that lays out what information is subject to this process, and which personnel are on the clean team and allowed to review this information, and how they can summarize this information for other members of the buyer's management. I will talk to our antitrust team and dig up a sample agreement and send it to you.

Q: What is the relationship between NDA and the confidentiality clause of the definitive agreement (the actual purchase agreement)?

A: You have raised a very good question, and this is a point that a lot of people miss in documenting a deal. My practice on this, when preparing a definitive agreement, is to look at the NDA and decide (i) which provisions should be amended or terminated for the period between signing and closing and (ii) which provisions should be amended or deleted after the closing. For example, it is not unusual to have a confidentiality agreement provide for a three year term, and also provide that the recipient can only use the information for the purpose of deciding whether to buy the business. If that agreement is not revised, then after the closing under the literal terms of the NDA the buyer can't use the information to run the business it just bought! At the signing of the definitive agreement I usually prepare an amendment of the NDA to address these issues.

Q: Did you say that a "non-binding LOI" is still a contract? If so, how do standard rules of contract law apply if it is non-binding?

A: This is little bit of shorthand on my part. When I refer to a "non-binding" letter of intent, that generally means that there is no contractual commitment to complete a deal, and each side is free to decide they don't want to complete the deal. However, these LOI's do typically include some provisions that are binding, such as a commitment by the seller to provide due diligence materials, and an agreement that each side is to bear their own expenses, and agreement by the buyer that it will not contact any employees or suppliers or customers without the seller's consent, etc. Because of those binding provisions, I think these are generally viewed as bilateral binding agreements, with some provisions that are non-binding, and the agreement creates an implied covenant of good faith and fair dealing (assuming that is a recognized concept under the applicable state law).

We hope that you find the foregoing Q&A to be helpful. If you have any other questions on choosing an acquisition structure please contact:

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