M&A Practice Brief

Preparing Your Business Records for a Financing or M&A Transaction

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Is your company considering raising money or anticipating a full or partial exit transaction? If so, there are things you can and should be doing right now (and well in advance of the planned transaction, if possible) to make sure your company is in the best position to enter into a process with an investor or acquirer and position your business for a smooth and efficient transaction. Raising money or selling your business can sometimes feel like a marathon, and much like training in advance can help you achieve better results on race day, preparation in advance for a financing or M&A transaction can put you in the best position to have a successful outcome.

An important piece of any significant corporate transaction is the diligence review of your company by the counterparty. Set forth below are some steps that you can take right now to organize your business records in preparation for such a review. These actions will help you

- identify and fix any issues in advance of a transaction, which will save time and reduce costs at the time of the deal and help avoid concerns from the investor or acquirer
- deliver the company's diligence materials in an organized, complete manner, which will expedite the transaction process
- be ready to prepare management presentation or investor materials that tell a compelling story about your business

Financial Statements and Tax Returns. Make sure that you have copies of the company's financial statements and tax returns for the preceding five to seven years. Financial statements should be reviewed to confirm that they comply with applicable accounting standards. You should have a system in place for tracking the states in which you are doing business and regularly assessing whether the company is required to file tax returns in such jurisdictions. This includes determining whether any sales and use taxes, payroll taxes or other taxes beyond your general corporate income taxes are applicable in such jurisdictions. If you have inaccurate or incomplete tax records or financial statements, you should engage tax and accounting advisers and legal counsel as needed to address any issues in order to avoid delays and other problems at the time of a transaction.

Corporate Governance Materials. Confirm that your company's organizational documents and other corporate governance materials are current and complete and will not prohibit or limit the company's ability to complete a transaction. This involves reviewing your company's certificate or articles of incorporation (or other applicable formation documents) to make sure that that they have been properly signed (and filed with the appropriate Secretary of State in the case of incorporation documents) and that there are no provisions in those documents that would prohibit or limit the company's ability to complete a transaction, that the company is not complying with, or that have become obsolete. You should also locate and review your company's minute books to ensure that signed minutes exist for each meeting of the board and stockholders of the company that has been held, as well as fully executed written consents for any corporate actions taken outside of a meeting. Your legal counsel can help you review the company's governance documents and identify any gaps or potential issues in advance of a transaction.

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Capitalization Records. Confirm that your company's capitalization records are accurate and complete. Periodically, and in connection with each new issuance of securities, review your company's capitalization records to maintain a current and accurate capitalization table and stock ledger (or similar documentation for a non-corporate entity) reflecting all issuances of stock, options, warrants and any other securities and check that you have current addresses for all equity holders. For each equity issuance, you should compile all necessary supporting documentation, including: (i) valid board (and, if applicable, stockholder) approval for the issuance, (ii) a fully executed copy of the issuance document (e.g. subscription agreement, stock purchase agreement, stock option agreement or warrant agreement), (iii) a fully executed stock or other equity certificate, if applicable, and (iv) copies of any federal and state securities filings required in connection with the issuance. You also should confirm that the names and dates on all of the supporting documents have been properly filled in and are consistent across all documents. To the extent your company has issued stock options or other awards under an equity incentive plan, the equity incentive plan and records should be complete and accurate. You should verify that (a) the equity incentive plan was properly approved by the company's board and stockholders, (b) each grant under the plan was validly approved by the board, (c) you have fully executed copies of all the award documents, (d) there were a sufficient number of shares reserved under the plan at the time of each grant, (e) you have copies of any federal and state securities filings required in connection with the issuance, (f) all appropriate tax filings (including Section 83(b) elections, if filed) were timely made and (g) a significant transaction will not result in accelerated vesting of the awards. If you have inaccurate or incomplete capitalization records, you should get legal counsel involved early to avoid additional costs and delays at the time of a transaction.

Contracts. Identify and organize all of your company's material contracts. Material contracts may include customer contracts, vendor agreements, loan documents, leases, license agreements, employment agreements, employee handbooks, independent contractor agreements, consulting agreements, benefit plans and insurance policies. While gathering these contracts, review each one to make sure it (i) is fully executed and properly dated, (ii) is not missing any pages, exhibits, schedules or attachments, (iii) includes all amendments or modifications to the contract, and (iv) has not expired and will not expire prior to the expected date of any proposed transaction. Also, you should identify any contracts that contain any notice or consent requirements in connection with a significant transaction or any provisions that would deem such a transaction a default under the contract or accelerate payments or assess fees or penalties in connection with a transaction. In addition, if you have any oral agreements, "handshake" agreements, or have made promises that have not been fulfilled to any employees, customers, vendors, or investors, you should consider getting those properly documented in advance of a transaction. Company legal counsel can help you review your contracts and identify any potential issues that may need attention in connection with a transaction.

Intellectual Property. Confirm that your company has the proper rights to own or use the intellectual property required to operate the business. You should periodically review the status of all of the company's registered intellectual property and maintain a system for tracking upcoming filing dates and action items for registered intellectual property to avoid missed deadlines or other lapses that might jeopardize the company's ownership of critical intellectual property. You should also (i) confirm that the company has agreements in place with all employees, consultants, and independent contractors assigning rights in the company's intellectual property to the company and obligating those individuals to maintain the confidentiality of the company's sensitive information and (ii) establish a system to ensure that all

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future employees, consultants, and independent contractors enter into these agreements as part of the hiring or engagement process.

Permits and Compliance. Determine if any federal, state, or local governmental licenses or permits are required to operate the business and ensure that the company has and maintains all such licenses and permits. You should review these permits and licenses to determine how they might be impacted by a potential transaction and whether any notice to or special consents from any governmental entities will be required in connection with a transaction.

Beyond improving the transaction process, preparing your business records in this way will instill confidence in a buyer or an investor that you operate an organized and well-run business. It is especially beneficial to get accountants and legal counsel involved early in the process to help mitigate complications, delays and costs at the time of a transaction.

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Brian T. Sullivan is an attorney in the M&A practice group of Wyrick Robbins, which represents clients across a broad range of industries in connection with their significant corporate transactions. The group publishes Practice Briefs periodically as a service to clients and friends. The purpose of this Practice Brief is to provide general information, and it is not intended to provide, and should not be relied upon as, legal advice.

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