

**ANATOMY OF A MERGER: A PRACTICAL GUIDE TO  
NEGOTIATING AND DRAFTING  
BUSINESS ACQUISITION AGREEMENTS**

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The title of this article is a conscious homage to James Freund's extraordinary *Anatomy of a Merger* (Law Journal Press 1975). Although dated in some respects (*e.g.*, an extensive discussion of pooling versus purchase accounting), this book remains the best practical guide for the lawyer engaged in negotiating business acquisitions, full of practical tips and brilliant insights into the strategy and tactics of negotiating business deals.<sup>1</sup>

The purpose of this article is to provide the reader with practical advice based upon the author's forty years experience in negotiating business acquisitions. I have tried to illustrate some of my observations with real-life examples. Some of these observations are truisms; others may be idiosyncratic or even iconoclastic. Oscar Wilde once said "Experience is simply the name we give our mistakes." It is the author's hope that this article will help others avoid some of the mistakes which he has committed.

**I. THE LAWYER'S ROLE**

**A. Lawyers and Businessmen**

Lawyers and businessmen are quite different animals. Lawyers are by nature risk-averse, always imagining the worst-case scenario and capable of producing a parade of horrors at the drop of a hat. For these reasons, we are often unfairly regarded as "deal killers," out to sabotage even the most simple and innocuous transactions.

Businessmen, in contrast, are inveterate risk takers. "Nothing ventured, nothing gained" is their motto. All but the most unsophisticated businessmen know that success comes from evaluating risks in terms of potential rewards.<sup>2</sup>

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<sup>1</sup> Movie buffs and readers of a certain age will recognize the title of Freund's book as a pun on the celebrated 1959 motion picture, *Anatomy of a Murder*, a courtroom drama directed by Otto Preminger and starring Jimmy Stewart and George C. Scott. The movie garnered numerous Academy Award nominations but was overshadowed at Oscar time by *Ben Hur*.

<sup>2</sup> I once had a law partner who seriously contended that he advised his clients *never* to sign a guaranty because "no good could ever come of it;" he thus totally disregarded the "reward" portion of the risk/reward equation.

Businessmen correctly see their job as making decisions in the absence of complete information and are not afraid to do so.

## **B. The Lawyer's Role in Business Acquisitions**

In my view, the proper role of the business lawyer in any business transaction is to help his client evaluate the legal risks involved in a business decision, and not to make the business decision for him. This conclusion follows from the premise that lawyers are, by and large, not as well equipped by training or experience to make business decisions as those persons who are engaged in running their own businesses or are hired by stockholders to run their businesses for them.

The business lawyer must know how businessmen think, and how legal advice fits into the risk/reward calculation. He must, above all, *inform* his clients of the legal risks involved in making business decisions, including the likelihood and the consequences of adverse outcomes. Once the client is fully informed about these legal risks, the lawyer's role is over, and the businessman should be the one making the decision.

## **C. Communicating with Clients**

Business clients often complain that they can't "get a straight answer" from their attorneys. They expect answers that are *prompt, concise, correct and to the point*. They understand that not all legal questions have a black or white answer, but they are frustrated by responses that are verbose and fail to come to a conclusion. Inexperienced lawyers frequently respond to clients' questions by sending a long memorandum resembling a law review article, citing every case decided on a subject, discussing the different conclusions reached in different judicial circuits, and coming to a non-conclusion by listing a string of factors to be considered or giving an "on the one hand/or the other" analysis. They inevitably find that the client is unimpressed by their erudition and frustrated by their failure to give him useful advice. Even though the law or the facts may be in a gray area, it is best to give the client some idea of the outcome of his actions. Businessmen are comfortable with dealing with uncertainties, it is *complete uncertainty* they can't stand. Tell them it is "highly likely," "likely" or "equally probable" that a court would act in a certain way, or, when possible, express the possibilities as a percentage.<sup>3</sup>

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<sup>3</sup> Clients like percentages, but I personally dislike using them because they imply a precision that does not exist. I was once told by a labor lawyer that there was an "87.5% chance" that my client would prevail on appeal. I didn't find that very believable.

## **D. Three Special Cases**

There are three cases in which the role of the legal advisor described above are put to the test: Those involving the dishonest client; the unsophisticated client, and the irrational client.

### **1. *The Dishonest Client***

An important part of assisting a client in reaching a business decision is advising him as to the likelihood of an adverse result (*e.g.*, the practical probability that a stockholder would bring suit challenging an arguably self-dealing transaction), but you should *never* cross the line and advise a client to engage in clearly illegal or unethical conduct on the basis that he is unlikely to get caught. This is not only unethical, but may expose the attorney to civil or criminal liability.

Tax fraud is a good example.<sup>4</sup> The likelihood of a tax audit of a business or individual return is extremely low, but this should never influence you to advise a client to take a chance in the “audit lottery” when there is no legitimate basis for his tax position.

### **2. *The Unsophisticated Client***

Frequently, your client will have little business experience or familiarity with a particular business problem. (The sale of a small business, for instance, is usually a one-in-a-lifetime event for the seller.) In these circumstances, clients sometimes want their attorneys to make the business decisions for them. (We have all heard the statement “my lawyer won’t let me do that.”)

This is an often tempting but always risky situation. In such cases, the best course is for the attorney to try to *educate* the client as to the legal and business context and encourage him to make a decision based on good legal and business advice. A business advisor, frequently an accountant, can be engaged to help. I often find myself saying to clients, “If the decision were up to me, I would (or would not) take the risk and do X; but it’s your money and your decision. Whatever you decide to do, I’ll help you achieve it.”

### **3. *The Irrational Client***

On rare occasions, you will encounter a client who is bound and determined to take a course of action (say, to buy a business) which will have

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<sup>4</sup> A restaurateur once asked me how much cash he could pocket without the IRS getting wise. I of course refused to answer.

predictably disastrous consequences. Advising these clients is like talking lemmings out of going over a cliff. No amount of reason seems to prevail.

I once represented a client with a modest inheritance who dreamed of owning a particular country inn. When the inn came on the market, he eagerly jumped at the opportunity to buy it. Unfortunately, the price he agreed to pay was, in the opinion of all of his advisors, grossly excessive.<sup>5</sup> At my suggestion, he engaged a respected accounting firm to do a set of projections of the future cash flow of the inn. Their calculations showed that he would run out of money in less than a year. Time and again, I tried to convince him of the folly of his actions. I only succeeded in angering him. Ultimately, the deal closed and, sure enough, the inn went out of business a year later and he lost his entire investment.

While I often reflect with sadness on this avoidable tragedy, my conscience is nonetheless clear: I did my duty as an attorney and advisor to dissuade my client from what I correctly thought was a ruinous course of action, but he made his own foolish decision in spite of my best efforts.<sup>6</sup>

On the other side of the ledger, my clients have over the years made many millions of dollars doing deals which I thought were too risky from a business standpoint. Perhaps they were all lucky; more likely, my business instincts were far too conservative, which confirms the wisdom of limiting my role to that of a legal, not a business, advisor.

## **II. SOME GENERAL OBSERVATIONS ON NEGOTIATION**

The business sections of the public library and larger bookstores are full of popular books on the art and science of negotiation.<sup>7</sup> Harvard Law

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<sup>5</sup> Curiously, his bank lender was suspicious that he was *underpaying*, and asked me whether there was some secret cash payment that was not being disclosed.

<sup>6</sup> I sometimes wonder whether I should have resigned as counsel, but I realize that this would not have saved him from the consequences of his actions. He would simply have hired another attorney to do the job.

<sup>7</sup> Some of the better ones are Fisher, Ury and Patton, *Getting to Yes* (Penguin Books, 2d ed. 1991) (“Fisher & Ury”); Nierenberg, *The Art of Negotiating* (1986); Hunt, *Structuring Mergers & Acquisitions* (Wolters Kluwer, 3d ed. 2007), ch. 25; Harbaugh and Britzke, *Primer on Negotiating: Controlling Information and Making and Meeting Offers*, (PLI 2006) (“Harbaugh & Britzke”), Freund, *The Acquisition Mating Dance and Other Essays on Negotiation* (Prentice Hall, 1987); *The Essentials of Negotiation* (Harvard Bus. School 2003).

School, for example, has had a Program on Negotiation since 1983 (website: [www.pon.harvard.edu](http://www.pon.harvard.edu)), and the academic literature on negotiation (including the game theory branch of mathematics) is proliferating at an alarming rate.

There is a general consensus among the authorities that the best negotiator is one who can develop credibility, employ “principled” negotiation rather than “take-it-or-leave-it” positions, and find creative solutions that satisfy the interests of both parties.

#### **A. “Positional” versus “Principled” Negotiations**

The popular literature on negotiation consistently points out the advantages of “principled” negotiation based on the interests of the parties, over “positional” negotiation where the parties take a hard line on a take-it-or-leave-it basis. “Positional” negotiation is often referred to as “adversarial” or “zero-sum” bargaining; “principled” negotiation is often referred to as “problem-solving” bargaining. Dean Harbaugh describes the differences as follows:

“The classic form of bargaining, one that most people envision when they think about negotiating, is the adversarial model. Adversarial bargaining can be conceptualized as a zero-sum process in which the negotiators reduce each issue being negotiated to a finite fungible item, such as money or units to be bought or sold. In the adversarial model, negotiators attempt to get as much money or as many units on their side of the table as is possible. Each dollar or unit gained by one negotiator is taken away from and becomes an equally sized loss to the other negotiator. Adversarial negotiation gets its zero-sum label because the gains and losses of the parties balance off and equal zero.

Problem solving negotiation is conceptualized as a non-zero-sum process in which the negotiators resist reducing the issues to a series of fungible items that can only be divided between the parties. Instead, problem solving negotiators attempt to identify the underlying needs, goals, values and interests of the parties. Once the parties’ needs have been identified, problem solvers seek solutions that satisfy the essential and important needs of all parties without depriving any party of something that is highly valued. The parties in a problem solving negotiation tend to exchange items that each values according to

different standards. In this model, the exchange sheet rarely balances out, and a non-zero-sum label can be applied.” Harbaugh & Britzke, p. 5.

A particularly good example of the distinction between positional and principled negotiations is the breakdown of the negotiations between the Kennedy Administration and the Soviet Union over the nuclear test ban treaty.

“A critical question arose: How many on-site inspections per year should the Soviet Union and the United States be permitted to make within the other’s territory to investigate suspicious seismic events? The Soviet Union finally agreed to three inspections. The United States insisted on no less than ten. And there the talks broke down – over positions – despite the fact that no one understood whether an “inspection” would involve one person looking around for one day, or a hundred people prying indiscriminately for a month. The parties had made little attempt to design an inspection procedure that would reconcile the United State’s interest in verification with the desire of both countries for minimal intrusion.” Fisher & Ury, p. 5

Citing principles to justify a desired result is, of course, part of any lawyer’s stock in trade as an advocate of his client’s interests, and is one of the reasons why lawyers tend to be among the most skillful and effective negotiators.

## **B. The Role of Leverage**

However, I must admit my discomfort with the idea that “principled” negotiation is innately superior to “positional” negotiation.<sup>8</sup> A successful business negotiator need not have superior debating skills if he or she has a thorough grasp of the parties’ relative bargaining power and an ability to leverage that power. Let me illustrate with an example.

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<sup>8</sup> For example, Fisher and Ury’s first chapter is entitled “Don’t Bargain over Positions.”

### **1.      *The Dog in the Manger.*<sup>9</sup>**

Very early in my career, I assisted a very experienced M&A lawyer in negotiating the sale of stock of a closely-held automotive parts manufacturer to a large publicly-held company. The agreed price for 100% of the company's stock was, say, \$5 million. For reasons I have long since forgotten, a sale of stock (as opposed to a sale of assets or a merger) was absolutely essential to the selling stockholders.

The problem to be solved was how to allocate the \$5 million purchase price among the various groups of stockholders. Our client was the founder of the company and owned a majority of the common stock; several professional investment firms owned a class of convertible preferred stock; and a small number of shares of common stock were held by a businessman who had extended the founder credit during the company's start-up phase.

The problem seemed absurdly simple: There were only two classes of stock and the value of the preferred stock on a "cashless" conversion basis was easily determined. The preferred would get X; the common, \$5 million minus X.

But wait. The wrinkle was that the businessman wanted more than his percentage share of the business. The selling shareholders and their counsel met in Manhattan the day before the closing to "iron out" the details. A group of the best and the brightest Wall Street lawyers, investment bankers and accountants hammered away at the recalcitrant businessman and his counsel (whom I recall was his local *divorce* lawyer) all day and far into the night with no success. Finally, in the wee hours, the founder and the preferred shareholders finally relented and agreed to pay the businessman his price.

The stock purchase agreement was then signed and the businessman left. The minute the door closed, the Wall Street types began criticizing his accent, his clothing and his obvious lack of education and financial sophistication. After this had gone on for a while, my senior partner interrupted and said: "*I don't get it. This guy got 150% of the value of his stock; you got 95% of the value of your stock. And you're saying that he's the dumb one?*"

The point of this example is not to disparage "principled" negotiation, but merely to demonstrate that all the principled negotiation in the world cannot trump a determined opponent who knows how to exercise his bargaining leverage. The mistake that the other selling shareholders made in this case was

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<sup>9</sup> The term "dog in a manger" refers to Aesop's fable of that name, in which a vicious dog lies in a manger full of hay, refusing to allow the cattle to eat, even though the hay was useless to him.

not the lack of a skillful presentation of a principled basis for allocating the purchase price, but rather, allowing the businessman to get into a position to veto the deal in the first place.

*As a general rule, “principled” negotiation is most effective when the parties are (or believe themselves to be) in equal bargaining position; where one party has a clear bargaining advantage, he may use “positional” negotiation to his advantage. As a corollary, “positional” negotiation favors the party with the superior bargaining position; “principled” negotiation favors the party with inferior bargaining positions.*

## **2.      *The Myth of the Level Playing Field***

As Freund wisely observes, leverage enters into virtually every business acquisition transaction:

“Rereading today what I wrote years ago about negotiating acquisitions, I’m struck by the implicit assumption that the negotiations take place on a level playing field; *i.e.*, that each party approaches the conference room with the same degree of voluntariness and roughly the same quantum of desire to accomplish the transaction, and that each has a similar willingness, if the significant provisions cannot be worked out to its satisfaction, to walk away from the deal.

Well, that’s not a bad academic model to start from in assessing what can be accomplished through bargaining; but as an insight into today’s real world of M&A negotiations, the premise is a bit naïve. The converse is possibly closer to the facts — namely, that in most deals nowadays, one or the other of the parties has arrived at the table in less voluntary fashion, possesses a stronger desire to achieve a negotiated outcome, and has a greater reluctance to terminate the negotiations unsuccessfully.” Freund, *The Acquisition Mating Dance*, p. 51.

Bear in mind that using “positional” or “principled” negotiation is not an “either or” proposition. Finding the right mix is part of the art.



### **C. Types of Leverage**

What factors create positive or negative leverage in negotiating business acquisitions? A non-exclusive list would include: compulsion, desire, competition, time, and personal career objectives.<sup>10</sup>

#### **1. Compulsion**

The first factor - which applies most often to sellers – is whether the party is forced by legal or practical necessity to enter into an acquisition transition. Underlying reasons may include the party's adverse (or desperate) financial condition, the death, incapacity or retirement of a principal stockholder or key employee, need to pay unexpected liabilities (*e.g.*, estate taxes), or stockholder disagreements. Technological or industry competition may also compel a decision to buy or sell, as when a key patent expires or is found to be infringing, or when a competitor has developed new technology or some other competitive advantage over the company which it can overcome only by combining with another firm.

#### **2. Desire**

A key factor in determining leverage is the answer to the question: Who wants the deal more?<sup>11</sup> When the seller has a unique product, market niche or asset, and is under no compulsion to sell, the playing field usually shifts in its favor. For purely personal or psychological reasons, a buyer may have a burning desire to buy a country inn, a sports team, or some other ego-gratifying business, or perhaps to become a CEO of a public company. For similar reasons, a founder of a business may be reluctant to part with "his baby," or the seller's management may be loathe to relinquish the perks and prestige that they possess.

#### **3. Competition**

There is a saying in the business brokerage business that "one buyer is no buyer." The pressure on the buyer to make concessions rises dramatically when it is faced with an "auction" situation involving multiple contestants for an acquisition. In such situations, the buyer is forced to come quickly to his "best price" for fear that another bidder may acquire the company for a lower price. The opportunities for a seller to play bidders off against each other here is a powerful advantage. Contrast this situation with one in which there is only a single buyer and a single seller; there the buyer is much more inclined to test the

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<sup>10</sup> See Freund, *The Acquisition Mating Dance*, pp. 54-57.

<sup>11</sup> See Freund, *The Acquisition Mating Dance*, pp. 115-123.

seller's resistance to a price or terms which are less than the buyer's best offer. The same dynamics apply when the buyer has multiple acquisition opportunities, and there are few or no competing buyers.

#### **4. Time**

Time is often a vital factor in determining leverage. A party faced with a deadline to complete an acquisition is at a great disadvantage to an adversary which can proceed on a more relaxed time schedule. Consider the bargaining position of a company which is about to lose its lease on a vital manufacturing facility or a key government contract, or is faced with an adverse change in the tax laws which takes place January 1 of the following year.

#### **5. Personal Career Objectives.**

In negotiating with large business organizations, the personal career motivations of individual officers may play a major role. The retiring CEO of a major company may be unwilling to cap a distinguished career by making a risky acquisition which would tarnish his reputation. A new CEO, on the other hand, may want to embellish his reputation by showing that he can make a major or important acquisition. The psychology of the individuals involved in acquisition negotiations should always be considered: Mr. Jones is usually thinking about whether this deal will advance him up the corporate ladder or result in his firing.

#### **D. Evaluating and Manipulating Leverage (The Concept of BATNA)**

The factors affecting a party's leverage are usually *external* to the legal issues presented in negotiating a business acquisition, and are frequently unknown to the attorney. Yet ignorance or misperception of the parties' relative bargaining power will always complicate negotiations and may even doom them to failure.

A thorough analysis of the parties' bargaining power should be made at the earliest stages of acquisition planning. This requires, at a minimum, a meeting between the client and its attorneys in which a realistic assessment is made of the parties' strengths and weaknesses, and a decision is made as to the "realistic outcome" of the negotiation process. If your seller client is dealing with one buyer and is under time pressure or compulsion to sell, it should realize that it cannot realistically expect to get its top price or to get "all the meat off the bone" in negotiating the terms of the deal. If your client is in a strong bargaining position, its "realistic outcome" would be more favorable. In either case, the success or failure of a business acquisition negotiation should be measured by the parties' success in obtaining the "realistic outcome" as opposed to some other standard.

### **1.       *The Importance of Perceptions***

Negotiation, like poker, is a psychological game: its outcome frequently depends on the parties' *perceptions* of their relative bargaining power, more so than their *actual* bargaining power. If your opponent believes you have pocket aces, you are in a strong negotiating position, even if you do not have them. It is important that you be aware of the *actual* strengths and weaknesses of your opponent's position and that your opponent be aware of your client's actual strengths *but not its weaknesses*.

### **2.       *What's the Bottom Line?***

You should explore with your client in advance what its "bottom line" is. That is, at what point does it make sense to walk away from the deal, rather than keep on negotiating? This concept is most often used in price negotiations, but also applies to key non-price terms. Defining a bottom line in advance allows your client to resist the pressure and temptation to be too accommodating in an effort to bring the negotiations to a conclusion. There are, however, two things to beware of: First, clients tend to be less than candid with their attorneys when it comes to disclosing a bottom line price, usually due to the fear that the attorney will too readily concede that price rather than negotiating for a better price. Second, focusing on the bottom line limits your flexibility to negotiate alternative terms, and inhibits the exploration for creative solutions which can satisfy both parties.

### **3.       *Using BATNA***

The concept of "BATNA" (Best Alternative to a Negotiated Agreement) is often said to be preferable to a single bottom line position.<sup>12</sup> A party's BATNA is the answer to the question "What would you do if this deal did not go through?" Sometimes the alternative is simple: "We'd simply keep on operating the business at a profit," or "We'd buy another company with an equally strong foreign distribution network." Sometimes the alternatives are not so attractive: "We'd have to go out of business," or "We'd lose our competitive position in the marketplace." The benefit of doing a BATNA analysis is to give your client a realistic idea of its bargaining power and to act accordingly.

### **4.       *An Illustrative Tale***

BATNA analysis does not imply passive acceptance of the *status quo*. Smart companies often *develop* alternatives which strengthen their bargaining position. The following example illustrates how thinking in terms of BATNA

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<sup>12</sup> Professor Roger Fisher is usually given credit for having developed this elegant concept and its hideous acronym.

can lead to creative business strategies. It is noteworthy that none of the parties to this transaction had ever heard of the term “BATNA,” and were led to an advantageous result by their application of common sense rather than academic concepts.

Several years ago, I represented a group of investors interested in developing a large parcel of land surrounding a golf course on Cape Cod. They secured an option to purchase the land and proceeded to apply for local zoning permits. Their development proposal met with furious community resistance and led to a proposal from the town to purchase the land for conservation purposes at a very attractive price. However, the town’s proposal required town meeting approval, a process which could not be completed until several months after the clients’ option to purchase the land was scheduled to expire.

Our clients first approached the landowner to negotiate an extension of the option. Since the town’s proposal had been widely publicized, the landowner was aware of our client’s precarious position and was ready to drive a very hard bargain. However, our clients were up to the challenge: Although no bank lender was then willing to make them a land acquisition loan, they located a private investor who agreed to lend them the full purchase price, albeit on terms that can only be described as usurious.

The clients then approached the landowner and offered him two alternatives: Either extend the option period for three months in consideration of a percentage of our clients’ profit on the resale to the town; or close on the sale upon the original option terms. The landowner initially attempted to call our clients’ “bluff,” but after a day of furious negotiations on the option expiration date, finally agreed to terms. Our clients went on to sell the property to the town at a handsome profit.

### **E.        Synthesizing The Two Approaches**

I have pointed out above the importance of understanding the concept of leverage. But the successful deploying of leverage will accomplish only so much; even if your client has the bargaining advantage, a non-negotiable demand can cause ill feelings and at best will force your opponent (and its counsel) to “lose face.” It is far better to marshal a reasonable argument why your client needs a particular contract provision, and dig your heels in on that matter of “principle.” Your opponent can more easily concede to a reasoned argument than an ultimatum. The “fist in the velvet glove” approach is very powerful because it combines both “positional” and “principled” negotiations.

My conclusion is that one should always employ the “principled” method of negotiation, involving marshalling arguments and finding compromises, but be ever mindful of the parties’ bargaining strengths and weakness.

### **1.        *Marshalling Arguments***

The ability to marshal an argument *pro* or *con* a given proposition is the lawyer's stock-in-trade, but its execution does require some thought and advance preparation. You should approach any acquisition negotiation knowing the reasons for the particular contract provision you are advocating and the best arguments in support of that proposition. "I find that rarely is a negotiator able to win a point when he has no cogent argument to support his position, except where the bargaining strengths are unequal." Freund, *Anatomy of Merger*, p. 14.

### **2.        *The Creative Discovery of Common Ground***

Every successful negotiation involves finding compromises which both parties are willing to accept. When the parties cannot agree on a provision after giving principled arguments *pro* or *con*, the resolution of the issue requires the finding of a creative solution which will satisfy both parties' interests. This involves exploring with your opponent the real reasons for his reluctance to accede to your position. A cooperative, problem-solving attitude on the part of both parties is essential. Sometimes a concession on another issue (particularly involving money), is sufficient to overcome the other party's resistance.

Freund believes, as I do, in the "ultimate solubility of most issues"<sup>13</sup> through creative problem-solving. Here is an example.

I once negotiated a buy-out of a corporate stockholder where a large part of the consideration was paid in the form of a five-year consulting contract for, say, \$100,000 per year. The selling stockholder insisted on the continuation of the payments even if he died within the consulting period. My client had no business objections to that arrangement, but was very concerned that the *post-mortem* continuation of payments would transform the contract from a tax-deductible service contract to a non-deductible payment for the purchase of stock. The solution which we found was to provide the consultant (at the company's expense) with a five year \$500,000 declining term insurance policy, the face value of which declined by \$100,000 per year. If he died within five years, the company would be spared the cost of paying the remaining consulting payments, and the stockholder's estate would receive the full value of the contract on an accelerated basis. Both sides would win.

### **3.        *Playing the Leverage Card***

When the parties have reached an insoluble impasse in negotiation and your client has the bargaining advantage, it is time to assert your client's leverage. This should be done in as diplomatic a manner as possible: "Look, I

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<sup>13</sup> Freund, *Anatomy of a Merger*, p. 21.

understand the importance of this issue to your client, but my client simply can't agree with it. If you can't concede on this point, let's call the deal off, shake hands and remain friends."

When the other party plays the leverage card, it is the moment of truth for your client. You should, of course, persist in trying to find a creative solution to the impasse, but if you can't, your client must decide whether its bottom line has been reached and whether it will either concede the issue or walk away from the deal and accept its BATNA.

Paradoxically, this is usually an opportunity for you to test your opponent's *real* leverage by calling its bluff. If your client is in fact willing to walk away from the deal, there is no risk in testing your opponent's threat to do so. On the other hand, if your client is willing to concede, there is only a *little* risk to ignoring this ultimatum, so long the parties can revive the negotiations after a period of sulking in their tents. I have found that if your opponent is willing to accept your concession today, he will be equally willing to accept it a week later, when your client calls and says that after a week of soul-searching, it sees the wisdom of the opponent's position.<sup>14</sup>

Of course, this sort of brinksmanship should only be employed if you have the unqualified support of your client and have weighed the risks and rewards of the gambit.

### **III. BE PREPARED: GATHERING AND PROTECTING INFORMATION**

"Information is crucial to the outcome of bargaining. Indeed, research into negotiation outcomes suggests that there is a strong correlation between the control of critical information in negotiation and a successful outcome. The party that better controls the critical information in the negotiation does "better" no matter how that term is defined. This correlation between the control of information and outcome prevails without regard to the strategic approach of the negotiator. Thus, whether you decide to proceed as an adversarial negotiator or as a problem solving bargainer, controlling the critical information is a key to success.

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<sup>14</sup> The big exception to this rule is when the other party is about to irrevocably change its position after terminating negotiations, for example, by accepting an offer from another competing bidder.

Without information, a negotiator cannot effectively determine bargaining ranges and rationales, cannot identify underlying needs or possible solutions, cannot know what arguments will persuade, what promises are valued, and what threats or warnings will be feared, and cannot measure the accuracy of an opponent's statements or decide when to accept an offer or press for more. Without information, a negotiator is handcuffed by his or her needs and position, [and] unable to recognize and appreciate the other party's goals, needs, values and concerns." Harbaugh & Britze, pp. 15-16.

#### **A. Know the Law**

Business acquisitions require at least a basic knowledge of corporate law, tax law and securities law, as well as an understanding of any regulatory requirements to which the parties are subject. An understanding of basic accounting rules and principles and common business valuation methods is also essential. Negotiating a business acquisition also requires that you be able to deal with basic issues of employment law, real estate law, environmental law, ERISA, intellectual property law, commercial law, antitrust law (including the Hart-Scott-Rodino Act) and the laws of other states or countries. Although the lead attorney can and should rely on the expertise of other attorneys specializing in these areas, he or she must be able to spot the issues as they arise and converse intelligently with the experts regarding the specifics of a given transaction.

Freund – perhaps with tongue in cheek – identifies ten “non-traditional roles” that M&A lawyers are called upon to play: financial whiz, public relations expert, writer, psychologist, moralist, employee benefits consultant, stock market analyst, businessman, generalissimo and seer.<sup>15</sup>

#### **B. Know the Facts**

The type of information needed to negotiate intelligently and competently can be classified into “historical facts” and “motivations.”<sup>16</sup>

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<sup>15</sup> Freund, *The Acquisition Mating Dance*, pp. 110-114.

<sup>16</sup> Harbaugh and Britzke refer to motivations as “intentional (or emotional) facts.” Harbaugh & Britzke, p. 16. This terminology seems a bit confusing and counterintuitive, and I favor the term “motivations” which I use here.

## **1. *Historical Facts***

Historical facts include all publicly available information regarding the parties and, of course, all the information regarding the seller produced in the due diligence process.

The more you know about your client's business, the better equipped you will be to understand, articulate and protect its interests in the negotiations. If you are representing an existing client, you probably already know a lot about its business, its legal structure and corporate governance. If not, you need to get up to speed. What is your client's financial condition? Ask for a copy of its financial statements.

What do you know and what can you learn about the opposing party? If it is a public company, read all of the available public information, including annual reports, 10-Ks, 10-Qs, proxy statements and registration statements. Research the backgrounds of its management team and read the public documents containing the text of similar business acquisitions to which it has been a party.

## **2. *Motivations***

Motivations are equally important. The "needs, goals, values, fears, hopes, resources, ambitions, interests, anger, guilt, greed, jealousy and anxiety" of the parties will to a great extent determine their behavior.<sup>17</sup>

If your client is a seller, make sure you know the reasons for the sale. Is it under some compulsion to sell, such as the disability or death of the principal stockholder? Does the principal stockholder simply want to cash in his investment and retire? Are there pressing debts to be paid? Are there multiple potential buyers or just one? How will employees, customers, competitors or regulators react to the announcement of the deal?

If your client is a buyer, what are its motivations for acquiring the seller? Is your client a financial buyer or a strategic buyer? Are other potential buyers for the seller likely to appear? Is this a geographic extension or product extension acquisition? How important is continuity of the seller's management or workforce to your client?

The opposing party's motivations are always more of a matter of conjecture. The best one can hope for at the inception of the negotiation is to develop "confident expectations" of the opposing party's motivations. The challenge to the negotiator is to test these expectations by obtaining information in the course of bargaining and to adjust to changes in circumstances.

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<sup>17</sup> Harbaugh & Britzke, pp. 16-17.



### **C. Assessing Informational Needs**

Harbaugh and Britze suggest that a lawyer and his client prepare for a negotiation by creating an “information assessment agenda,” containing three columns of information: “[1] information that you *need* from the opponent to confirm or deny your confident expectations; [2] information that you want to *protect* from the other side because of its sensitive nature;<sup>18</sup> and [3] information you want to *give* to the opposition to influence their perception of the situation.” Harbaugh & Britzke, p. 17 (emphasis in original).

Harbaugh and Britzke further recommend that the lawyer and his client “prioritize” the information in each column, anticipate the other party’s information assessment agenda and rehearse their responses to anticipated questions.

### **D. Obtaining Needed Information**

How does a negotiator go about obtaining information – particularly information regarding motivations – from an opponent? Simple. You ask for it. (And you thought all that shop talk between lawyers during negotiations was just idle chit-chat.)

Broad, general and non-leading questions are best designed to elicit information: “What do you think a reasonable time schedule would be to close this deal?” Follow-up questions should be more specific. “That seems pretty short to me. Is there any reason why you couldn’t extend the time schedule to x months?” A good negotiator must be a good listener. Don’t dominate the conversation; let the other guy talk, and observe his non-verbal communication. You will be amazed at what people are willing to tell you.

### **E. Protecting Sensitive Information**

When your opponent probes for information about the “smoking gun” or the “skeleton in the closet,” there are only three possible responses: Honesty, misrepresentation, and evasion. Honesty has an obvious downside. Misrepresentation is unethical and may expose you and your client to legal

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<sup>18</sup> Of course, in the M&A context, protected information would certainly *not* include historical facts required to be disclosed by a seller as a part of the due diligence process for obvious legal and ethical reasons, as well the seller’s self-interest in avoiding the consequences of misrepresentation. Seller’s motivations, on the other hand, do not have to be disclosed. See footnote 19 *infra*.

liability.<sup>19</sup> Evasion is the only safe alternative: answer a question with a question, over- or under-answer a question, answer a different question, rule the question out-of-bounds, ignore the question, or (truthfully) deny knowledge.

#### **F. Setting the Table**

Most acquisition negotiations these days are conducted *impersonally*: One attorney prepares a draft of a letter of intent or acquisition agreement and emails it to the other party's counsel, who marks up the draft or revises it and sends a redlined version back. The drafts volley back and forth until all but a few difficult issues have been resolved, and the attorneys then speak by phone to deal with these issues. This is an efficient way to clear away the underbrush of trivial issues and language clarification, but it is a terrible way to obtain or communicate valuable information. Try to meet in person with opposing counsel or at least engage him in an open-ended discussion if you want to maximize your chances of discovering critical information.

### **IV. THE ESSENTIAL ATTRIBUTES OF A GOOD NEGOTIATOR**

Most of the non-academic works on negotiation acknowledge that they are an attempt to "organize common sense and common experience in a way that provides a usable framework for thinking and acting" and that negotiation skills cannot be taught from a book but must be acquired by practice. The following ground rules for negotiation are not novel insights and should come as no surprise to any practicing attorney.

#### **A. Credibility**

Establishing your credibility is an absolutely essential element of a successful negotiation. Bluffing and blustering may sometimes get results, but these are high risk strategies which can poison the entire atmosphere of a deal. Consider your own reaction to discovering that the other party to a transaction is lying about a key element of the deal.

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<sup>19</sup> Supreme Judicial Court Rule 3:07 adopts the Massachusetts Rules of Professional Conduct. Rule 4.1 (Truthfulness in Statements to Others) states that "[i]n the course of representing a client a lawyer shall not knowingly (a) make a false statement of material fact or law to a third person." There is some wiggle room, however. Comment [1] provides that "A lawyer . . . generally has no affirmative duty to inform an opposing party of relevant facts" and Comment [2] states that "Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party's intentions as to an acceptable settlement of a claim are in this category."

“Be yourself” is particularly good advice for establishing credibility.

“First point: everyone has his own negotiating style, and the worst thing you can do is to adopt a negotiating technique that does not feel comfortable, simply because a man in a book says that he uses it to advantage. In *my* book, credibility, based on an evident sincerity, is the most important single asset of a good negotiator.

This applies both to form and substance. If you are using an uncomfortable negotiating style and not exuding credibility, you will probably get nowhere; if gambits are not your forte, and you are bumbling through one that somebody mentioned on page 81, it will boomerang. With respect to substance, you should only ask for what you feel you can reasonably support. Try for more and your arguments don’t ring true; ultimately the hollowness in your approach will show up and get you in trouble. Some experienced negotiators go even further and ask only for what they actually think the other side *should* give them. Which brings us back to the same basic idea: you must feel comfortable in what you are doing.” Freund, *Anatomy of a Merger*, p. 10 (emphasis in original).

A good way to establish credibility is to demonstrate early in the negotiations that you are willing to concede an issue to opposing client if he makes a reasonable argument. Suppose, for example, that the letter of intent does not provide the seller with registration rights for the resale of the buyer’s stock being issued in a merger. As buyer’s counsel, you have discussed this issue with your client in advance, and you have confirmed that your client does not regard this as a serious matter. Graciously conceding this issue (without asking for something in return) establishes your credibility as a reasonable person who is not “out to screw” the seller.<sup>20</sup>

There may be times when you may even want to make a concession that has not even been requested, to establish a *rapprochement* which may stand you in good stead at a later time. Suppose while you are drafting the first draft of the acquisition agreement, you call the other party’s attorney and say: “It just dawned on me that we didn’t discuss registration rights in the letter of intent. I

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<sup>20</sup> This is an exception to the general rule against uncompensated concessions which holds that you should always get a *quid pro quo*.

have spoken with my client and he has agreed that this is something that your client may want, and that we can provide your client with piggyback rights without serious cost.” Not only will this ingratiate you with opposing counsel (whom you may have spared a certain amount of embarrassment), but it will also be difficult for him to look this gift horse in the mouth and insist upon demand registration rights. This technique is particularly appropriate where you feel that it is only a matter of time before opposing counsel spots the problem and insists on these rights.<sup>21</sup>

## **B. Perspective**

### **1. *Know What’s Important***

In the give-and-take of negotiation, it is essential to understand that *all issues are not of equal importance*. Knowing which issues are truly important to your client (and which are not) will guide you in managing the negotiation process.

Avoid playing “Trivial Pursuit.” Much of the time and money spent on negotiating business acquisitions is spent on “lawyer’s issues” (by which I mean those issues which the client delegates to his lawyers because he either doesn’t care about or understand them). Be aware that you are going to have to make concessions in order to do the deal, and don’t make a molehill into a mountain.

Far too frequently, law firms delegate the negotiation of the terms and conditions of acquisition agreements to associates who, though intelligent, thorough and motivated, are not adequately briefed by a partner on the client’s needs and motivations. As a result, negotiations often tend to focus on issues the client would regard as trivial or nonessential instead of the truly important issues that advance the client’s interests.

### **2. *Take a Long-Range View***

The negotiation of a business acquisition is very often the first encounter in a long-term relationship between the principals of the seller and the buyer. If the seller’s principals become part of the buyer’s management team, they will have to develop a cooperative working relationship with the principals of the buyer. In any event, there may be post-closing agreements (for example, consulting contracts or supply contracts) between the parties that will require them to deal with each other over the long term.

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<sup>21</sup> One of the many advantages to preparing the first draft of the agreement (*see* “Volunteering for the Draft,” Section IV *infra*), is that you can build in to the first draft a few unresolved, squanderable points like this.

Smart clients will often say to their attorneys: “Look, I’m going to have to live with this guy to run a key division of my company. I don’t want to start off on the wrong foot by having him think he’s been cheated or short-changed on some minor point in this deal.” Smart lawyers will raise this relationship issue with their clients when the negotiations get sticky or contentious.

On the eve of a recent closing, I pointed out to my client (the buyer), that the seller had made an error in the calculation of the closing adjustment for vacation pay. The seller thought it owed my client \$12,000, when it in fact was owed \$36,000 *by my client*. At the closing, my client, with my encouragement, insisted that the amount be correctly recalculated, reasoning that passing up a \$48,000 benefit in a \$10,000,000 acquisition was a small price to pay for the good will this gesture generated with the seller (or to avoid the potential ill will that would have been created if the mistake were discovered post-closing).

### **C. Persistence**

“It may well be that the most important ingredient for pursuing a difficult negotiation is a prior good night’s sleep. As an exhaustive session draws to a close, all of us have given up on points that would not have been conceded in the early bargaining, when we were relatively fresh. The same incentive to drive a hard bargain just doesn’t exist when you are physically and mentally tired. There is a tendency to want to ‘wrap it up’; often the price for such finality is to forego secondary goals. All of which is to point up the obvious fact that, like the proverbial tortoise and hare, the persistent, unruffled, untiring lawyer will more often than not ultimately prevail over his flashy but early-wilting antagonist.” Freund, *Anatomy of a Merger*, p. 25.

Persistence is also essential to creative problem-solving. When an impasse arises, your efforts to find a solution should be relentless. Don’t give up. *There is a solution*; it just takes time and dogged determination to find it. The best negotiators will find creative solutions not merely because they are creative thinkers, but also because they won’t quit. Remember: Persistence trumps talent.

### **D. Timing**

#### ***1. Magic Moments***

Knowing *when* to raise an issue or seek a concession is an invaluable talent. There are certain “magic moments” in the course of acquisition

negotiations when certain issues should be raised. One is at the letter of intent stage, when the buyer's appetite for the acquisition is usually at its highest point. A smart seller's counsel will press for important non-financial concessions at this stage (limitations on indemnification are a good example). Once the drafting of the acquisition agreement has been delegated to the buyer's attorneys, the buyer usually loses interest, while his attorneys ferociously defend the pro-buyer protections they inserted in the agreement.

Another magic moment is at or near the closing. As the parties approach the finish line, there is a psychological gravitational force which pulls them together. At this moment, the parties will often make concessions to "get the deal done" which they would never have made a few weeks earlier.

It is frequently useful to call attention to issues of vital importance ("deal-breakers") early in the negotiation process, often at the letter of intent stage. ("Look, the outside investors (or my ex-wife) are not going to personally guaranty the company's reps.") This has the advantage of emphasizing the seriousness of the issue to your client, getting the attention of the other principal, and avoiding a waste of time and money if the parties cannot agree on an essential deal point.

The problem with this strategy is that the other party may in fact *not* consider your client's issue to be of very great importance. But once you have signaled how important the issue is to your client, the other party may extract an appropriately large concession as a price for agreeing on the issue. The better approach may be to raise the big issue more casually, in the context of a number of trade-offs.

Another occasion on which it is advisable to remain silent regarding a significant issue is when the issue would be resolved in your client's favor as a matter of law. For example, *Tobin v. Cody*, 343 Mass. 716 (1962), holds that the seller of a controlling stock interest in a corporation is subject to an implied covenant not to compete with the buyer. As buyer's counsel, you should consider whether to specifically provide for a non-compete covenant (which opposing counsel may try to dilute or negotiate away) or to take the bird in the hand offered by the caselaw.

## **2. *Time Pressure***

External factors often impose time limits on completing a transaction which require the parties and their attorneys to negotiate under pressure. More often, the importance of one or both parties to "get the deal done" creates an artificial deadline. Time pressure can be used to your advantage. When the other party is anxious to act quickly, you should move deliberately; this will increase the likelihood that your opponent will make concessions.

Early in my career, I had the responsibility of negotiating on behalf of a tenant a series of lease amendments for a large industrial complex owned by a wily and parsimonious New York real estate investor with approximately 50 years more experience than I. Our first negotiation session in Manhattan started at 10:00 a.m.; by late afternoon we had made virtually no progress. At about 4:00 p.m., however, the investor suddenly proposed a half dozen major concessions; I promptly counteroffered and fifteen minutes later, we had a deal. His secretary later told me that day that the investor always met his father for drinks every day at 5:00 p.m. at the Rainbow Room. Armed with that information, I scheduled every negotiating session thereafter to start no earlier than 3:00 p.m.

## **V. VOLUNTEERING FOR THE DRAFT**

He who drafts the contract has the upper hand in the ensuing negotiations. There are so many opportunities in drafting a contract – “choices in the introduction and phrasing of concepts, the omission of certain language, the deliberate use of ambiguity and so on” (Freund, *Anatomy of a Merger*, pp. 26-27) – that the draftsman is able to set the agenda for the negotiations. The recipient of the first draft is placed in a defensive position of responding to the draftsman’s choices rather than initiating the agreement on his own terms. Controlling the drafting of the agreement also allows you to control the timing of the negotiations, which will proceed as fast – or as slow – as you and your client choose.

For this reason, the astute attorney will always seize the opportunity to prepare the first draft. Because the prevailing etiquette is that the buyer’s counsel drafts the acquisition agreement, the seller is more often at a disadvantage. Nonetheless, you should always try to take control of this assignment, or at least to draft significant portions of the agreement.

Penurious clients sometimes unwisely prefer that the “other side” do the drafting in order to economize on their legal bills. You should point out to your client in advance that the benefits of drafting the agreement outweigh the burdens. Occasionally, you can persuade the other side that by taking on the burden of drafting the agreement you will be saving them money.

### **A. The Unforgivable Sin**

Transactional lawyers are inveterate copycats, preferring to mark up the version of an acquisition agreement used in the most recent deal. This is a terrible mistake. Not only is each deal different in significant ways (the last deal may not have involved significant real estate, intellectual property, or governmental approvals), but the last deal also reflects the results of negotiations that you may not want to concede in the current deal. As Freund points out,

“I want to call special attention to one cardinal sin that I find young (and often mature) lawyers commit time and again. The ABC deal comes in to the office. The partner evaluates it, calls in an associate, gives him the facts, and tells him to prepare a draft ‘modeled on the XYZ acquisition that we did in January.’ The associate goes to the shelf, pulls down the thick black binder on the XYZ deal, makes a photocopy of the agreement and proceeds to mark it up for the ABC deal. Fatal, fatal error. Do you know why?

“The reason is that the XYZ agreement which found its way into that binder was the final, executed, *negotiated* agreement. Using it as a model for a first draft bequeaths to the ABC lawyers, gratis, the work product of the XYZ lawyers. All of the provisions that you struggled so hard to resist and finally compromised – the additional purchaser’s representations, the ‘materiality’ limitations, the ‘knowledge’ caveats – are fixed firmly in place. What the associate should have done, of course, was to go back to the *first draft* of the XYZ deal in the files, and mark that up. But believe me, this happens over and over, and you don’t always catch it before the draft agreement is delivered to the other side.” Freund, *Anatomy of a Merger*, p. 142.

## **B. One Size Does Not Fit All**

Word processing software is a wonderful invention. It allows us to draft in minutes documents which once took hours or days to create. But every stock purchase transaction is not like every other stock purchase transaction. Before marking up a standard office form, you must first understand the particular business context in which your client is operating. Is the seller under some compulsion to sell? Are there other buyers or other alternatives to selling the company? What is your client trying to accomplish by selling the company?

Knowing your client’s business needs and motivations is essential to drafting and negotiating a deal that makes sense.

An example may help. My oldest client is a large multi-state distributor of industrial supplies. It has made nearly 100 acquisitions during the past four decades, nearly all of which involve a cash purchase of another distribution company in a new geographic market. The basic structure of almost every deal is a purchase of the seller’s inventory at book value and a purchase of



the other fixed assets – usually including real estate – at their appraised fair market value; the client agrees to collect the seller’s accounts receivable and remit the proceeds. The client is indifferent to the financial condition of the seller, its customer base, its workforce and its brand name and usually assigns no additional value to goodwill. Why? Because the client is looking for one thing only: A new branch location from which it can deliver commodity products using its own well-developed skills in purchasing, pricing and marketing. The form of asset purchase agreement used for these transactions should be quite different from the agreement you would draft for a financial buyer concerned with retaining existing management and assuring continuing future earnings and cash flow.

### **C. Extremism is No Virtue**

The draftsman may be tempted to draft a “perfect” pro-buyer (or pro-seller) document, which skews every clause in favor of his or her client. This strategy is occasionally successful when one is dealing with an inexperienced attorney on the other side. More often, however, it is a formula for complicating and slowing down the negotiation process, by inviting objections to provisions where a more balanced and “reasonable” solution would be perfectly satisfactory to your client.

When representing a seller, I have found that observing at an early stage that the negotiations will go more smoothly if the buyer’s counsel gives me his “second draft” rather than an objectionable first draft, is an effective way of making this point, particularly with an experienced M&A attorney on the other side.

### **D. Riding the Coattails**

Occasionally, a party – particularly a public company – will have made a number of similar acquisitions which are a matter of public record with the SEC or elsewhere.

This can be a treasure trove of information, showing the points the client was willing to concede in other transactions. You should always investigate the buyer’s SEC filings to discover possible issues for negotiation. It is very difficult for the buyer to insist upon language in an acquisition agreement when the seller points out that the buyer gave an entirely different clause to XYZ Corporation.

When representing a company with a public track record of this sort, you should be alert to this negotiating gambit and be prepared to distinguish the XYZ deal from the deal you are negotiating. On occasion, it is possible to turn this gambit on its head, by arguing that giving the seller a certain concession

would “open the floodgates” by compelling your client to give a similar concession in all its future acquisitions.

## **VI. DEALING WITH THIRD PARTIES**

In a typical business acquisition, an attorney will interact with various players other than the buyer, the seller and their attorneys. These may include investment bankers, business brokers, accountants, government agencies, and a host of other consultants and service providers. The following are my views on dealing with a few of the most common relationships.

### **A. Investment Bankers and Business Brokers**

These parties can add real value principally by locating potential financial and strategic buyers for the seller’s business, advising on conditions in the M&A market and acting as salesmen for the transaction. Investment bankers frequently advise publicly-held buyers on issues of valuation and corporate strategy and often assist buyers in locating acquisition financing.<sup>22</sup>

Since these parties are usually compensated on a contingent fee basis, and are compensated only if the transaction is consummated, they have an inherent conflict of interest. They have a natural bias towards encouraging the seller and buyer to “make a deal,” which can make their advice less than objective.

Some investment bankers tend to regard themselves as super lawyers, freely dispensing legal and tax advice to your client. This can lead to awkward situations when their advice conflicts with yours. My approach to this problem is usually to be respectful and grateful for any assistance in evaluating legal issues (particularly from experienced and sophisticated advisers), but to be firm about the role that the lawyer must play as the client’s primary legal advisor.

### **B. Accountants**

A client’s accountants play a vital role in performing financial due diligence and in providing tax and accounting advice to your clients. Transactions with publicly-owned companies often raise SEC accounting issues

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<sup>22</sup> A special role is played by an investment banker engaged to provide a “fairness opinion” stating (usually to a seller) that the transaction is “fair from a financial point of view,” to the seller and its stockholders. This can provide protection to the seller’s board of directors against stockholder claims of breach of fiduciary duties, since the business judgment rule allows the board to rely on the opinions of outside experts. The topic of fairness opinions is beyond the scope of this article.

such as proxy statement disclosure, the necessity for audited financial statements in certain cases, and the adequacy of internal controls of an acquired company under the Sarbanes-Oxley Act. These issues require top-notch accounting advice.

While a good M&A lawyer will always have a working knowledge of the accounting rules, it is usually folly to try to “play accountant,” and your role should be properly deferential to the accountants. Occasionally, however, you will encounter an accountant for a private company (usually with a long history of providing services to the client) who is out of his depth. This presents a very delicate problem of persuading the client to get sophisticated assistance for the accountant without appearing to advocate disloyalty. The one thing you should never do in this situation is to assume the role of giving your client accounting advice; you will almost always make a mistake if you try.

I always try to copy my client’s accountants on the various drafts of the acquisition agreement and exhibits. Although I find that the accountants rarely respond, my intentions here (I confess) are defensive in nature. If there is a dispute over an accounting concept or accounting terminology, I do not want to be accused of a blunder because I exceeded the limits of my expertise.<sup>23</sup>

### **C. Government Agencies**

You will frequently have to deal with government officials in securing permits, approvals and certificates necessary to close the deal. The best advice I ever got on dealing with government agencies occurred in my first year practicing law. This is my “Mickey the Dunce” story.

I was assigned the simple task of obtaining an uncontested “voluntary conservatorship” from the Probate Court for an aged and infirm aunt of an important client, who was mentally competent but physically unable to attend to her business affairs. I dutifully researched the law and prepared the papers for filing with the court.

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<sup>23</sup> This may be a case of “the generals always fighting the last war.” Early in my career, I made the mistake of using the term “net earnings” as a measure of a bonus in an employment agreement. This phrase was arguably not a generally accepted accounting term (“net income” being the preferred terminology). When a dispute arose over the meaning of these words, I discovered to my chagrin that my client’s accountants (whom I had not previously consulted) washed their hands of my transgression and were of no help in resolving the dispute.

When I went to the court to file them, I was referred to an Assistant Registrar, who told me I needed a physician's certificate attesting to her mental competence. Preposterous, I replied, noting with irrefutable logic that if the woman was competent, she was entitled to a voluntary conservatorship; and if she was not, then she was entitled to an involuntary one. The Assistant Registrar refused to allow me to file the petition without the certificate and told me to come back with one before he would even consider scheduling a hearing.

I returned to the office in a foul mood and promptly related my experience with the uncooperative clerk to my senior partner in highly critical terms. My senior partner said:

“Look, the people who work as clerks in the court system get job satisfaction in two ways: Either they find some guy who thinks he's a know-it all, and run him in circles to prove their superior knowledge; or they find somebody who needs help, and demonstrate their superior knowledge by guiding him through the maze of regulations. Go back tomorrow and say ‘Hi, I'm Mickey the Dunce. I don't know anything, but I need help.’ See how that works.”

The next day I went to a different Assistant Registrar and took the recommended approach. I think I even mispronounced the word “conservatorship.” To my amazement, the clerk told me that she would accept my filing, would schedule a prompt hearing and allow me to file a physician's certificate before the hearing. She also promised that she would assign my case at the very top of the list on the hearing date.

My senior partner's advice has proven over the years to be invaluable and nearly infallible. You will be astonished how cooperative government officials can be if you flatter rather than antagonize them. Mickey the Dunce can accomplish things far more effectively than the know-it-all.

A corollary to the Mickey the Dunce Rule is that it is always easier to “dictate the terms of your surrender” to a government agency than it is to prevail in combat.<sup>24</sup>

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<sup>24</sup> Another corollary, which may surprise you, is that it is sometimes more effective to send a paralegal on a mission to an agency than a lawyer. A good paralegal with a working relationship with the agency is perceived as a person in need of help, rather than a know-it-all, and can be an invaluable resource.

## **VII. TRICKS OF THE TRADE**

The following list of tips for successful negotiation of business acquisitions is borrowed in large part from Hunt, *Structuring Mergers and Acquisitions*, (Wolters Kluwer, 3d ed. 2007), §25.03, and is excerpted here with permission. These points are tactical, rather than strategic, but are good common sense reminders of the decisions that must be made during negotiations.

### **A. Do's**

#### **1. *Compromise***

The power of compromise is one of the most important lessons a negotiator can learn. Fundamentally, negotiation is all about compromise. Compromise comes in many forms. You can back away from an issue in order to move the process forward. You can trade an issue that is important to you for one that is important to the other side. Knowing your bottom line on an issue allows you to compromise in order to get the deal done, but not give away the entire deal.

#### **2. *Keep Notes***

Throughout the deal process, including the negotiations, keep a running list of the significant issues that rise. Make sure that you track issues that are of importance to you, and those that are important to the other side as well. In addition, keep a record of your conversations. You will learn that a lot of information is passed between the parties during negotiations, and it is easy to forget who's responsible for tracking down information or what the resolution of a certain issue was.

#### **3. *Keep Your Important Cards Close to Your Chest***

Focus on the issues that need to be addressed. Try not to add additional commentary on the deal, the people or tangential topics. If your counterparty is doing his job well, he is listening to everything you say, and could glean valuable information from you that could be used against you later. On the other hand, you should always subtly remind your opponent of the factors that enhance your bargaining leverage, such as the existence of other interested buyers or your client's alternatives if it does not do the deal.

#### **4. *Be Consistent***

Be firm on those things that are important. Try not to go to battle on minor issues. Set the expectation with the other side that you are objective, fair and reasonable. Back up your statements with evidence or strong rationale.

You should also be able to judge the overall temperament of the negotiations in order to know when to stick a stake in the ground on a certain issue.

**5. *Don't Give Away the Less Important Stuff Too Early***

If you come to terms too soon on all the simple points, you may not have something to trade later on. You should have a good enough understanding of all the issues in the deal that you learn which are important to the other side. While these points may not be important to your client, you are able to maintain a certain amount of leverage by not conceding these issues to the other side too soon. It is often good strategy to listen to *all* of your opponent's proposed changes before deciding which ones you will concede.

**6. *It's OK to be a Jerk Every Once in a While***

Depending on the circumstances, it may be appropriate to get emotional during a negotiation. Reasons to make a bold statement would include if the other side is not hearing your concerns loud and clear, if they are veering off course, if their own behavior becomes intolerable, or if you need to ensure that an issue of importance turns in your favor. This tactic is most effective if it contrasts with your usual cooperative demeanor.

**7. *Stop to Take the Temperature***

In every step of the negotiation, it is important to revisit the original objectives and expectations of the deal, and make sure that the direction of the discussions is consistent with those intentions. From a business perspective, you should be concerned that the evolving contract supports the valuation and financial analysis performed in the deal.

**8. *Track Progress***

At the end of each negotiation session, agree on the open items with the other side, what is required to resolve them, and what the next steps should be. Every step of the way you should be pushing the ball closer to the finish line.

**9. *Ask Questions***

If you do not understand something, ask questions. One party may say something that is interpreted entirely different by the other side than was originally intended. If you think an issue is difficult to understand, it is all right to spell it out and ask the other side if they understand what you are saying. Misunderstandings do not move a deal forward.

## **10.     *Educate Your Opponent***

A well-informed counterparty is more likely to see things your way. Spend time investing in your counterparty by providing him with information that educates him and is supportive of your position. Let him know why certain items are of importance to you; likewise, don't force issues that are not as important.

## **11.     *Decide on the Tough Issues***

Many times, the difficult issues are not just price and structure. In fact, those points are often the easiest to tackle, since without agreement in these fundamental areas, there would be no basis for a deal. The tough issues are often those that don't appear until after the negotiation is already underway. It behooves you to try and preempt the process by ferreting out the difficult issues as soon as possible. You should then decide when you want those issues to be addressed. For example, there may be a lawsuit or regulatory issue that is pending, the premature resolution of which may scare away the other side. However, if left to the end of the negotiation, the counterparty may not perceive the issue to be quite as severe if they have made substantial progress on most other aspects of the deal.

### **B.     Don'ts**

#### **1.     *Don't Get Hung up on Issues***

No transaction ever gets done unless both parties want to move the process forward. This means that neither side has the luxury of getting hung up on issues. If a particular point looks like it is not going to get resolved on a given day, agree to put it aside and revisit it later. You will be amazed at how quickly the list of unresolved issues dwindles.

#### **2.     *Don't Keep Raising New Issues***

You should get all the issues out on the table as quickly as possible in a negotiation, partly to understand the overall magnitude of the process, but also to prevent both sides from introducing new issues during the deal. New issues that are left too late in the process can negatively affect the entire process and damage your credibility, since these points may alter a party's viewpoint on issues already negotiated. *See* Section VII(C)(6) *infra*.

#### **3.     *Be Careful when Trying to Bluff***

People sometimes liken deal negotiation to a game of poker. This is a risky strategy, since in a transaction the whole deal is at stake rather than a

single hand. While bluffing comes in different shades of gray and certainly can have its place in a negotiation, it is not for the faint of heart.

### **C. Tactics to Look Out For**

#### **1. *Deceit***

In most cases, peoples' natural tendency is to give the other side the benefit of the doubt and to assume that they are acting in a forthright manner. While I'm not suggesting that you treat every counterparty as a criminal, you should be astute in your interactions with the other side and observe their approach to negotiations. Did he deliver on his promise? Has he provided the information you asked for? Does the term sheet or contract accurately reflect what you discussed and agreed to?

#### **2. *Calling on a Higher Authority***

A common strategy is for a lead negotiator to have the responsibility to negotiate certain issues but not others. "I'll have to check with my client on that issue" is a good way to buy time to think or to deflect responsibility for taking a hard line. While this strategy can work, the principal dealmaker runs the risk of undermining his credibility with the other side, because they become unsure over what issues the dealmaker has authority. They may become reluctant to resolve an outstanding point for fear that a "resolved" or "closed" issued may get reopened.

#### **3. *Good Guy/Bad Guy***

Much like the higher authority approach, a bad guy may play tough on issues in order to make as much progress as quickly as possible. To the extent the bad guy goes too far or fails in his efforts, the good guy then steps in and backtracks if necessary. However, if the bad guy's approach is successful, the good guy simply steps in to continue the deal. This high-risk approach can work under certain circumstances, but can damage credibility if used as an overriding strategy.

#### **4. *Intimidation***

Another tactic to be wary of is intimidation, where the negotiator tries to bully the other side into conceding on an issue. Intimidation may suggest a lack of leverage or a masking of issues that are not desired to be revealed. Common signs of intimidation are when a negotiator introduces personal attacks or tries to pull seniority over the negotiator for the other side.



## **5. *Beware of the Trial Balloon***

Often, a party may float an idea or propose a solution to a problem. While in many circumstances, this is a legitimate means to exploring the other side's flexibility on an issue, you should be careful about giving too much away in responding to a proposal positioned as a "trial balloon."

## **6. *Avoid Uncompensated Concessions***

Some negotiators employ the "slice the baloney" technique of asking for just one more little concession to seal the deal, and then repeating the process until the "slices" add up to most of the baloney. The surest way to thwart this tactic is to insist that every concession you make is offset by a concession on the part of the other party.

All of these tactics may have their rightful use, place and time in a negotiation, and can be effective if not abused. However, misuse of any of these tactics is high risk and is certain to reveal weakness or damage credibility. So, just as you should be wary of using these approaches, you should be aware when others are using them on you.

## **VIII. SUMMARY**

The following is my attempt to distill the most important points to bear in mind in any business acquisition negotiation.

### **A. The Importance of Client Communication**

Let's start with the obvious: as an M&A lawyer, you are engaged by your client to accomplish an important business objective. Your efforts should all be directed to achieving that ultimate goal by providing the client with an evaluation of the legal risks of each course of action and allowing him to make the business decision.

But first you must clearly identify the objective. This requires you to think like a businessman. You must discuss the proposed transaction with your client at a very early stage and learn his business goals. You should prioritize these business goals, which are usually (1) do the deal; (2) at the best price; and (3) upon advantageous legal and business terms. You and your client shall agree upon and prioritize the most important nonprice terms of the deal. You should also take this opportunity to learn your client's motivational facts – his needs, values, fears, hopes, resources, ambitions and interests relating to the deal.

You should explain to your client, as necessary, the nature of the business acquisition process and the various legal and business issues that arise

during its course.<sup>25</sup> At this point you should be able to come to a conclusion as to which issues are more important than others, and to guide your negotiation and drafting accordingly.

It is equally important to engage your client in the negotiation process. To be sure, clients often abandon interest in the negotiations after agreeing upon the price and other central deal points, delegating to lawyers the deadly boring minutia of the technical terms of a 50-page acquisition agreement (not to mention the disclosure schedules) which are usually of no interest to them. But there are important business issues that arise in the course of the negotiating the legal terms of the deal which your client, not you, should make. You should constantly make sure that you and your client are “on the same page” during the course of negotiations.

## **B. Be Cooperative**

Avoid confrontational negotiation. The best approach is to set the tone of two parties *cooperating* in the mutual objective of finding business and legal terms that they can both live with. Ask for and share information, but be careful about revealing weaknesses.<sup>26</sup> Marshall arguments for and against specific provisions and explore compromises and alternatives when impasses occur. Volunteer to draft the agreement and do not hesitate to redraft in your language various provisions which you find unacceptable.

## **C. Employ Leverage**

Leverage is present in almost every business deal. Be aware of the factors (discussed in Section II(C), *supra*) which give your client a bargaining advantage or disadvantage. Be subtle about deploying leverage; it is always better to allow the other party to “save face” by making some innocuous compromise rather than giving an ultimatum.

Be aware that leverage depends on the *perception* of the parties. Be aware of your client’s bottom line and identify the client’s BATNA (Best Alternative to Negotiated Agreement) and take steps where possible to improve your client’s BATNA.

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<sup>25</sup> See Griffin, *The Acquisition Mating Dance*, elsewhere in this handbook, for an introduction to the business acquisition process.

<sup>26</sup> Always be aware of the restrictions imposed by Rule 4.1 of the Massachusetts Rules of Professional Conduct. See footnote 19 *supra*.

#### **D. Gather and Protect Information**

Business acquisition negotiations provide many opportunities to gain information regarding the strengths and weaknesses of your opponent's bargaining position. Don't try to negotiate a deal by email. Meet in person with your opposing counsel, or at least engage him or her in conversation regarding the background of the transaction. Use this opportunity to ask questions to elicit information on your opponent's motivations. Don't be afraid to be evasive when your opponent asks for sensitive information.

#### **E. The Essential Attributes of a Good Negotiator**

*Credibility* is the one essential attribute of a good negotiator. If your opponents feel that you are trustworthy and reasonable, they will usually respond in kind. If not, you are unlikely to achieve much success.

Remember that persistence trumps talent; be relentless in advocating your client's interests, but have the perspective to know what is really important to your client and not to waste your time on trivia. Be aware that there are "magic moments" in a deal – at the letter of intent stage and at or near the closing – when concessions are most likely to be made. Use time pressure to your advantage when possible.

#### **F. Drafting**

Seize the opportunity to draft the acquisition agreement whenever possible; it gives you a terrific advantage in the subsequent negotiations. When you can't do the first draft, make sure to submit drafts of proposed modifications *in your words*, rather than allowing your opponent the opportunity to draft them. Beware of using a previously negotiated deal as your model and always tailor the draft to the particular facts and context of the seller's business. Don't skew the first draft of the agreement to excessively favor your client, at least when you have an experienced M&A attorney on the other side.

#### **G. Dealing with Third Parties**

Be mindful of the limitations and resources of investment bankers and accountants, and tactfully resist their efforts to "play lawyer." Take advantage of the "Mickey the Dunce" strategy in dealing with government agencies.

#### **IX. A FINAL NOTE**

Be flexible. Every negotiation is a unique event and every negotiator is a unique individual. Tactics that work in one context may not work in another.

Most of all, be yourself. Remember Freund's admonition that "[E]veryone has his own negotiating style, and the worst thing you can do is adopt a negotiating technique that does not feel comfortable, simply because a man in a book says that he uses it to advantage."<sup>27</sup>

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<sup>27</sup> Freund, *Anatomy of a Merger*, p. 10.