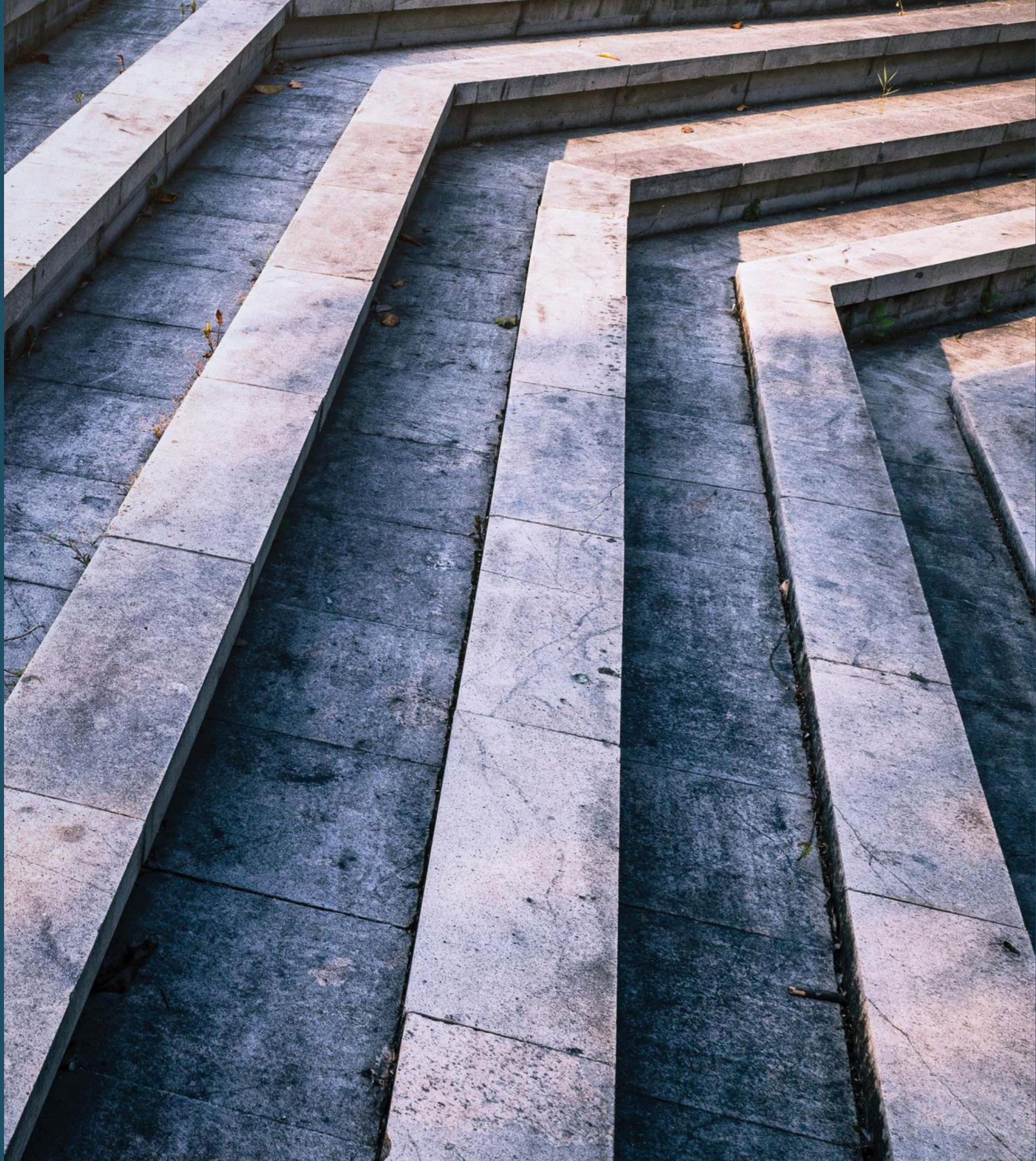
Vinson&Elkins

Navigating

Debt Financing in an Acquisition

October 7, 2021



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Overview

- **Part I**: Acquisition Financing - the Basics
  - What is “Acquisition Financing”?
  - What are “Commitment Papers”?
  - What is “Conditionality”?
  - What is an “Auction Process”?
  - What are “Debt Financing Provisions”?

- **Part II**: A Deeper Dive
  - Structuring
  - Bridge to Bond & Securities Demand
  - Credit Support

Part I: Acquisition Financing – the Basics

What is “Acquisition Financing”?

Typical Stages of an Acquisition Financing

Financing Process Commences — e.g., 3 weeks — **Bid Date** — e.g., 1 week — **Signing Date** — 1-6 months, longer in limited circumstances — **Closing**

Financing Process Commences:

- Banks approached; provided model and/or Quality of Earnings Report
- Structure socialized
- Terms socialized, often with several rounds of grids

Bid Date:

Single-headed commitment letters signed by banks and submitted along with a bid draft / comments on acquisition agreement:

- SunGard conditionally, no "diligence out"
- Agreed financing structure and amounts
- Sign-off on bid version of the acquisition agreement
- Expiration date matching acquisition agreement outside date (in some cases, plus a cushion)
- May be more than one bid date

Signing Date:

Multiheaded commitment letters signed by banks and sponsor, acquisition agreement executed:

- Bank commitments allocated
- Bank economics allocated
- All open points resolved
- Sign-off on final acquisition agreement

Closing:

Credit agreement, bond indenture and related documents signed, funds advanced and acquisition consummated

Note: Graphic adapted from *Leveraged Financing 2019: Financing an Acquisition – Current Trends* presented on Practical Law Institute

What are “Commitment Papers”?

Commitment Papers

Bank Deal

- Commitment Letter:
  - Letter
  - Transaction Description
  - Term Sheet
  - Funding Conditions
- Fee Letter:
  - Fees
  - "Market Flex"

Bridge to Bond

- Commitment Letter:
  - \+ Bridge Term Sheet
- Fee Letter:
  - \+ Securities Demand
- Engagement Letter
- Fee Credit Letter

Other "Letters" & Agreements

- Highly Confident Letter
- Interim Facilities Agreement
- Syndications Strategies Letter

What is “Conditionality”?

Conditionality

- Consummation of Acquisition
- Minimum Equity Contribution
- No "Material Adverse Effect"
- Financial Statements
- Offering Memorandum
- Marketing Period / Inside Date
- Limited "Sungard" Conditionality
- Solvency

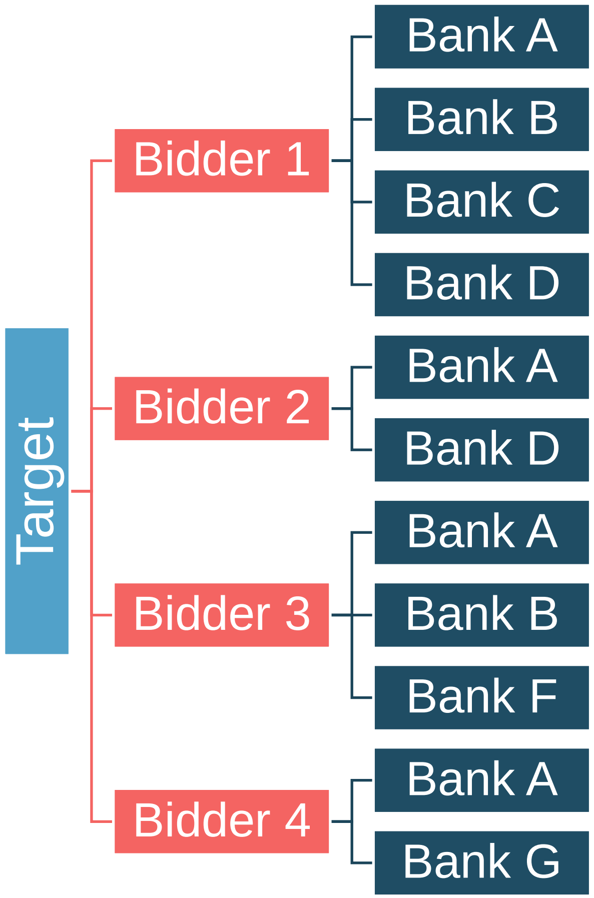
What is an “Auction Process”?

… and what are “trees”?

Auctions and Trees

Seller(s) – selling shareholders
Target – company up for sale

Bidders – potential buyers (could be 'strategics'/'trade' (aka corporates) or private equity bidders)
Banks – prospective finance providers to the bidders



- The "**Sell Side**" team generally includes
  - the seller(s)
  - the target
  - one or more banks acting as M&A advisors to the sellers (note these banks often are some of the same banks competing to provide financing to the bidders)
  - often a financial advisor (e.g. Rothschild)
- Often the banks acting as M&A advisors will offer a 'staple' financing
  - terms are sent out with M&A process materials
  - guide valuation and provide confidence that leverage is available
- Here, Bank A is a potential financing source for all bidders – they are providing/offering the 'staple' financing
- Banks B and D are working with multiple bidders (Bank B with bidders 1 and 3; Bank D with bidders 1 and 2)
  - Different individuals within the bank would be working for different bidders, similar to the way law firms tree themselves up
- Each of banks C, E, F and G are exclusive to their bidder
  - may be required by the bidder for confidentiality reasons

What are “Debt Financing Provisions”?

Debt Financing Provisions

- In a leveraged buy-out or a transaction without a funding condition, the debt financing provisions serve to allocate risk of a financing failure as between Buyer and Seller.

- "Xerox provisions" emerged in the wake of the 2008 financial crisis and serve to limit liability of the debt financing parties *vis-à-vis* Seller/Target.

Common Terms and Provisions

Part II: A Deeper Dive

Structuring

Choosing the Right Debt Solutions

Captial Provider

- Commercial banks
- Funds and other Institutional Investors (e.g., CLOs)
- Direct Lenders

Acquisition Consideration

- Term Loan A
- Term Loan B
- Bilateral Loan
- Direct Loan
- Bridge Loan
- Bond Issuance
- Mezzanine Debt
- Seller Financing

Working Capital Solutions

- Cash Flow Revolving Credit Facility
- Asset-Based Revolving Credit Facility
- Reserve-Based Revolving Credit Facility
- Recurring Revenue Revolving Credit Facility
- Factoring Arrangement
- Securitization

Assumed or Acquired Debt

- In certain circumstances, it may be preferable to leave a target's debt outstanding upon closing rather than paying it off or refinancing it.

- Feasibility Considerations:
  - Call protection
  - Pricing
  - Covenant package
  - Guarantee and collateral requirements
  - Existing debt of Acquiror

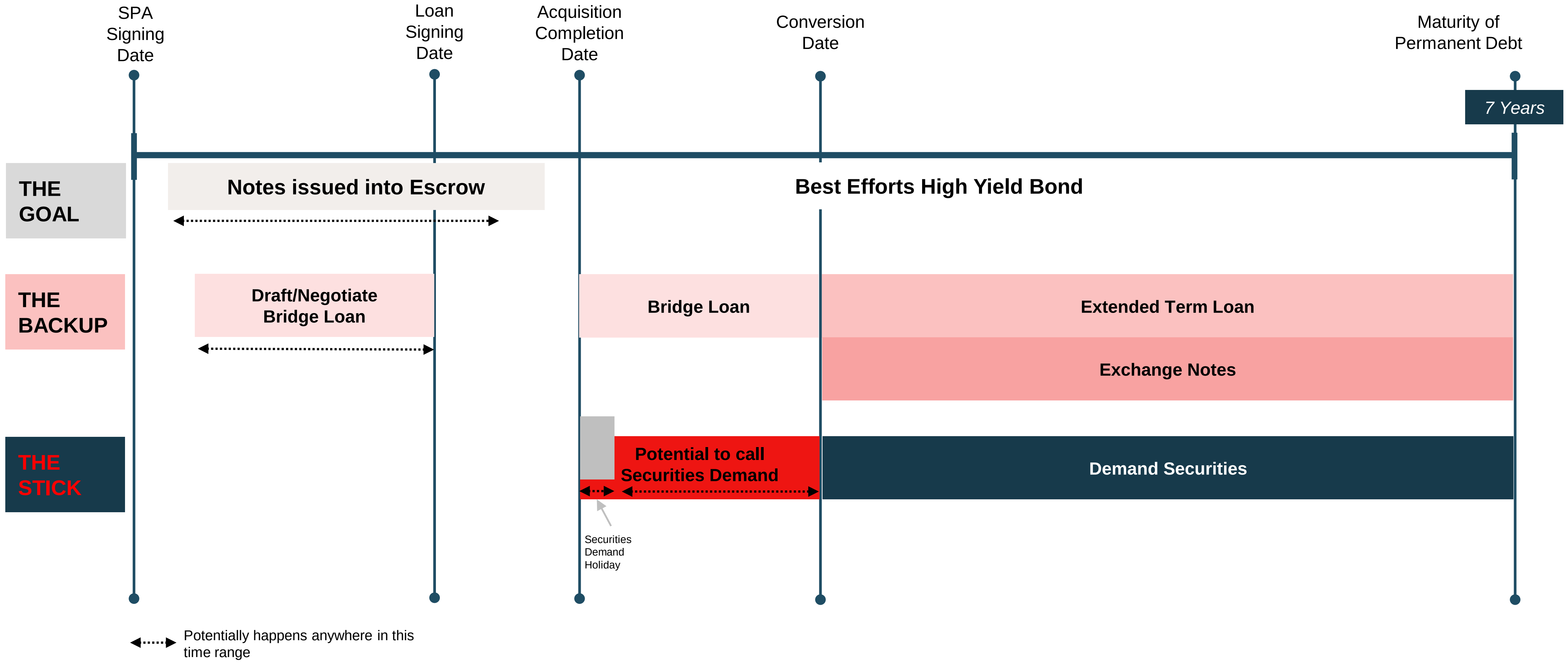
- Portability provisions mitigate the need for change of control consents from debt holders.

Portability conditions vary transaction to transaction, but may include one or more of the following:

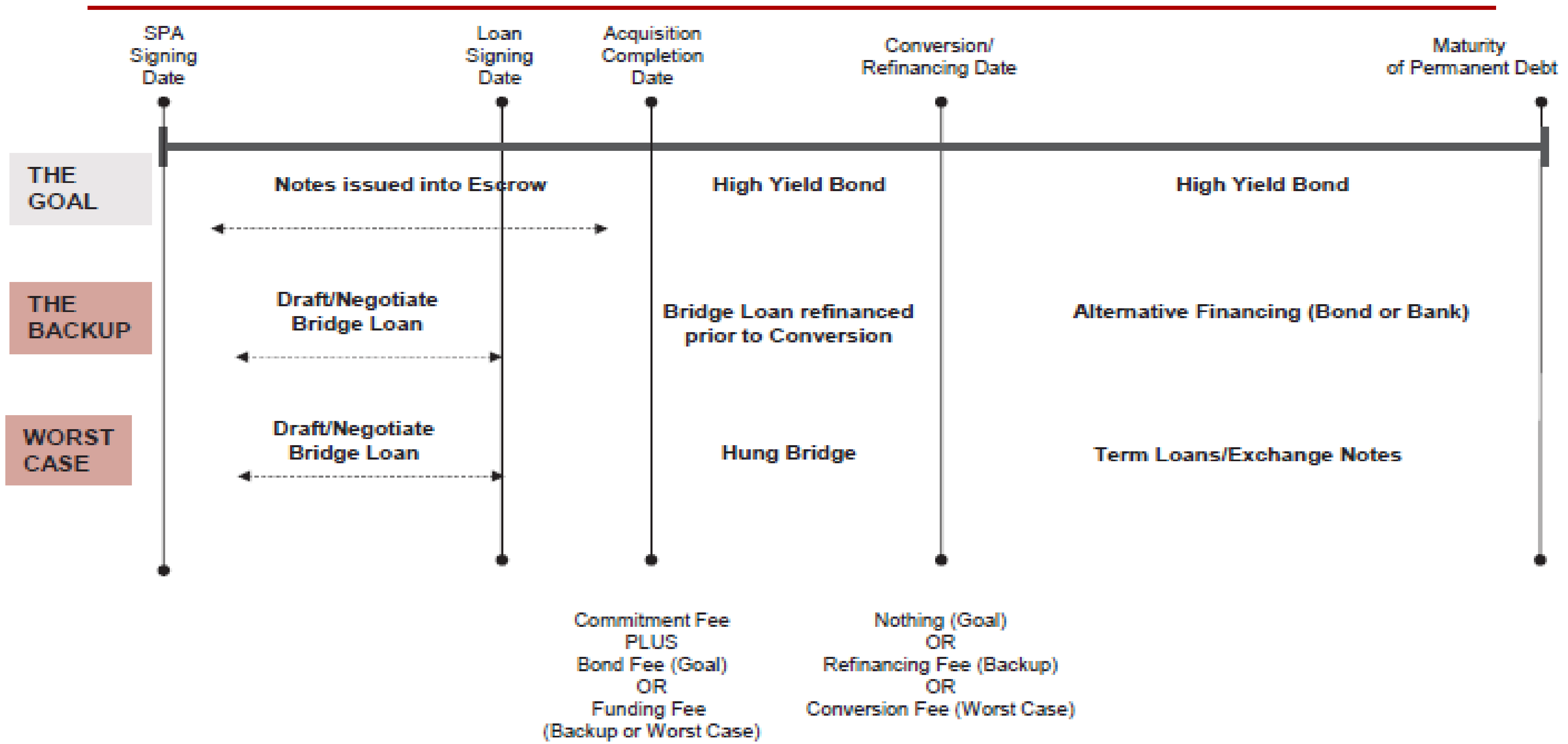
- Leverage Ratio
- Ratings
- Minimum Equity Contribution
- Minimum AUM
- KYC
- Timing

Bridge to Bond & Securities Demand

The Route to Permanent Financing



Understanding The Take-out Fee



Credit Support

U.S. v. UK/European Differences

- Guarantees
  - All domestic subsidiaries, subject to customary limited exceptions
  - Foreign subsidiary guarantees typically excluded
- Collateral
  - Substantially all assets
  - All jurisdictions, subject to exceptions
  - Equity pledge of borrower and subsidiaries, subject to exceptions

- Guarantees
  - Guarantor coverage test is typical (e.g. 80% of Group EBITDA)
  - Further limited to agreed jurisdictions and subject to further limitations
- Collateral
  - Material assets
  - Specified Jurisdictions
  - Equity pledge may be limited to specified material subsidiaries

THANK YOU

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*By appointment only