

## Chapter 17

### Anatomy of an Acquisition Agreement

**Brian Stuart Duba<sup>1</sup>**  
*Frost Brown Todd LLC*  
Lexington, Kentucky

#### Synopsis

§ 17.01.	<b>Introduction.....</b>	<b>576</b>
§ 17.02.	<b>Pre-signing Documents .....</b>	<b>578</b>
	[1] — Introduction.....	578
	[2] — Confidentiality Agreement.....	578
	[3] — Letter of Intent.....	580
	[4] — Due Diligence Checklist .....	581
§ 17.03.	<b>The Acquisition Agreement.....</b>	<b>582</b>
	[1] — Overview.....	582
§ 17.04.	<b>Definitions Section .....</b>	<b>583</b>
	[1] — Introduction .....	583
	[2] — Knowledge.....	584
	[3] — Permitted Encumbrances .....	586
	[4] — Mining Title.....	587
	[5] — Mine Plan .....	588
§ 17.05.	<b>Asset v. Stock Sales and Backdoor Liability</b>	
	<b>Assumption in Asset Sales .....</b>	<b>590</b>
	[1] — Introduction .....	590
	[2] — Fraudulent Conveyance.....	591
	[3] — Business Continuation Doctrine .....	591
	[4] — Stock Transaction Liabilities.....	593
	[5] — Note Regarding Consents.....	594
§ 17.06.	<b>Sale and Transfer of Assets; Closing.....</b>	<b>595</b>
	[1] — Introduction .....	595
	[2] — A Note on Having Two Buyers .....	595
	[3] — Assets.....	596
	[4] — Excluded Assets.....	597
	[a] — Benefit Plans.....	597
	[b] — Certain Contracts.....	598
	[c] — Permit Collateral .....	598

---

<sup>1</sup> The author wishes to thank Kirby Ifland, 2012 summer associate (Harvard Law School, Class of 2013), for his thoughtful comments and contributions to this chapter. The opinions expressed and any deficiencies of this chapter are, of course, solely the author's.

	[d] — Insurance.....	598
	[5] — Liabilities .....	599
	[a] — Assumed .....	599
	[b] — Retained .....	599
	[6] — Consideration.....	600
	[a] — Payment Terms .....	600
	[b] — Valuation .....	600
	[c] — Wire Transfers .....	601
	[d] — Non-cash Consideration.....	601
	[e] — Earnout .....	602
	[f] — Working Capital Adjustment .....	602
	[g] — Inventory Purchase Price Adjustment.....	603
	[h] — Holdback/Escrow.....	604
	[i] — A Note on Complicated Consideration Provisions.....	605
	[7] — Allocation of Purchase Price .....	605
	[8] — Closing and Closing Obligations.....	606
<b>§ 17.07.</b>	<b>Representations and Warranties .....</b>	<b>607</b>
	[1] — General Description.....	607
	[2] — Materiality Qualifiers and Knowledge Qualifiers .....	607
	[3] — Sellers' and Shareholders' Representations and Warranties.....	608
	[a] — Introduction .....	608
	[b] — Financial Statements.....	609
	[c] — Inventory.....	609
	[d] — Accounts Receivable.....	609
	[e] — Permits.....	609
	[f] — Real Property.....	610
	[g] — Reserves .....	616
	[h] — Mining Plan .....	616
	[i] — Affiliate Agreements .....	617
	[j] — Solvency.....	617
	[4] — Buyer.....	617
<b>§ 17.08.</b>	<b>Covenants.....</b>	<b>618</b>
	[1] — Introduction. ....	618
	[2] — Pre-Closing and Closing .....	610
	[a] — Access and Investigation .....	619
	[b] — Operation of Business.....	619
	[c] — Delivery of Interim Financials.....	619
	[d] — Approvals and Consents .....	620
	[e] — No Shop.....	621
	[f] — Payment of Liabilities.....	621

	[g] — Estoppels, Ratifications, and Amendments.....	622
	[h] — Recordation.....	622
	[i] — Evidence of Title.....	623
	[j] — Employees.....	623
	[k] — Tax Compliance Certificates.....	623
	[l] — Closing Deliverables.....	624
	[m] — Utilities.....	624
	[3] — Post-Closing.....	624
	[a] — Payment of Retained Liabilities; No Distribution.....	624
	[b] — Noncompetition, Nonsolicitation and Nondisparagement.....	625
	[c] — Mining Permit Matters.....	626
	[d] — Transition Services.....	629
	[e] — Transfer and Property Taxes.....	630
	[f] — Further Assurances.....	630
<b>§ 17.09.</b>	<b>Conditions Precedent .....</b>	<b>631</b>
	[1] — General Description.....	631
	[2] — Deliverables Closing Conditions.....	631
	[a] — Real Property Comfort.....	632
	[b] — Financing.....	642
	[c] — Diligence.....	632
	[d] — Adverse Facts Closing Conditions.....	633
	[e] — Breach of Warranty Closing Condition.....	633
	[f] — Supplements to Disclosure Schedules.....	634
	[g] — Material Adverse Effect.....	634
	[3] — Seller’s Conditions.....	635
<b>§ 17.10.</b>	<b>Termination .....</b>	<b>635</b>
	[1] — Failure of Conditions Precedent.....	635
	[2] — Breach of the Agreement.....	635
	[3] — Drop Dead Date.....	636
	[4] — Effect of Termination.....	636
<b>§ 17.11.</b>	<b>Indemnification .....</b>	<b>636</b>
	[1] — General Notes.....	636
	[a] — Why So Important?.....	637
	[b] — Public Company Stock Sale.....	638
	[c] — Standard Indemnity Section Outline.....	638
	[d] — Why Warrant?.....	638
	[e] — Shareholders Liable.....	639
	[f] — Note on Importance of Insurance.....	639
	[g] — Survival Periods.....	640
	[2] — Anti-sandbagging v. Pro-sandbagging.....	640

	[3] — Indemnification by Seller and Shareholders.....	641
	[4] — Deductible or Baskets.....	642
	[5] — Escrow and Related Concepts.....	643
	[6] — Separate Title or Reclamation Indemnity.....	644
	[7] — Sole Remedy and Carveout for Fraud.....	644
	[8] — Third-Party Claims .....	646
	[9] — Treatment of Direct Claims.....	646
<b>§ 17.12.</b>	<b>General Provisions.....</b>	<b>645</b>
<b>§ 17.13.</b>	<b>Determining Market Provisions .....</b>	<b>646</b>
	[1] — Introduction.....	646
	[2] — ABA Deal Points Studies .....	646
	[3] — J.P. Morgan M&A Holdback Escrow Report.....	646
	[a] — Electronic Data Gathering, Analysis and Retrieval (EDGAR). .....	647
<b>§ 17.14.</b>	<b>Conclusion.....</b>	<b>647</b>

**§ 17.01. Introduction.**

The acquisition of an active business operation is a challenging transaction for lawyers, business persons and accountants. Whether the acquirer purchases the “business” by purchasing all of the assets of the target company (an “asset” transaction), or by purchasing all of the ownership interests held by owners of the target (a “stock” transaction), there are a myriad of operational, legal and practical matters that should be addressed in order to consummate a transaction with minimal interruption to operations and minimal adverse consequences.<sup>2</sup> Despite the extreme complexity involved in evaluating (a) the value of a target, (b) the assets of the target, (c) the procedures for closing the transaction without adverse consequences and (d) the legal risks applicable to the target (and equally important, allocation of liability for such risks) the ability to consummate acquisition transactions is critical to an efficient capitalist market because it enables the allocation of resources to the most efficient users thereof in an efficient, lump sum transaction. Therefore, mergers and acquisitions lawyers play a vital role in greasing the gears of the free market by helping business folks consummate whole-company acquisitions.

---

<sup>2</sup> Of course, mergers are also a form of acquisition, but the issues are essentially the same as with a stock acquisition.

Unlike leases, coal sales agreements, and contract mining agreements, to name a few examples, acquisition agreements are not documents that most clients become familiar with through their daily business activities. For many clients, an acquisition or disposition of a company will occur very rarely throughout their career, making the job of counsel all the more important when it comes to advice regarding what is reasonable from a business perspective, not just a legal perspective.

Further, an acquisition agreement cannot be pulled off the shelf without a great deal of risk that the provisions will not provide the language and protection necessary for the deal and assets at hand. There is simply no generic agreement that works.

To exhaustively cover all of the legal issues that need to be considered when acquiring a coal business, one would need to draft a chapter that touches on every legal issue covered by every white paper submitted to the Energy and Mineral Law Foundation since its inception, and then some, because all of those issues may come up and be of concern to a purchaser, especially in a stock transaction. This chapter does not do that, but what it does is describe the master agreement that governs the acquisition: the Asset Purchase Agreement, Stock Purchase Agreement or Merger Agreement, as applicable. A customary acquisition agreement is long and complicated, but as with a coal lease or a coal purchase agreement, or any other commonly utilized form of agreement, the standard terms all serve an essential purpose. It is also essential for buyer's and seller's counsel to master every provision in the agreement in order to adequately represent their clients in an acquisition transaction. As the chapter discusses various provisions of an acquisition agreement, it briefly touches on substantive issues of the law as it relates to a coal acquisition, including tax, real estate, environmental issues, the contract law of consents, and human resources matters.

This chapter discusses the acquisition agreement from the purchaser's perspective, focusing on key provisions specific to our industry and completely ignoring certain provisions that are applicable to all transactions and that were deemed less important or interesting than the items covered in detail. Covering the acquisition agreement mostly from the purchaser's perspective is reasonable because the initial draft of an acquisition agreement is generally

prepared by the purchaser and the purchaser is, generally speaking, the party most interested in having a complex, comprehensive agreement. After all, when a company is selling all of its assets or shareholders are selling all of their stock, their only real concern — absent release of personal liability in the event of reclamation liability, personal guarantees or other liabilities that pierce the veil of limited liability — is receiving the consideration they are owed, which is cash in the vast majority of transactions. Throughout this chapter, drafting recommendations and examples are provided.

After a very brief discussion of the pre-signing activities related to an acquisition, this chapter discusses a selection of the most important provisions in an acquisition agreement for an active mining company and the overall layout and goals of an acquisition agreement. Finally, this chapter discusses tools that can be used to argue over what “market” terms are for various provisions in the agreement.

## **§ 17.02. Pre-signing Documents.**

### **[1] — Introduction.**

Because of the importance of the standard documents that precede the execution of an acquisition agreement, the following briefly describes the Confidentiality Agreement, Letter of Intent and Due Diligence Checklist, which are executed or provided (in the case of the checklist) in the order listed. A full chapter could be devoted to each of the following, but for current purposes a few important points regarding each are worth discussing.

### **[2] — Confidentiality Agreement.**

Confidential information is essential to the success of mining companies. The location of a target’s owned or leased property, the royalties they pay to their landlords, and the prices they are paid for their coal (and by whom) are three of the most obvious types of information that are very valuable to a target and become less valuable once disclosed to competitors. As such, before any action is taken to discuss terms of a deal, and especially before a target discloses information that the purchaser will need to value the going concern, a confidentiality agreement will be proffered by the target. Such an agreement, as its name suggests, creates a contractual obligation to keep