

M&A Deal Points

FEBRUARY 2020





M&A Deal Points Study: Non-Competition Provisions

This report summarizes our findings on non-competition provisions in recent private target M&A transactions. Specifically, we reviewed (1) the prevalence of non-competition provisions in private target M&A agreements publicly filed in 2018 and 2019; (2) the prevalence and type of non-competition provisions in asset deals versus equity deals; (3) the prevalence of non-competition provisions applicable to employees of the selling entity; and (4) the association between the type of selling entity (private equity versus venture capital) and the type of non-competition provision.

Kira's state-of-the-art machine learning technology automatically identifies and extracts information from contracts and comes with over 900 built-in provision models. Our team of lawyers trains Kira to automatically find provisions by giving it sample language of that provision culled from publicly filed agreements. Once Kira has sufficient examples of a provision, it can find that provision in new agreements imported into it.

Kira is not limited to publicly filed documents. With Kira, professionals can conduct their own deal point studies on the documents of their choosing—for example, a law firm's deal documents from its document management system—to find information of interest to them. The information gathered can be shared throughout the organization and used for drafting and negotiating future agreements or revising standard forms.

For a full list of the currently available private target M&A deal point-related provisions that Kira can identify out of the box, please see the end of this report.

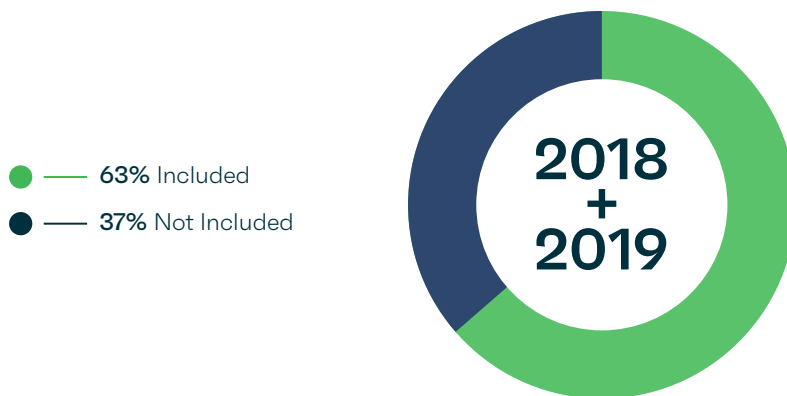


Analysis of 2018 and 2019 Private Target M&A Deals

Our data set consisted of 115 M&A agreements filed on EDGAR between January 1 and December 31, 2018 and 115 M&A agreements filed on EDGAR between January 1 and December 31, 2019, using the following parameters: deal values between \$30M and \$500M, involving private targets being acquired by public companies. Transactions in which the target was in bankruptcy, reverse mergers and divisional sales were excluded. We imported these agreements into Kira and analyzed the results. Using Kira’s “Non-Compete” provision model, we used Kira to determine the prevalence of non-competition provisions. Kira was able to accurately¹ identify these provisions, even though there was considerable variation in how they were drafted. We used Kira’s workflow tools to categorize whether the non-competition provisions applied to (1) interest holders and/or the selling entity in asset deals; (2) interest holders of the target company or selling entities in equity deals; and (3) employees, regardless of deal structure. In addition, we determined whether the selling parties were backed by private equity sponsors or backed by venture capital firms and analyzed which parties were subject to the non-competition provisions.

Non-Competition Provisions

When we reviewed the results in our sample sets, we found that in the aggregate, 63% of the transaction agreements included non-competition language.²



Source Data: 115 M&A agreements filed on EDGAR in 2019 and 115 M&A agreements filed on EDGAR in 2018, analyzed by Kira.

¹ For example, the “Non-Compete” provision model achieved a 90% “recall” score, which means that out of 100 examples of that provision our staff highlighted to train Kira, it will find 90 of them. The provision model has also achieved a 88% “precision” score, meaning that out of the results that Kira finds, 88% of them are correct examples of non-competition language. In comparison, studies have shown that traditional word searches rarely achieve more than 70% recall or precision.

² For purposes of our analysis, six agreements indicating California governing law were excluded since California law is particularly restrictive with respect to non-competition provisions for individuals.

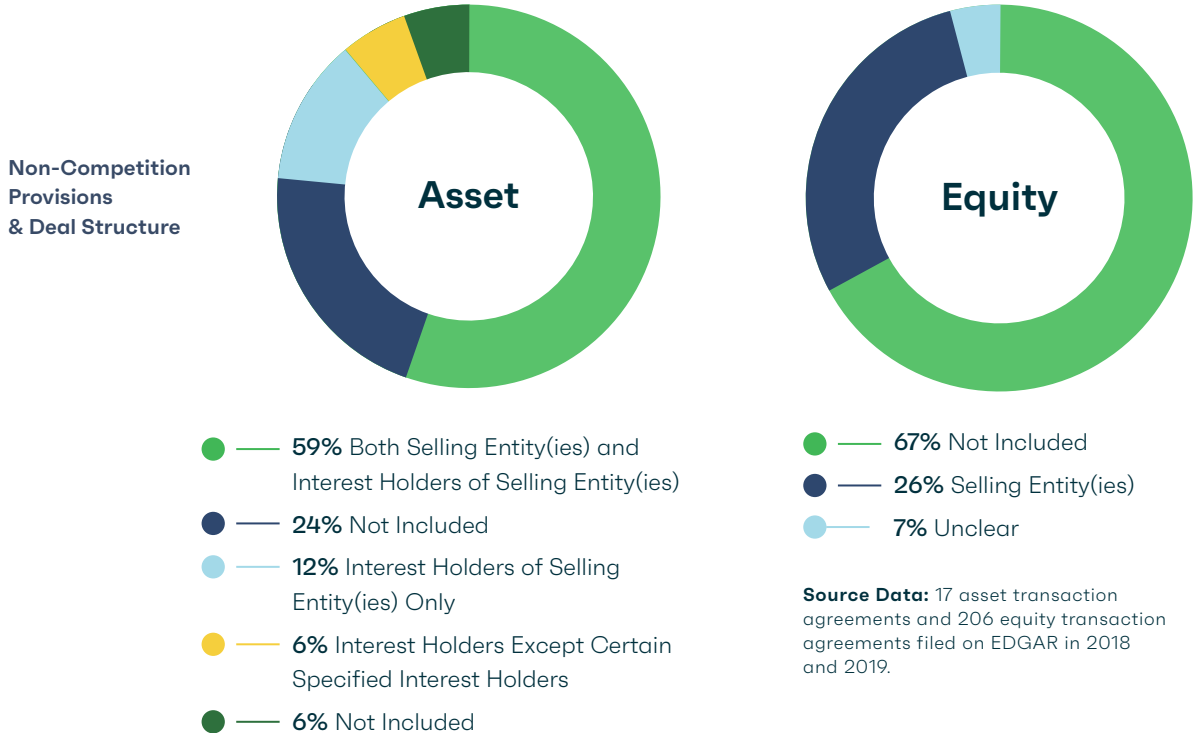


In addition to quickly assembling aggregate statistics, Kira automatically creates an easily searchable archive of the actual precedent language. A review of the results in our sample set confirmed that the non-competition provisions include significant variations in their application to different types of parties involved in the transactions.

Out of 17 asset deals:

- Ten agreements included non-competition provisions applicable to both the selling entity(ies) and its interest holder(s);
- Two agreements included non-competition provisions applicable only to the selling entity's interest holders;
- One agreement included a non-competition provision applicable to the selling entity interest holders except for certain specified interest holders;
- One agreement was unclear as to whom the non-competition provision would apply; and
- None of the agreements included non-competition provisions applicable only to the selling entity(ies).³

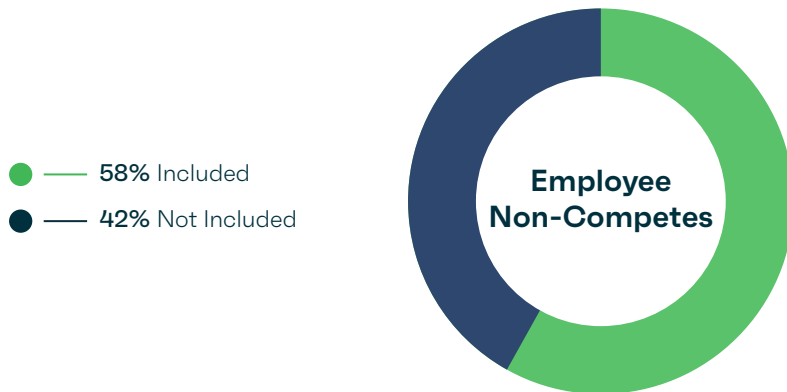
Out of 206 equity deals, 53 agreements included non-competition provisions applicable to the selling entity and/or target company shareholders, and 15 agreements were unclear as to whom the non-competition provisions would apply.



³ The percentages add up to more than 100% because some agreements included non-competition provisions that applied to more than one type of party, so were included in each relevant category.



Of the 141 agreements including non-competition provisions, regardless of deal structure, 82 agreements contained non-competition provisions applicable to the target company's management, directors and/or employees.



Source Data: 141 M&A agreements filed on EDGAR in 2018 and 2019 with non-competition provisions.

Relationship Between Non-Competition Provisions and Type of Selling Entity

We also used data from our sample set to determine the association between the prevalence of non-competition provisions and the type of selling entity. We included categories for private equity-backed and venture capital-backed sellers.

Of 65 agreements involving private equity sponsors as selling entities, 31 included non-competition provisions (48%). Of these, we found:

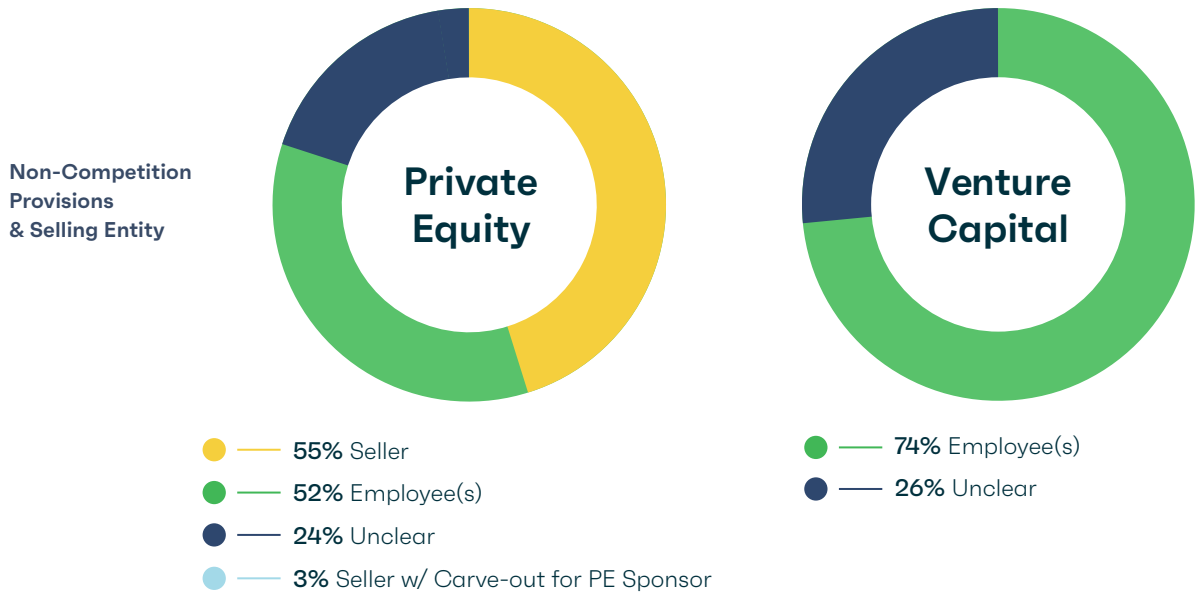
- 17 agreements included seller non-competition provisions;
- 16 agreements included employee non-competition provisions;
- One agreement included a seller non-competition provision that included a carveout for the private equity sponsors; and
- Four agreements were unclear as to whom the non-competition provision would apply.

Of the 41 agreements involving venture capital funds/firms as selling entities, 31 included non-competition provisions (76%). Of these, we found:

- 23 agreements included employee non-competition provisions; and
- Eight agreements were unclear as to whom the non-competition provision would apply.



This indicates that transactions that are venture capital exit deals are significantly more likely to include employee non-competition provisions than private equity exits.



Source Data: 65 M&A agreements filed on EDGAR in 2018 and 2019 involving private equity sponsors as direct or indirect selling entities, and 41 M&A agreements filed on EDGAR in 2018 and 2019 involving venture capital sellers. The percentages add up to more than 100% because some agreements included multiple non-competition provisions applicable to different parties.

Undoubtedly, the publicly available transaction agreements in our sample sets represent only a tiny fraction of all of the transaction agreements entered into each year that include non-competition provisions. Using Kira, you can create a similar analysis of your firm's own deals (and even study a specific industry or geography) with significantly greater speed, consistency and accuracy than a manual review. Kira allows you to unearth what's standard practice for the many private transactions which are never publicly disclosed, and to easily find real precedent clause language to apply to future transactions.

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M&A Deal Points for Public and Private Targets

Kira comes pre-trained to find provisions frequently negotiated during the course of an M&A transaction, which can assist in the tracking of market intelligence information.

The smart fields in this group are optimized for use on merger agreements, share purchase agreements and asset purchase agreements.

In addition to common fields such as; title, parties and date, the combined 172 fields in these groups include (but are not limited to) the following:

- No-Shop
- Size / Purchase Price
- “Material Adverse Effect” Definition
- Materiality Scrape
- Termination
- Working Capital Adjustment