



KDP

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Completion Mechanisms Completion Accounts vs Locked Box Accounts

Part 4

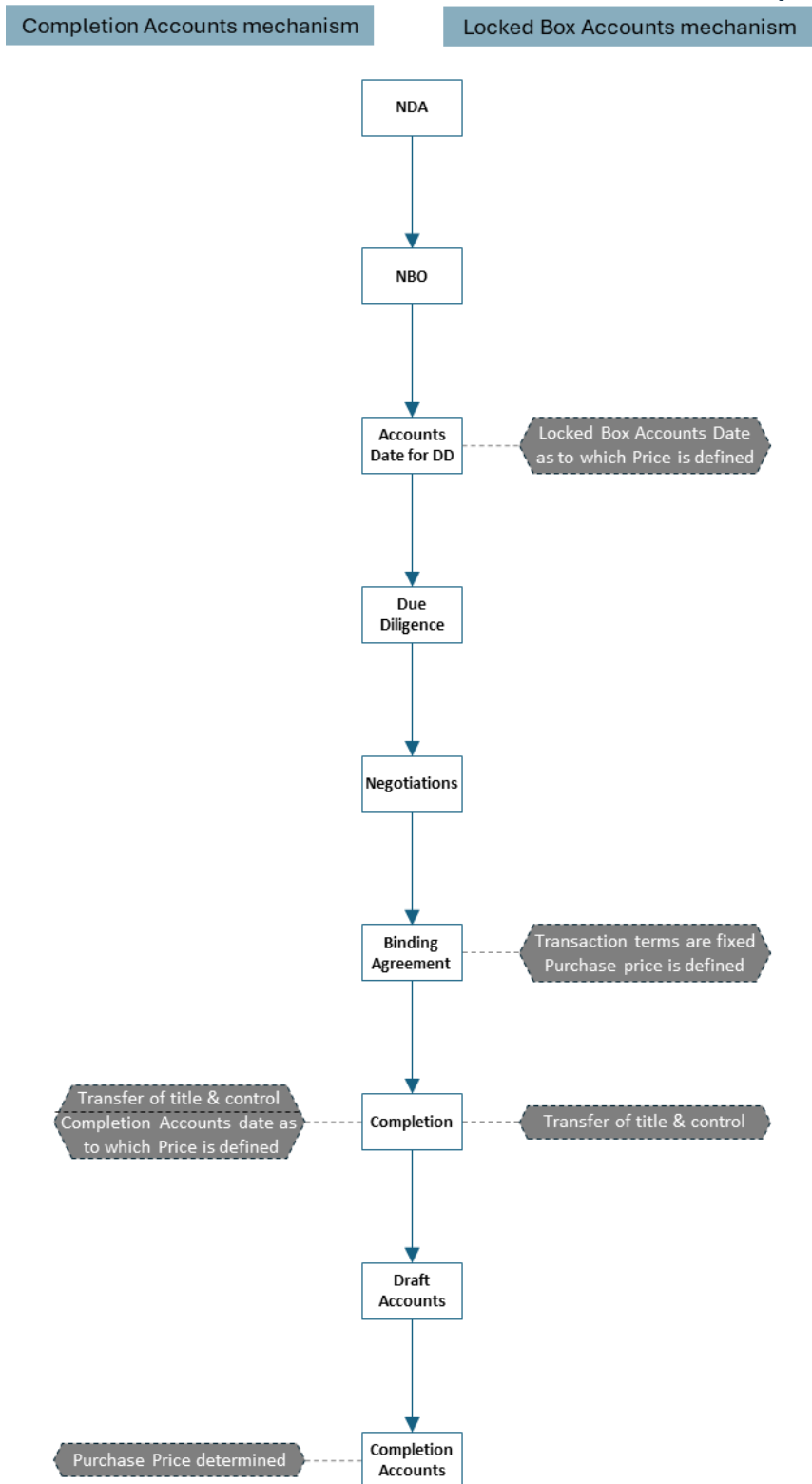
The Comparison

Part 1. The Comparison: Completion Accounts vs Locked Box Accounts

As a form of extended summary below we provide a comparison between the two completion mechanisms in their pure forms:

| | Completion Accounts | Locked Box |
|---|--|---|
| Finalizing Purchase Price | After Completion, upon agreement on the Completion Accounts | By Signing |
| Economic return passes on to the Buyer | as of Completion | virtually as of Locked Box Accounts Date |
| Purchase Price | Finalized under Completion Accounts | Finalized under Locked Box Accounts |
| Role of the due diligence | <ul style="list-style-type: none"> - Reconfirms or calibrates headline purchase price; - Provides valuable analysis about business, its debt and cash positions, working capital, etc.; - Provides reference point to compare with the Completion Accounts; - Indicates of the likely reclassification of items | <ul style="list-style-type: none"> - Locked Box Accounts used to finalize purchase price; - Allows getting better understanding of the related parties' transactions - Provides valuable analysis about business, its debt and cash positions, working capital level |
| Provisions in SPA specific for the mechanism | <ul style="list-style-type: none"> - Definitions for cash, debt, working capital, trade payables, trade liabilities, treatment of various items; - Rules for preparation and approval of Draft Completion Accounts; - rules to apply in case of dispute on the Draft Completion Accounts; | <ul style="list-style-type: none"> - Defining Leakage & Permitted Leakage; - Process and timeframe to check for Leverages; - "Strong" representations and warranties as to the correctness accuracy and completeness of the Locked Box Accounts; |
| Common benefits for the Parties | Captures all changes in the Equity Value that occur by Completion Date | <ul style="list-style-type: none"> - Purchase price is finalized latest on Signing the SPA - Comparatively shorter and simpler transaction process; |
| Specific benefits | <p>Buyer's benefit:</p> <ul style="list-style-type: none"> - Already in control of the target in case of a post-Completion dispute on finalization of price - True-up of the Completion Accounts is made while the Buyer has control over the Target | <p>Seller's benefit:</p> <ul style="list-style-type: none"> - Better control over the sales process; - Less aggressive treatment of the items in the accounts |
| Common risks for the Parties | <ul style="list-style-type: none"> - Risk of disputes on finalization of price after Completion Date - Transaction process is comparatively longer, more complex and requires engagement of resources for a longer period | Risk of imperfect purchaser price calculation or imperfect Value Accrual structure |
| Specific risks | <p>Seller's risk:</p> <p>Dispute on the Purchase Price, when the Target and its accounts are already under Buyer's control</p> | <p>Buyer's risk:</p> <ul style="list-style-type: none"> - Deterioration of Business after Locked Box Accounts Date; - Seller's lack of motivation to continue to maximize profit after Locked Box Accounts Date; - Leverages in case of insufficient knowledge about the related parties |
| Perceived friendlier to | Perceived comparatively friendlier to Buyers | Perceived comparatively friendlier to Sellers |
| Better fit for: | <ul style="list-style-type: none"> - Acquisitions where there are no separate reliable accounts (e.g. a part of a business), where a thorough and robust due diligence is not possible; - Acquisitions involving pre-Completion restructuring; - Other cases that entail higher risk of Leverages or other means to impact the Equity Value; - Acquisitions of international group of companies; - Acquisitions of businesses with higher fluctuations in working capital or in the financial position, or higher exposure to external political factors; | <ul style="list-style-type: none"> - Quick and simple acquisitions of non-complex businesses; - Multi-bidder sales processes (it is easier to compare competing bids); - Acquisitions of less than 100% of the equity to form long-term joint venture with the seller |

Figure 1



The Transaction Process: We started this series of articles regarding completion mechanisms by outlining key milestones in a typical private acquisition. We intend to close the series by adding to this process backbone, as in *Figure 7*, the specifics of each completion mechanism to arrive to the full comparative picture in *Figure 8*:

(i) **NDA** – Both completion mechanisms start the same way. At the stage of the NDA is still early to decide which completion mechanism to apply.

(ii) **NBO** – The NBO is the right document to indicate the investor’s / the seller’s preferences about the completion mechanism of the transaction.

(iii) **Accounts Date for DD** – For transactions governed by the Completion Accounts Mechanism, the headline purchase price proposed by the investor is calculated as to the Accounts Date of the DD. For transactions governed by the Locked Box Accounts Mechanism, EnV and purchase price are calculated as at this date. If such a transaction is completed, the economic benefit from the Target would pass on to the investor from the Accounts Date of the DD.

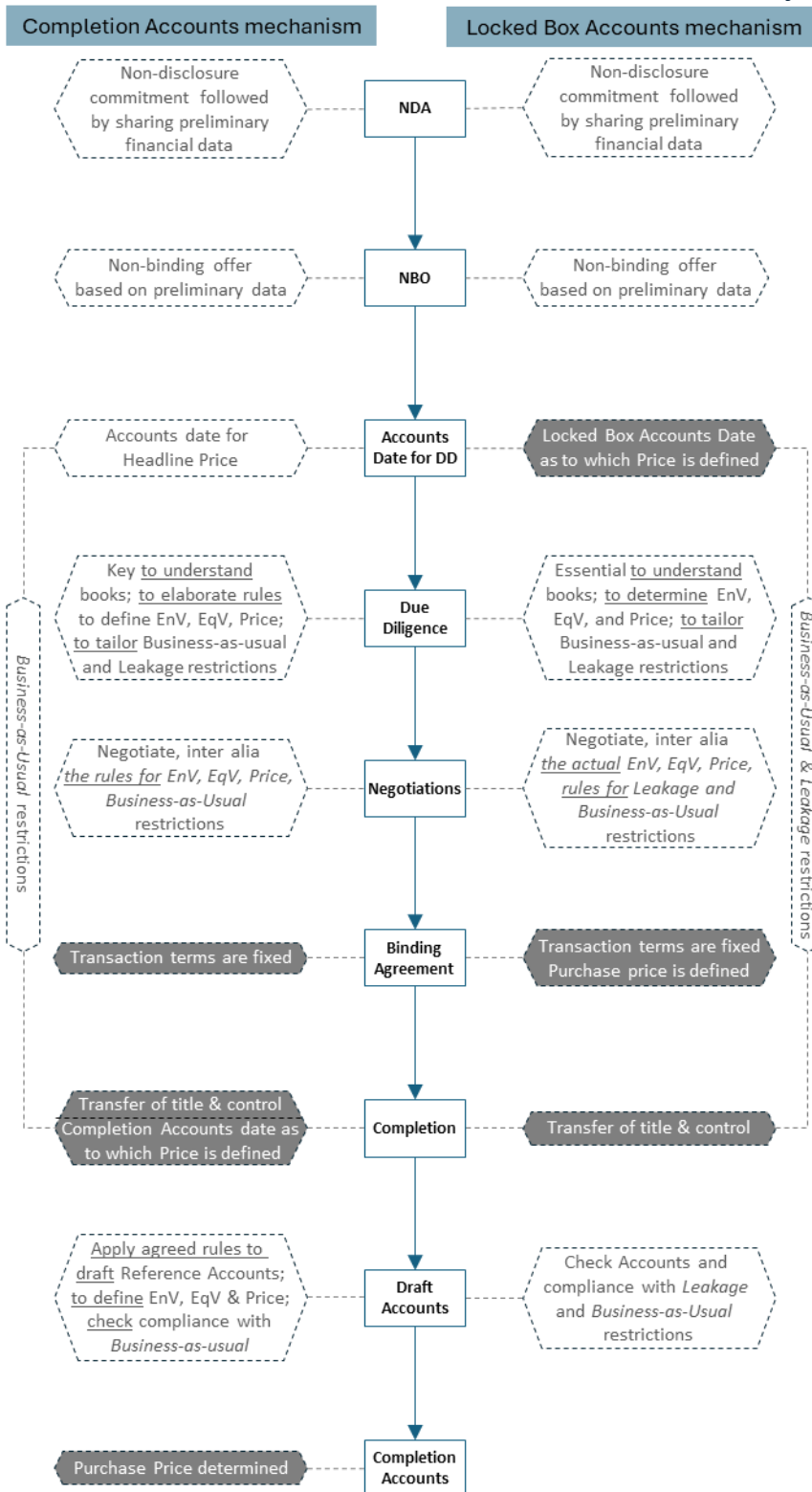
(iv) **Due Diligence** – In transactions governed by the Locked Box Accounts Mechanism, the normalized EBITDA, the EnV and the purchase price are all determined based on the due diligence results. For transactions governed by the Completion Accounts Mechanism, the due diligence results provide the basic data required to tailor the rules for adjustment of EBITDA, for calculation of EnV and for correcting it determine EqV.

(v) **Negotiations** – In transactions under Completion Accounts Mechanism, the parties negotiate the rules that have to be followed to define the final purchase price. Defining the purchase price is made based on the Completion Accounts, which will be produced after Completion. For transactions governed by the Locked Box Accounts Mechanism, negotiations are for the final EnV and final purchase price, as well as for protection from Leverages and potentially the value accrual. Most of the other terms of the transaction are also impacted one way or another by the chosen completion mechanism.

(vi) **Binding Agreement** – As mentioned earlier, the Binding Agreement fixes all terms and conditions of the transaction, commitments for the

next steps, etc. In transactions under Locked Box Accounts Mechanism, finalized are also the Target’s EnV, its purchase price and possibly the Value Accrual. For transactions governed by the Completion Accounts Mechanism, in which Target’s EnV and purchase price are still to be finalized, the parties finalize instead the rules for their determination (once Completion Accounts are in place – see below). The governing completion mechanism impacts in different level also the conditions precedent to

Figure 2



Completion, Business-as-Usual Restrictions, reps and warranties of the parties, clauses related to breach and liability, termination, governing law and jurisdiction, etc.

(vii) **Completion** – For transactions governed by the Locked Box Accounts Mechanism, the transfer of title and control over the Target to the investor occurs effective from Completion, but it also triggers the transfer of economic benefit to the investor with retroactive effect as of the Accounts Date of the DD. For transactions governed by the Completion Accounts Mechanism, both title and economic benefit from the Target pass on to the investor from Completion. Signing and Completion may occur simultaneously if there are no conditions precedent to Completion. Under Bulgarian law, the transfer of title over shares of a limited liability company requires registration into the Bulgarian Commercial Register to take effect vis-à-vis third parties acting in good faith. The registration in the Commercial Register requires several business days after signing of a share transfer agreement with notarized signatures and content. Due to this time gap, SPAs regulating transfer of shares of Bulgarian limited liability companies often define Completion as the date of registration of the share transfer with the Commercial Register, not the date of signing of the notarized share transfer agreement between the parties.

(viii) **Draft Completion Accounts** – For transactions governed by the Completion Accounts Mechanism, preparation of Draft Completion Accounts is mandatory, it is a preparation for the last step – agreement on Completion Accounts. For transactions governed by the Locked Box Accounts, the draft Completion Accounts would be the last step in the transaction process (if there is no dispute), and these accounts serve as verification for compliance with the Leakage and Business-as-Usual Restrictions and the representations and warranties of seller.

(ix) ***Completion Accounts** – Completion Accounts exist as a step only in the processes for transactions governed by Completion Accounts mechanism (if there is no dispute). By agreeing on the Completion Accounts and having in the SPA the rules for calculation of the Target’s EnV, debt, cash and working capital adjustment, the parties determine also the final purchase price for the Target.

Please reach out to us if you want to discuss!

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